Competition issues in the UK TV advertising trading mechanism

ITV plc response to Ofcom Consultation of 10 June 2011

REDACTED VERSION FOR PUBLICATION

REDACTIONS ARE MARKED BY A [✂] SYMBOL

3 August 2011

CONTENTS

EXECUTIVE SUMMARY

1. Introduction

1.1 On 10 June 2011, Ofcom published a consultation on a potential reference to the Competition Commission ("**CC**") for a full Market Investigation of the UK TV advertising trading mechanism (the "**Consultation**" or the "**Consultation Paper**").

1.2 ITV plc ("**ITV**") welcomes the opportunity to assist Ofcom in its Consultation. This paper sets out ITV's views on whether the case for reference to the CC has been met. A cross-reference table reflecting where in this paper ITV's responses to each of Ofcom's questions can be found is provided in Annex A.

1.3 In this paper, ITV shows that:

(i) There are no "reasonable grounds" for suspecting competitive harm in the TV advertising market (see further PART A); and

(ii) Even if Ofcom concludes that it does have such reasonable grounds, it should exercise its discretion and not refer the TV advertising market for an in-depth Market Investigation by the CC (see further PART B).

1.4 ITV welcomes Ofcom's views on the points raised in this paper and would be happy to discuss any of them in more detail should that be helpful to Ofcom.

2. Industry Background

2.1 In assessing whether or not there are reasonable grounds for suspecting that features of TV advertising prevent, restrict or distort effective competition, it is important that Ofcom considers TV advertising in context.

2.2 UK television is changing beyond all recognition. As David Abraham (CEO of Channel 4) noted in his 24 May 2011 speech to the Royal Television Society: *"The world in which Channel 4 operates today is dramatically different to the one I entered just over a decade ago. Today, the whole of broadcasting – as it was then – is in many ways a subset of a converged content and technology sector that dwarves it"*.[1]

2.3 The process of market change presents significant economic challenges for advertising-financed TV – hitherto a critical part of the UK's pay/public/advertising financed virtuous circle of television competition. This change is characterised by a range of key trends, including:

---

[1] http://www.guardian.co.uk/media/2011/may/24/david-abraham-rts-speech-full (David Abraham's Royal Television Society speech: full text – Speech by the Channel 4 chief executive at Bafta, 24 May 2011).

(i) Audience fragmentation: multichannel TV, the internet and gaming have vastly increased viewer choice (see for example Figure 6.1 and Section 1 of Annex C).

(ii) Declining TV advertising market (see for example Figure 17.2) – spend on advertising has decreased significantly over the last 10 years and is forecast to continue its decline.

(iii) Rise of the connected consumer (see for example paragraphs 3.22-3.25 of Annex B) - multi-screen use is already common (at least 20% in all demographics). This will rise further as connected TVs become more commonplace (estimated to account for two-thirds of TV viewing in 2020).

3. No reasonable grounds for reference

3.1 For the reasons set out below, there are no reasonable grounds for suspecting competitive harm.

<u>TV advertising cannot be viewed in isolation</u> (Section 5)

3.2 TV advertising competes with other media for its share of spend by advertisers. Advertisers and their agents are sophisticated purchasers who are free to switch how they target customers (both within broadcasting and between media) at short notice.

3.3 Within any given year, advertisers typically have a defined marketing budget which is allocated across different media. Advertisers are increasingly "media neutral" (see e.g. paragraph 5.9) and online advertising is capturing an increasing proportion of their spend. By way of illustration we refer to Chart 3.1 of the Ofcom Consultation (which shows the rapid growth of internet advertising as a proportion of total advertising spend in the UK) and paragraph 3.4 of the Ofcom Consultation (which notes that in 2010 internet advertising had the second largest share of UK advertising (26.1%) behind press advertising (27.5%) but just in front of TV advertising (26.0%)).

3.4 As regards the constraint imposed on TV by internet advertising, ITV does not agree that a clear distinction should be drawn between internet search and internet display advertising (see further paragraph 5.13). In any event, internet display advertising – which the CC has previously recognised as the closest online substitute to TV advertising – has grown significantly in recent years (see further paragraphs 5.15-5.20 and paragraphs 3.6-3.8 of Annex B) and is already a significant competitor to TV advertising. As noted by Ofcom at paragraph 3.8 of its Consultation, in 2010, TV advertising accounted for 36.4% of display advertising while internet display advertising accounted for 8.9% (i.e. a quarter of the size of TV).

3.5 The growth of internet advertising (including display advertising) is driven by global players such as Google and Facebook who are able to offer advertisers services which are simply not open to traditional national broadcasters. We note for example the recently announced global partnerships between Google and Heineken, and between Facebook and P&G.

3.6 Internet display advertising is widely expected to continue to grow strongly. Recent Enders Analysis research concluded that *"we expect the secular shift of advertising to* *the internet to continue, with growth in display outpacing that of search, driven by social media and, to a lesser extent, online video"*.[2]

3.7 Internet advertising also provides advertisers with rich data sources enabling increasingly measurable and targeted advertising and with new and innovative marketing methods (see for example paragraph 17.9, and paragraphs 4.3-4.9 of Annex B).

<u>TV advertising is highly competitive</u> (Section 6)

3.8 Even if the market is defined narrowly to comprise only UK TV advertising, the market is competitive. Recent years have been characterised by falling prices (Chart 3.12 of the Consultation shows CPTs falling by around a third over the last 10 years), new channel entry, and innovation in content and delivery methods (see paragraphs 6.4-6.6).

3.9 TV advertising is a "B-2-B" market with strong and sophisticated customers (see paragraph 0). In 2003, the top 4 media agencies accounted for approximately 35% of ITV's revenues (and ITV in turn accounted for about the same proportion of the agencies' spend). By 2010, ITV accounted for only around 20% of the top 4 agencies' spend (i.e. they have become less and less reliant on ITV) whilst the top 4 agencies – as a result of increasing consolidation – accounted for over 70% of ITV's revenues.

<u>No evidence of harm to advertisers</u> (Section 7)

3.10 The current model does not harm advertisers and Ofcom does not provide evidence to the contrary. Rather, Chart 3.12 of the Ofcom Consultation shows CPT for TV advertising falling over time. UK TV airtime prices have also fallen faster than in other comparable countries (see Figure 11.2).

3.11 Advertisers have also benefited from broadcaster innovation and investment in content which have increased viewership and in particular the number of available impacts (see e.g. Figure 11.1).

3.12 Advertisers also have the choice (and the information to make that choice an informed one) about how to buy TV airtime. In doing so, they make a commercial decision as to which of the options available to them (contract directly with broadcasters, contract through a line-by-line agency, or contract through an umbrella agency) best suits their needs (see paragraphs 7.4-7.13). There are numerous examples of agencies winning new business (see Table 7.1), advertisers switching between umbrella and line-by-line deals (see Table 7.2), and advertisers switching between direct and agency dealings with broadcasters (see paragraph 7.13).

---

[2] Enders Analysis *European internet advertising: display on top*, 15 June 2011.

<u>No evidence of harm to viewers</u> (Section 8)

3.13 ITV welcomes Ofcom's recognition of the need to take into account any potential knock-on effects a CC Market Investigation might have on the viewer side (paragraph 4.24). These are considered further in Section 8 and Annex C. ITV believes that the potential ramifications of a CC Market Investigation on the viewer side of the market should weigh heavily on Ofcom's conclusions on reference. Competition for viewers is intense with ITV (and other advertising funded broadcasters) having to compete against broadcasters (in particular Sky and BBC) who are not reliant on funding from TV advertising.

3.14 The increasing choice available to viewers (both within TV and across media) means that broadcasters have had to improve their schedule in order to retain viewers. UK broadcasters (and commercial broadcasters in particular) have continued to invest in high-quality content, including commissioning of risky new programmes and new formats (see further paragraph 3.6 of Annex C). Importantly, much of this content has been UK-originated which viewers value highly (see Section 2 of Annex C), a fact which underlines the importance and growth potential of the UK's creative industries. The UK's main commercial advertising-funded television networks spend more on original indigenous programming than their peers in all major European markets, and the UK has the highest number of indigenous channels (targeting home country audiences) of all major European markets. In addition, the arrival of intense digital competition has reduced the price of advertising on television in the UK but has also increased the cost of attracting audiences in an increasingly fragmented landscape, making each percentage point of SOCI more expensive to attract (see e.g. [✂] of Annex C).

3.15 UK broadcasters have also innovated in terms of new forms of delivery and new channels that have been enthusiastically received by customers. For example, all the main UK terrestrial broadcasters have their own Video on Demand ("**VOD**") services offering a substantial proportion of content, streamed or downloaded, free of charge. There has also been substantial innovation in platforms (e.g. YouView/Connected TV), and technology (e.g. PVRs, HD, 3D). The competitive position of advertising-funded TV broadcasters cannot be taken for granted as illustrated by the current position of commercial radio stations who now struggle to compete with the BBC (see further paragraphs 3.15-3.17 of Annex C).

3.16 These sorts of investments have delivered value to UK viewers (see further Section 5 of Annex C). We note for example that the levels of TV viewing have gone up, and that Ofcom research shows that the PSB channels – and their quality programming – are valued by viewers. Ofcom research shows that the vast majority of TV viewers are "satisfied" or "very satisfied" with TV in the UK (see Figure 8.3).

3.17 The quality of UK content is also reflected for example in the substantial investments incurred by overseas companies like Time Warner and NBC in audiovisual content production in the UK (e.g. acquisition of Shed by Time Warner, and of Carnival by NBC Universal). Relative to the size of the industry, the UK is the largest exporter of TV content (see also Figure 4.4 of Annex C) and, per capita, invests more in original content than almost any other country (see Figure 11.5). Original content investment by commercial broadcasters in the UK is higher than in all other major European markets (see paragraph 8.5). The UK also has the highest supply of indigenous channels of all major European markets (see paragraph 11.7).

No evidence of harm to consumers of advertised goods (Section 9)

3.18 The Consultation suggests that there may be a direct link between higher advertising prices (of which there is no evidence) and higher consumer prices. However, economic theory predicts that the cost of advertising can (at least indirectly) have either an upward or downward effect on the price of advertised goods. Economic theory also suggests that advertising prices may in fact have no impact at all on product prices as advertising is a sunk cost in short-run pricing decisions of firms.

The current trading model (Sections 10 and 11)

3.19 The current model for trading UK TV airtime has strengths and weaknesses. However, it can only sensibly be assessed against the counterfactual of a realistic alternative. Against that yardstick, the model works broadly well (see further Sections 10 and 11 and paragraph 14.2). In particular picking up on what appear to be Ofcom's key concerns:

(i) The current UK trading model does allow advertisers to make "meaningful comparisons" and to switch between agencies (see also paragraphs 3.21-3.23 below). Competition between media agencies for advertiser spend is intense (see paragraphs 7.4-0 and 10.18-10.19).

(ii) There is no evidence the trading model has resulted in a lack of innovation or investment (see further paragraphs 6.4-6.7 and Section 6 of Annex C).

(iii) The UK trading model entails low transaction costs for buyers as the overall contracts are agreed annually and broadcasters are responsible for optimisation. Advertisers choosing to buy through media agents further reduce their own transaction costs.

(iv) The trading model appropriately allocates risk between market participants. Broadcasters are well placed to address and mitigate the risks of delivering the audiences that advertisers value and it is the broadcasters who face the vast majority of that risk in the current system. Broadcasters understand programming investment risks and the need to attract audiences today and into the future (see Section 5 of Annex C).

(v) As regards CRR (see further paragraphs 10.32-10.34), ITV continues to believe that it is not necessary and that it has unintended adverse consequences (as acknowledged by the House of Lords Communication Committee in their report of February 2011). ITV recognises that a CC Market Investigation could present one potential opportunity for a reconsideration of CRR. However, a CC Market Investigation is not a prerequisite for a review of CRR which in the future could be undertaken separately. In any event ITV considers that CRR does not provide a sufficient justification for a prolonged CC Market Investigation, which would create serious risks for viewers and for the industry as a whole (see in particular Sections 15 and 16).

3.20 There are a number of different TV airtime trading models in other developed markets which we outline in Section 11. However, as that Section illustrates, on key metrics such as the expansion in the supply of impacts, scale of decline in the price of TV advertising, and levels of content investment and innovation, the UK system has delivered a better outcome for viewers and advertisers than models in many other developed TV markets. There can be no expectation therefore that an alternative model would improve market outcomes.

Transparency and the role of media auditors (Section 10)

3.21 Ofcom's benchmark for transparency (described at Consultation paragraph 6.15) is already being met by the UK trading model (see further paragraphs 10.20-10.31).

3.22 In particular, agencies and advertisers have at their disposal a wealth of information directly from broadcasters as well as from industry bodies such as BARB. Such information is available regularly and with limited delay vs. "real time".

3.23 Media auditors provide further transparency for advertisers (see paragraphs 10.26-10.31). Advertisers also use media auditors' reports to exert downward pricing pressure on their media agencies who in turn push for greater discounts from broadcasters. The downward effect on TV advertising prices is recognised by Ofcom at Chart 3.12 and paragraph 6.25 of the Consultation.

4. Discretion not to refer

4.1 Notwithstanding the compelling evidence to the contrary, even if Ofcom were to conclude that it does have reasonable grounds for suspecting competitive harm in the TV advertising market, it should exercise its discretion not to refer. For the following reasons, any reference would be wholly disproportionate to any adverse effects the current trading model may be perceived to be causing.

Scale of the problem (Section 13)

4.2 As above, there is no evidence of significant consumer or advertiser harm. In these circumstances, it is clear that the standards set out in the guidance on Market Investigation references (*"[Ofcom] will only make a reference when it has reasonable grounds to suspect that the adverse effects on competition of features of a market are significant"*) are not met (see further paragraphs 13.1-13.3).

No reasonable chance that remedies will be available (Section 14)

4.3 There is no reasonable likelihood that the CC would be able to impose remedies that would work better than the current trading model.

4.4 Previous experience (including MMC/CC reports) suggests that it is inherently very difficult to predict the effect of remedies in practice. Regulatory intervention creates real risks of unintended consequences, distorting normal competitive outcomes.

4.5 That is all the more so in a market which is complex and subject to transformational change (see in particular Sections 17, Annex B, Attachment 1 and Ofcom's own recognition for example at paragraphs 4.42-4.47 of the Consultation). The current trends suggest there will be substantial market change in the market for TV advertising at some point in the next 5–10 years (i.e. around the time any CC-imposed remedies would come into effect).

4.6 Any imposed solution will not be as effective as one which has been the result of market evolution.

<u>Prolonged uncertainty</u> (Section 15)

4.7 For the duration of a CC investigation (in effect for c. 4 years from the date of reference including a potential remedies phase), the advertising and viewing markets would be subject to uncertainty and distortion as industry participants seek to second guess or "game" the regulatory process.

<u>Disproportionate burden on advertiser funded broadcasters</u> (Section 16)

4.8 The burdens associated with a CC investigation would fall disproportionately on advertising-funded broadcasters (such as ITV and Channel 4) vs. their key competitors in the markets for viewers and content (in particular Sky and BBC). In other words, a CC investigation may also produce serious <u>adverse</u> consequences on competition in the markets for viewers and content (see also Section 3 of Annex C) if it hampers the ability of advertising-funded broadcasters to compete with licence-fee/subscription-funded broadcasters and creates a vicious circle of under-investment.

<u>Timing is wholly inappropriate</u> (Section 17)

4.9 The TV advertising market – and the broader advertising and media markets – are changing on a scale not seen before in audiovisual markets (see also Annex B and Attachment 1). The first digital revolution is over – multichannel digital television is in virtually all homes and internet access is now widespread. However, a second and more profound digital revolution is beginning. A combination of digitisation, high speed internet, mobile technology and the mass market launch of connected TV has created the prospect of further significant change in audiovisual and advertising markets in the UK.

4.10 Although the precise impact and timing of change is unpredictable, the direction of travel is clear: online and digital have emerged as transformative forces and will become even more important in future. For example, the roll-out of superfast broadband will take the UK to a new level of content delivery and consumption. This in turn will drive further convergence in media devices, enabling a more seamless cross-platform media experience and opening up UK living rooms to global players: Samsung and Sony have rolled out web applications on their connected TV screens; Tesco is moving into the on-demand space following its acquisition of Blinkbox; and Amazon has acquired LoveFilm, which is transitioning from a DVD rental to a connected VOD business.

4.11 Perhaps even more profoundly, Apple and Google are also rapidly expanding their presence in the TV space. Apple's iTunes store is a key player in the on-demand content space, its iPod, iPhone and iPad devices carry a number of VOD apps in the UK and internationally, and closer integration of Apple's mobile and tablet devices with its Apple TV connected set top box will increasingly bring Apple distributed content to the TV screen. Google meanwhile is seeking to build on its leading global position in online advertising, seeing content as a key source of value for the future. It has launched Google TV in the US, and is seeking to enhance the YouTube proposition through increasing investments in long form content. YouTube apps are already integrated into virtually all connected TV propositions.

4.12 Were the CC to undertake a wholesale review of the market, any solutions it might impose would, at best, take effect around the same time that the market would itself otherwise be changing. At a minimum this implies that a CC-imposed solution is likely to be out of date before it starts. More likely, it will stifle change as industry participants who would otherwise engage in market-led modifications will be looking over their shoulder at the CC. As a result, acting now creates an even greater risk of unforeseen consequences (in particular given the number of moving parts and the fact that the precise timing and impact of the various pressures for change is currently unknown). A CC investigation may stall – or even thwart entirely – what would otherwise be market-led responses to those changes.

PART A - NO REASONABLE GROUNDS FOR SUSPECTING COMPETITIVE HARM

5. The market for TV advertising cannot be viewed in isolation

5.1 Ofcom concludes (at paragraph 4.54) that the relevant market is the market for TV advertising in the UK.[3]

5.2 A market so defined is in any event competitive (see Section 6) and has not caused any competitive harm (see Sections 7, 8 and 9). The chosen market definition does not therefore change the conclusion that there are no reasonable grounds for suspecting competitive harm.

5.3 However, it is important to recognise that the sphere within which TV advertising sales takes place is changing (see further Sections 17 and Annex B) and that it is constrained by factors outside the narrow TV advertising sector. We describe below certain areas where Ofcom's analysis in the Consultation Paper has not given sufficient weight to the constraint imposed on TV advertising by other media (the internet in particular) and how the boundaries between advertising in different media are increasingly blurred:

(i) **Advertising spend decision making:** advertisers need to decide how to allocate total marketing budgets between media. As consumers move online, advertising is following (see further paragraphs 5.5-5.11);

(ii) **Online advertising:** notwithstanding previous CC conclusions, it is clear that the constraint of online advertising on TV is strong and growing (see further paragraphs 5.12-5.21);

(iii) **Internet reporting systems:** the internet offers sophisticated and targeted measurement systems. Calls for cross-media comparable data are increasing (see further paragraphs 5.22-5.26);

(iv) **Internet used for brand building <u>and</u> product information:** the internet is used for the same marketing purposes as TV (see further paragraph 5.27);

(v) **Dissimilar lists of advertisers are also consistent with substitution:** a snapshot assessment of top advertiser lists tells us little about substitution between media (see further paragraphs 5.28-5.29); and

---

[3] In considering its views on market definition, Ofcom notes that *"The aim of market definition is to establish the products and services which are subject to a competitive price constraint. It entails an analysis of the short run competitive constraints faced by suppliers of a particular product or service and provides a framework for analysing whether a particular firm has market power"* (Consultation at paragraph 4.5). Whilst ITV understands the motivation for Ofcom to adopt the traditional model for assessing market definition, we note the March 2002 *Innovation and competition policy* report prepared for the OFT by Charles River Associates, which notes in Part I, paragraph 1.2: *"Most practitioners recognise that the traditional approach to competition policy issues of defining the relevant market, assessing the existence of market power or dominance, and then considering whether a particular behaviour or merger is anti-competitive can be seriously flawed in some circumstances. These circumstances are more likely to arise in high technology markets than in more standard markets"*.

(vi) **Supply side substitution:** global digital players are quick to react to market opportunities which show some supply-side substitution already taking place (see further paragraph 5.30).

5.4 As Ofcom notes at paragraph 4.43 of its Consultation: *"there could well be important developments in relation to internet advertising which could mean that the scope for demand-side substitution will increase over time"*. This Section 5 focuses in particular on those areas where – to date – the boundaries between TV advertising and other forms of advertising have already been blurred. If these are not sufficient for Ofcom to conclude at this stage that TV and internet advertising are part of the same market, they nonetheless demonstrate how television advertising is increasingly constrained by these other forms of advertising. In Section 17 and Annex B we describe in more detail the changes which will increase the rate of switching from TV to digital media and show a clear direction of travel towards a broader market definition. Attachment 1 – a report by Oliver & Ohlbaum on the changes happening in and around TV advertising – shows a consistent picture and should be read in parallel with Annex B.

Advertising spend decision making[4]

5.5 In considering the constraint exerted on TV advertising by other media, it is important to understand the process by which advertisers (and their agencies) decide how much to spend on TV. In particular, within any given year, advertisers typically have a defined marketing budget to cover all media spend. They then allocate that budget between products/brands (if the advertiser sells multiple different products) and between media.[5]

5.6 The allocation of spend between media is a decision which reflects not only the advertiser's broader strategic objectives but also its individual campaign objectives.

5.7 By way of illustration of broader strategic objectives, we observe that both media agencies and advertisers are aligned: consumers are moving online so advertising must follow:

(i) Sir Martin Sorrell, Chief Executive of the WPP Group (the world's largest advertising company) commented in 2010: *"it's only a question of time. Because if consumers are spending 20, or 25 percent of their time online and clients are*

---

[4] Ofcom appears to recognise this decision making – which at the top level balances different advertising media against one another – at paragraph 3.24 of its Consultation.

[5] Ofcom notes at paragraph 4.50 that *"In terms of whether the relevant geographical market could be broader than the UK, we do not consider that advertising on channels broadcasting to other countries would represent a realistic substitute for advertisers seeking to address UK-based audiences. We would therefore assume that the relevant geographical market is national in scope"*. ITV accepts that, with minimal exception, advertising on non-UK broadcasters is unlikely to reach UK consumers. However, in practice, when determining how to spend their defined pot of marketing money, advertisers will also consider in which country/countries to spend that money. Broadcasters in the UK cannot therefore ignore what is happening outside the UK.

spending 12 or 13 percent of their budgets online, there's a natural gravitational pull to that 25 percent".[6]

(ii) Marc Pritchard, Global Chief Marketing Officer (CMO) of Procter & Gamble commented in 2009: *"[The internet] really is such an incredible way to connect with consumers and really have much deeper ongoing relationships with them. ... Our media strategy is pretty simple: Follow the consumer. And the consumer is becoming more and more engaged in the digital world"*.[7]

5.8 As regards individual campaign objectives, in selecting which media to buy, the decision is guided not simply by price but rather by value.[8] Such value metrics may include the perceived level of consumer engagement with a particular medium but also the ability for advertisers to determine how well their advertisements are working, both in the sense of absolute numbers of people who see them and how those people then react to the advertisement. We discuss the issues regarding available data sources for internet and TV advertising at Annex B and see that, in fact, internet advertising provides numerous sophisticated ways for advertisers to track their spend.

5.9 That advertising spend is effectively a decision as to how to split the pot – and in particular that the internet is seen as an alternative to TV – is also borne out by trends among market participants to restructure their businesses in ways which blur the traditional boundaries between digital and other media. We note for example:

(i) Historically, most large brand-owners have split their advertising departments between "brand" and "direct response" with digital managed by the "direct response" team. However, this is changing as digital emphasis and spend has been seen to have a broader transformative effect on marketing strategies. By way of example, HSBC, Vodafone and Nissan have re-structured their marketing departments to install a central Chief Marketing Officer and integrated team responsible for both brand and direct response advertising, suggesting the increased importance of brands being adequately represented in the online space. Vodafone's digital pitch in 2006 mandated that the winning digital agency would be part of a brand strategic steering group.[9]

(ii) Agencies are following suit. By way of example, in 2008 a leading UK media agency, Carat, abandoned its "channel focused" planning and buying departments and integrated its digital experts into the heart of the organisation. Digital media planning is now being replaced by "media neutral" planning.

---

[6] Sparksheet Branded Media Q&A with Sir Martin Sorrell, 5 January 2010.

[7] *Passion for digital pumps P&G's spending* (8 June 2009, http://adage.com/article/digital/passion-digital-pumps-p-g-s-spending/137134).

[8] Ofcom recognises (at paragraph 4.26) that prices for goods/services do not need to be the same for products to exercise a competitive constraint on one another.

[9] The Digital Consultancy.

Advertisers liaise with brand teams that aim to provide the media neutrality needed for modern day communication. Leading media agencies such as Mediacom, MediaEdge CIA and GroupM and many more, now also have media neutrality as their offering.[10]

(iii) Dare Digital (Leading Digital Agency), MCBD (Leading TV Agency) and Elvis (Leading Promotions Agency) merged to offer single brand solutions. This merger was driven by reducing overheads and delivering more integrated "brand" (i.e. cross-media) solutions.[11]

(iv) ITV has also restructured its sales function to ensure that traditional TV airtime trading is more aligned with online (see further paragraph 17.9).

5.10 It is important to analyse the constraint other media – and the internet in particular – exert on TV advertising in this context. It is correct that in the annual deal rounds TV companies are in effect competing for a share of each client's broadcast spend. But in terms of the money actually spent on TV, broadcasters both individually and collectively are fighting to retain spend against alternatives and in particular the growth of the internet.

5.11 Even if these other media are not – yet – close enough substitutes for Ofcom to consider them as part of the same relevant market as TV advertising, they impose an increasing constraint on the conduct of broadcasters. This is explored further below and in Annex B.

Online advertising

5.12 We describe in further detail below and in Annex B the growing constraint of online advertising. We note however at the outset three particular points which – in ITV's view – have been mischaracterised in the Consultation:

(i) It is not correct to portray internet display advertising as insignificant. As noted by Ofcom at paragraph 3.8 of its Consultation, in 2010, TV advertising accounted for 36.4% of display advertising while internet display advertising accounted for 8.9% (i.e. a quarter of the size of TV). Ofcom also notes in Chart 3.3 of the Consultation that since 2008 internet display advertising has grown more in absolute terms than internet search advertising.

(ii) It is also not correct that *"The fact that internet display advertising accounts for a much smaller proportion of total advertising expenditure than TV advertising suggests that there is little direct substitution between the two"*.[12] There is no

[10] The Digital Consultancy.

[11] The Digital Consultancy.

[12] Ofcom consultation at paragraph 4.33.

economic theory which supports the contention that an alternative product must be of equal (or even close to equal) size to be considered a substitute. The relevant concern for market definition and for the consideration of competitive constraints, is marginal substitution. The alternative does not need to be able to replicate the hypothetical monopolist in order to exercise a constraint.

(iii) At paragraph 4.34 of the Consultation, Ofcom notes that *"The internet does not yet offer the mass, broad demographic appeal of television. Whilst television is in virtually every home in the UK, internet penetration, albeit growing, was in around 74% of homes by the end of 2010…At this point in time the internet does not offer the reach and coverage that TV can although this will change over time as penetration of broadband increases"*. Although we challenge that the internet is not already mass reach (see further paragraphs 4.1-4.2 of Annex B), the second part of the quotation is important: the internet's current position is not the end of the story.

5.13 ITV does not agree that a clear distinction should be drawn between online search and online display advertising. We note in particular that suppliers of online advertising (e.g. Google) increasingly offer both forms. Moreover, the use of display advertising has to date been restricted to some extent by the available online infrastructure (in particular broadband speeds). Infrastructure and technology improvements are being rolled out and in turn are encouraging further use of display advertising online and on mobile devices (see further Section 2 of Annex B). The ways consumers use the internet (and in particular the growth of social networking sites) is also increasing the use of display advertising (see paragraphs 3.6-3.8 of Annex B).

5.14 In any event, we consider below the constraint from display internet advertising in particular and the constraint from internet advertising more generally. Annex B and Attachment 1 describe further market developments which will impose increasing constraints on TV advertising.

The constraint from display internet advertising

5.15 In its 2010 review of CRR, the CC recognised that online display advertising is the closest online substitute to TV advertising but concluded that the constraint was not sufficient to consider it a part of the same market. Even in the year or so since that conclusion was reached, the constraint has increased: technology improvements (including connected TV, increasing broadband speed and faster mobile internet connections) have driven further spend on to digital (display) media. The growth of global brands such as Google and Facebook has done likewise (see further Attachment 1 and Annex B).

5.16 As Ofcom notes at paragraph 3.8 of its Consultation, in 2010, TV advertising accounted for 36.4% of display advertising while internet display advertising accounted for 8.9% (i.e. a quarter of the size of TV)).

5.17 Enders Analysis also notes the increasing rate of growth of internet display advertising. Between 2009 and 2010, online display advertising in the UK grew by over 30% (a result of a rebound in advertising budgets and the growth of social media like Facebook). Online display advertising in the UK is forecast to continue to outpace broader online growth: between 2011 and 2012 total internet advertising is forecast to grow 12.7%, whereas internet display advertising is forecast to grow at 16.9%.[13]

5.18 Google[14] and Facebook[15] are at the forefront of this growth. With companies of this scale and global reach heavily promoting its use, the growth of online display advertising is unsurprising. Some examples of their influence are described in 4.14(iv) of Annex B – each of Google and Facebook have recently launched global partnerships with large global advertisers (Heineken and P&G respectively) which build on their online advertising offer. National broadcasters are simply unable to offer equivalent global strategic support.

5.19 The move to online is also consistent with Ofcom's Second PSB Review which noted that: *"Our comprehensive research in Phase 1 showed the importance audiences place on the continued availability of high quality, original UK content that meets public service purposes, from a range of providers. For now, linear television remains the main way of watching this content, but audiences are enthusiastically taking up the opportunities of digital media, particularly younger audiences".*[16] In determining where to allocate their marketing budgets, advertisers follow audiences; the movement, observed by Ofcom, of audiences towards digital media will therefore add momentum to the growth of internet display advertising. See also paragraphs 3.6-3.8 of Annex B.

5.20 The switch from traditional media (including TV) to online display advertising was the subject of a recent Financial Times article which said:

---

[13] Enders Analysis *European internet advertising: display on top*, 15 June 2011.

[14] Display advertising is reported to have become one of Google's fastest growing businesses; advertisers such as Ford, Kodak and Armani have embraced it. It is also reported that 99% of Google's largest US advertisers now run campaigns on the Google Display Network, which includes websites such as Rolling Stone and the Food Networks up from just a few years ago. The largest advertisers are also believed to have increased their spending on the network by 75% in the past year (Source: International Herald Tribune, 23 September 2010 p21). In this context, Google's $3.1 billion purchase of DoubleClick in April 2007 was designed to unlock a vibrant advertising business for banners, videos, and other so-called display ads. Google's display business is set to rise, from £1.56bn in 2010 to in excess of £1.87bn in 2011 (Source: Facebook set for display ad lead, FT.com, 10 May 2011, http://www.ft.com/cms/s/2/d4f537d2-7a65-11e0-af64-00144feabdc0.html.).

[15] Facebook is already the UK's largest display advertising publisher and is expected to be the world's largest online display advertising company by revenue this year, overtaking Google, with a forecast revenue of £2.12bn. Facebook is expected to extend its lead further in 2012. Due to the lure of its massive base of 500 million users (28 million in the UK alone), Facebook's advertisers are moving money away from other media providers (Source: Facebook set for display ad lead, FT.com, 10 May 2011, http://www.ft.com/cms/s/2/d4f537d2-7a65-11e0-af64-00144feabdc0.html). Mark Zuckerberg, the founder of Facebook, believes that Facebook is "almost guaranteed" to reach the one billion user mark (Source: Special Report: Facebook began as a geek's hobby. Now it's more popular than Google: Half of all those online have visited the social networking site. Soon it may become synonymous with the web itself, The Guardian, 4 January 2011, http://www.guardian.co.uk/technology/2011/jan/04/faceboook-mark-zuckerberg-google?INTCMP=SRCH).

[16] Ofcom's Second Public Service Broadcasting Review, 25 September 2008 at paragraph 1.2.

"The cost of placing ads on Facebook is rising rapidly as more big brands begin to move their television and print spending on advertising onto the world's largest social network…

"In my experience of digital advertising this is the biggest growth that we have seen since Google,' said Simon Mansell, chief executive of TBG. 'The main difference is that this is being fuelled by brand spend rather than [direct] response spend. That is an inflection point for the whole digital marketplace.…

"Over the year, we expect [Facebook advertising spending] to have grown by 80 per cent from last year,' said Jonathan Beeston, global marketing director at Efficient Frontier. Advertisers that have long held off spending more than a tiny fraction of their marketing budgets on the web are now diverting funds from traditional media, Mr Mansell said. They include food and drink advertisers such as Coca-Cola, owner of the most popular branded Facebook page with more than 32m fans, as well as retailers, entertainment groups and automotive brands…

"Demand for Facebook advertising is increasing faster than the supply of ad space on the site, as big brands' interest grows and the rate of new users joining the site slows in developed North American and western European countries, which some analysts believe are nearing saturation point".[17]

The constraint from all internet advertising

5.21 If we consider the broader advertising market we see that while TV advertising has accounted for a steady (approx. 28%) share of total advertising expenditure over the five years to 2010, internet advertising's share has more than doubled from 14.4% to 29.3%. TV companies which rely on advertising revenue are having to work harder and harder just to retain current levels of revenue in the face of advertisers increasingly moving their money online. In the longer term, Enders Analysis has forecast that UK online advertising will grow to £5.1bn by 2014 (over one third of the total UK advertising market). We expand on the above trends in Annex B.

<u>Internet reporting systems</u>

5.22 As we describe at paragraphs 4.3-4.9 of Annex B, contrary to the Ofcom suggestion at paragraph 4.35 of its Consultation that *"it is not clear to what extent advertisers and media buyers could rely on this tracking technology to plan their campaigns"* in fact the rich data sources available from the internet have been warmly welcomed by advertisers and agencies.

5.23 These data sources are often instantaneous and allow advertisers and their agents to modify campaigns to reflect the latest news from consumers. Each of these are

---

[17] *Facebook ad prices soar more than 74%*, FT 19 July 2011 (http://www.ft.com/cms/s/0/c1375fe0-b15b-11e0-9444-00144feab49a.html#axzz1SRa7yKRB).

characteristics of the online space which traditional media owners are having to tackle in order to stay competitive with their online rivals. Indeed, as the different advertising media converge, there are increasing calls for different advertising media to be measured in comparable ways. As David Abraham (CEO of Channel 4) noted in his 24 May 2011 speech to the Royal Television Society:

"One of the reasons TV advertising has held up so well in recent years is that it has a measurable and credible currency. This is testament to the excellent work of BARB and its successful evolution over recent years. We intend to ensure that our core trading currency is maintained as the Gold Standard, but alongside it we are working on major innovations that can give us additional and complementary data about our audiences, which will further strengthen our long-term position in the ad market.

"Our forecasts suggest to us that around two thirds of all TV audiovisual content viewing time (on TV, PC and mobile) will be tracked intelligently in some way by 2020 [….] Future ad sales models are unclear but two things are certain – change is likely and data is becoming more important".[18]

5.24 The forecasted increase in the availability of cross-media measurement data is borne out by the Broadcasters' Audience Research Board's ("**BARB**") recent announcement that it will be rolling out a web TV viewing meter during the second half of 2011.[19] BARB has also announced piloting a non-linear database to accommodate viewing data from non-linear sources that fall outside the core BARB service.[20] These announcements clearly demonstrate BARB's commitment to embracing new technologies and show that tracking systems are evolving alongside developing media forms to provide advertisers and media buyers with the information necessary to plan their campaigns.

5.25 WPP – the world's largest marketing group – also recently launched a new digital media and analytics tool called Xaxis which aggregates audience information across multiple online and offline channels.[21] Xaxis *"combines all of the demand-side data and technology resources of WPP and the trading leverage of the GroupM agencies into a single comprehensive resource"*. WPP's introduction of Xaxis is described as being in response to *"demand for solutions that allow advertisers to target specific audiences directly, independent of website, app or media platform"*. One Xaxis product will allow advertisers *"to precisely extend the reach of television audiences through digital media with zero waste"*.

---

[18] http://www.guardian.co.uk/media/2011/may/24/david-abraham-rts-speech-full (David Abraham's Royal Television Society speech: full text – Speech by the Channel 4 chief executive at Bafta, 24 May 2011).

[19] http://www.barb.co.uk/news/item/id/226/?source=homepage.

[20] http://www.barb.co.uk/news/item/id/221/.

[21] *GroupM launches Xaxis: ad industry's most comprehensive audience buying solution*, 27 June 2011 (2011http://www.wpp.com/wpp/press/press/default.htm?guid={18112332-684f-4027-8feb-ff465bba398f}).

5.26 Google is also in discussions to launch a cross-media (TV, internet and mobile) panel in the UK by mid 2012. The panel will work in a similar way to the current BARB panel although will (at least initially) provide less detail on TV viewing than BARB does currently. The panel will be formed of 3,000 homes who will have their TV viewing and their internet usage (on PCs, laptops, tablets and mobiles) tracked and monitored in a comparable way. The data processing will be operated by Google who will also own the data (although longer term, Google plans to hand over the panel for industry to run). The technical solutions for the data collection from the panel are not yet all in place but Google is working actively (in some cases with third parties) to develop the technology.

Internet used for brand building AND product information

5.27 It is implied at paragraph 4.38 of the Ofcom Consultation that the internet has been used largely for product information advertising rather than for brand building with TV retaining its stronghold over the latter function. This is not correct – see for example the online campaigns of *Old Spice*, *Marmite*, *Burger King Whopper*, and *KitKat* described at paragraph 4.13 of Annex B.

Dissimilar lists of advertisers is also consistent with substitution

5.28 At paragraph 4.39 of its Consultation, Ofcom analyses the lists of top 20 internet and top 20 TV advertisers in February 2011 and concludes – because there is little correlation between the two lists – that they evidence the two being complementary rather than substitutes. This sort of static snapshot comparison of advertiser lists does not however provide support for that conclusion.

5.29 Not only are there in fact six advertisers which appear on both lists but even if the lists were entirely different it would also be consistent with substitution between the two media formats. At the extreme, two distinct lists (not limited to the “top 20”) would imply that each customer has made a binary choice between the two.

Supply-side substitution

5.30 Ofcom is quick to dismiss the notion of supply-side substitution to suggest a broader market (paragraph 4.41). However, it is important to remember that traditional broadcasters are increasingly facing competition from global digital companies who are quick to react to market opportunities. For example (see further paragraph 17.7):

(i) Samsung and Sony have launched web applications on their connected screens;

(ii) Amazon recently acquired LoveFilm which will offer connected VOD;

(iii) Google (previously a search advertising provider) has expanded its display advertising offer (see e.g. footnote 14). Google also recently launched a new social network (Google+) which already has some 10 million users and is predicted to grow quickly.[22] Although it does not yet carry advertising, it certainly has the potential to follow Facebook (see e.g. paragraph 5.20) in the use of social networking sites for display advertising; and

(iv) Apple's and Google's rapid expansion in the TV space.

6. The TV advertising market is highly competitive

6.1 Even if the market is defined as UK television advertising, there are no reasonable grounds for suspecting harm. Rather, the television advertising market is highly competitive at every level of the supply chain. We consider further below (see Section 10) individual aspects of the current trading model but at the outset note a number of points which – in addition to the constraint exerted by other media – illustrate the broader competitiveness of the market.

Falling prices

6.2 As Ofcom notes at Chart 3.12 of its Consultation, TV advertising prices have fallen in recent years. This is consistent with a competitive market environment.

6.3 Although it is not possible to state accurately what the right counterfactual should be (i.e. whether prices have fallen as far as they would have done under an alternative model), a reasonable proxy should at least be the position in other markets. We note that the prices in the UK have fallen faster than in comparable countries (see further paragraph 11.6) and that ITV's profit margins are lower than most similar broadcasters in other countries (see paragraph 11.10).

Significant new entry

6.4 The trading model has not prevented entry of new channels – between 1998 and 2008 the total number of channels in the UK rose from 52 to 257.[23] While the years since 2008 have witnessed a slight fall-off in the number of channels (down to 240 in 2010), this has largely been the consequence of adverse conditions in the advertising industry more generally: *"most of the media industry has been in crisis mode since the global recession took hold in late 2008"*.[24]

---

[22] *Google finally takes on Facebook by invitation only*, 13 July 2011, The Times.

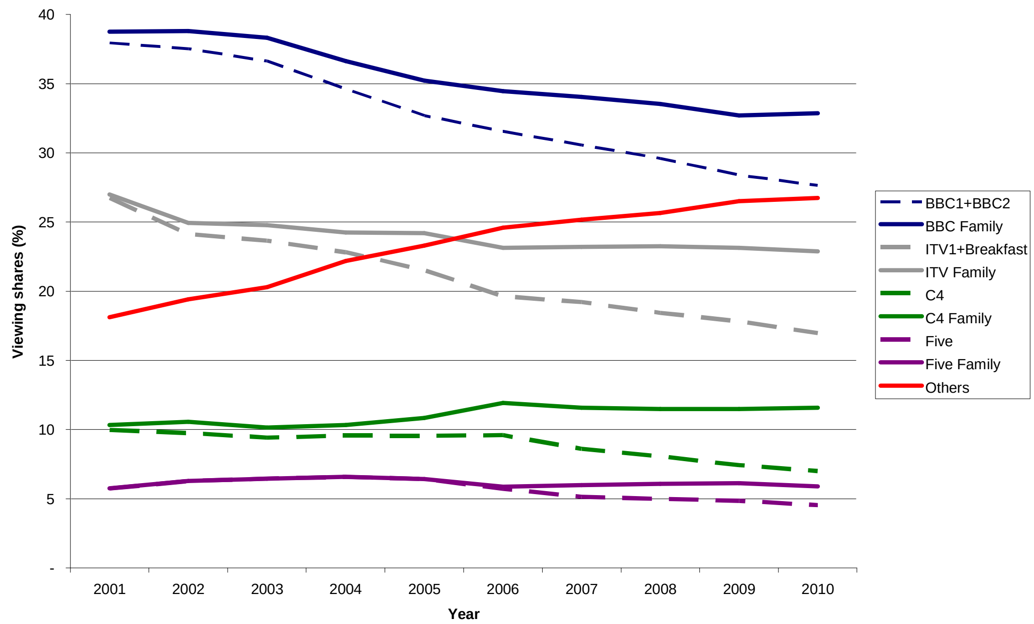
[23] Channels reported by the BARB as at the last week of December for each year. Interactive channels and regional variations are excluded.

[24] ZenithOptimedia, UK Media Yearbook 2010 (September 2010), p. 1.

6.5 The resulting "key difference" between the present landscape and that which prevailed in 2003 is, as Ofcom notes, *"that all five main PSB channels have shown a decline in their respective audience shares"*.[25]

6.6 Ofcom notes that much of that decline has been offset by gains within PSB "channel families". In response, we note first that the broader point – that channel entry is possible – still holds. Moreover, the rise of channel families also serves to demonstrate that incumbents have needed to innovate in order to maintain share. This is consistent with a highly competitive market. In any event, the broader picture (see Figure 6.1) is that non-PSB family channels have grown at the expense of PSBs.[26]

Figure 6.1:
PSB channel and PSB channel family viewing shares over time



Source: *BARB.*

6.7 That PSB channels have had to innovate to retain consumers is also reflected for example in their offer of video on demand and catch-up.[27] The growth of these types of services is noted by Ofcom at paragraphs 3.65-3.68. Ofcom goes on to say that *"at*

---

[25] Ofcom consultation at paragraph 3.43.

[26] That the PSB channels have been better able to retain their share of NAR does not imply that the market is uncompetitive but rather that advertisers place value on those channels.

[27] By way of illustration: *"BBC Online now comes behind only BBC1 and BBC2 in terms of reach, being used by nearly 20m adults a week…iPlayer continued its remarkable growth , with 1.6bn programmes played during the year"*, 12 July 2011, *The BBC must be a beacon for quality and standards: Lord Patten publishes BBC Annual Report and Accounts for 2010/2011* (http://www.bbc.co.uk/bbctrust/news/press_releases/july/annual_report.shtml).

present it is not clear that these alternative types of advertising are likely to overtake the current model". The test should not be whether or not the alternatives will overtake the current model, but rather the extent to which they will force or at least encourage change. Moreover, it is too simplistic to consider each element of change individually – the effects on the market will come from many sides (see e.g. Annex B and Attachment 1) such that they should be considered in aggregate.

Countervailing buyer power

Negotiating rounds between broadcasters and media agencies are hard-fought – media agencies have significant and growing countervailing power. This is largely a result of increasing concentration at the media agency level (see Ofcom Consultation at Table 5.1) and the pressure the media agencies are themselves under from their customers (see e.g. Consultation at paragraph 6.25 and paragraphs 7.4-7.13 below). [✂]

[✂]

ITV market strength

6.8 Although ITV does not agree with the CC's conclusions in 2010 that competitive concerns remain as regards ITV1's market position, these are in any event addressed by the contracts rights renewal ("**CRR**") undertakings which continue to dictate the terms of sale of ITV1 (including ITV1+1 and ITV1HD) airtime (see further paragraph 10.32-10.34 re: CRR).

6.9 Ofcom also refers to ITV's market strength (Consultation at paragraph 5.58-5.63) and refers in particular to the number of the top 1000 programmes for all Adults which were shown on ITV, Channel 4 and Five. Before placing any reliance on these figures, it is important to understand how they are calculated. In particular, each episode of a particular programme is counted separately. This means, for example, that each episode of Coronation Street (three episodes per week plus Sunday omnibus) is counted separately. However, from a TV advertising perspective this is not a sensible way of counting top programmes: advertisers do not want their adverts shown repeatedly in the same programme as this approach is unlikely to generate unique viewers (see further paragraph 10.17 regarding the controls advertisers include within their purchasing contracts which prevent this). If we instead calculate the top 1000 unique programmes, the results are rather different (see Table 6.1). While Ofcom's figures suggest that ITV has 99% of the top 1000 programmes, in fact its share of the top 1000 unique programmes is around 40%.

Table 6.1:
Top 1000 unique programmes for Adults on commercial channels

	ITV1	Channel 4	Five	Other
2003	446	304	239	11
2004	409	324	261	6
2005	410	336	243	11
2006	395	356	231	18
2007	411	351	206	32
2008	446	326	193	35
2009	422	316	209	53
2010	398	347	202	53

Source: *BARB.*

6.10 Similarly, as Ofcom observes at paragraph 6.46, the fact that ITV's "power ratio" is above 100, does not necessarily imply market power.

6.11 As regards the "power ratios" more generally, it is important to note that an increase in the power ratios does not necessarily indicate an improvement in profitability or "market power". To the extent that they do reveal differential willingness to pay for impacts on particular channels, this is likely to be related to the investments that broadcasters have made in content on these channels and the success of the broadcaster in attracting audiences that are of value to the advertisers. In the case of ITV1, its programming spend for each percentage point of adult SOCI has increased almost threefold in real terms between 1995 and 2010 (see further [✂] of Annex C).

7. No evidence of harm to advertisers

7.1 As we show below, there is no evidence – and Ofcom does not provide any – that the current model is harming advertisers. On the contrary, Chart 3.12 of the Ofcom Consultation shows CPT for TV advertising falling over time (see also paragraphs 6.2-6.3 above). Advertisers have also benefited from an increased number of channels, increased numbers of viewers, and innovation in terms of format delivery (see further Section 6).

7.2 Advertisers also benefit from the current levels of programming investment. By way of example we note the following comment made by Proctor & Gamble when giving evidence to the House of Lords Select Committee: *"we are not interested in beating ITV up. We are interested in a strong ITV delivering lots of audience, rich in the sort of people that we want to hit with our advertising. They are in a very particular position to deliver that"*.

7.3 Moreover, there is no harm to advertisers resulting from their relationship with agencies – competition among agencies for advertisers' business is intense.

<u>Advertisers switch between agencies</u>

7.4 At paragraph 6.58 of its Consultation, Ofcom states that *"the ability of advertisers to switch between media buyers is limited by the nature of their deals with the media buyers. That is, 3-4 year deals between advertisers and media buyers mean that advertisers only have the opportunity to make comparisons of the contractual terms they are being offered by media buying every few years and this would limit their ability to switch advertising expenditure between media buyers"*.

7.5 Ofcom is right that *"the advertiser's ability to switch at the end of a contract [imposes] a certain discipline"*[28] on media buyers. But that does not tell the whole story as, in practice, advertisers can and frequently do switch between media agencies.

7.6 In particular, it is ITV's understanding that the average term of contracts between media agencies and advertisers is relatively short (c. 3 years) and decreasing over time.[29] Break clauses are common and there are often few contractual remedies available to an agency in the event that an advertiser switches mid-contract. It is also increasingly common for advertisers (particularly the larger accounts) to impose absolute price guarantees on their agencies and/or performance-related fee/termination mechanisms (see paragraph 10.31(i)).

7.7 Furthermore, advertisers' ability to make comparisons of the contractual terms they are being offered by media buyers is facilitated by the fact that advertisers often retain auditors (see further paragraphs 10.26-10.31) and that they typically retain an agency *"for only a portion of its advertising…or only in particular geographic areas, thus enabling the client continually to compare the effectiveness"*[30] of one agency against the others.

7.8 Advertisers will invite several media agencies to pitch for existing accounts and agencies often win accounts from their competitors. For example:

(i) In 2009, 118 118 switched from incumbent agencies OMD UK and BLM Quantum to ZenithOptimedia following a pitch that also reportedly included Mediaedge:cia, Maxus, Mindshare, MediaCom and Starcom.[31]

(ii) In 2010, PHD won the £50m consolidated Kraft/Cadbury UK media planning and buying account following a head-to-head contest against Starcom MediaVest Group. Starcom was the incumbent on the £25m Kraft account and PHD was the incumbent on the £25m Cadbury account. Starcom had held the

---

[28] Ofcom Consultation at paragraph 6.65.

[29] By way of example, Santander is understood to review its contracts every two years.

[30] Source: WPP Prospectus dated 14 May 2009 http://www.rns-pdf.londonstockexchange.com/rns/2744S_-2009-5-14.pdf

[31] Source: http://www.bdrecruitment.com/news/news-article.php?id=395

Kraft account since 2004, when it captured the business in a pitch against Mindshare.[32]

(iii) In 2010, Experian awarded the media planning and buying business for its CreditExpert brand (estimated value of £8m) to Maxus. The incumbent was Media Campaign Services.[33]

(iv) In 2011, Arena Media won the £6.5m media account for Eurostar, previously held by Vizeum following a tender process which also included Walker, UM, Rocket and Maxus.[34]

7.9 By way of further illustration, Table 7.1 shows the latest advertisers "won" by each of the top media agencies.[35]

[32] Source: http://www.brandrepublic.com/news/1004439/PHD-wins-50m-Kraft-Cadbury-media/

[33] Source: http://www.mediaweek.co.uk/news/986488/Maxus-wins-8m-Experian-media-account/

[34] Source: http://www.brandrepublic.com/news/article/1074774/arena-media-wins-65m-eurostar-business/

[35] Note: some of the agencies may be part of the same buying group.

Table 7.1:
Recent advertiser “wins” by top media agencies Jan-Dec 2010

Agency	Total billings gained (£m)	Total billings lost (£m)	Net billings gained (£m)	Wins	Recent wins		
M4C	204	–	204	1	COI		
Maxus	78.5	2	76.5	4	Andalucia Tourism	Air Asia	CreditExpert
ZenithOptimedia	66.8	4	62.8	3	Gucci	The Perfume Shop	Aviva
Vizeum	43.8	1.2	42.6	4	Wyeth	Credit Confidential	Zoopla
PHD	37.1	–	37.1	7	Dyson	Viagogo	Kraft
MEC	33	2.5	30.5	8	Shearings	Orange (digital)	Specsavers (digital)
Universal McCann	18.3	–	18.3	6	Tempur	Marie Curie	Ecco Shoe
Mindshare	13.2	–	13.2	4	Mango	ITV Studios	Piaggio
MediaCom	15	3.9	11.1	1	Sky (online)		
Arena Media	11	–	11	2	ESPN	Red Driving School	
Eden	9	–	9	1	Phones4u		
Total Media	8.6	–	8.6	6	Fred Olsen Cruises	Geosweep	The Private Clinic
Twenty Twenty Media Vision	8	–	8	1	Carpetright		
John Ayling & Associates	7.9	–	7.9	4	Prudential	Milk Marketing	Save The Children
Walker Media	12.8	6	6.8	7	Network Rail	Olympic Dev't Authority	Visit Kent
Manning Gottlieb OMD	5	–	5	1	Bathstore		
The7stars	4	–	4	3	Robert Dyas	Discovery Networks	Allied Carpets
Principles Media	1.5	–	1.5	1	Ultralase		
Initiative	1	–	1	1	Greener Journeys		
MPG	5	4.1	0.9	5	Austrian Tourist Board	EBLEX	NBC Universal

Source: Campaign (http://www.campaignlive.co.uk/news/wide/1049461/).

Advertisers switch between types of agency contracts

Advertisers are also able to choose between “umbrella” and “line-by-line” deals with media agencies. Examples of advertisers who ITV are aware of having switched between these types of contracts in the last two years are shown in [✂].

[✂]

7.10 In other words, if there are features of umbrella deals which an advertiser does not like, it is free to switch to a line-by line deal (or *vice versa*). This may entail the loss of certain benefits associated with either type of deal (e.g. taking advantage of the buying power of an agency under an umbrella deal vs. the relative transparency on discounts of a line-by-line deal) – selecting which to choose is a commercial decision for the advertiser in question according to its own priorities.

Open to advertisers to contract direct

It is also open to advertisers to avoid agencies altogether and contract directly with media owners if they prefer. In practice, many advertisers prefer to contract via an agency to benefit from that agency’s economies of scale and to avoid the costs (particularly in the form of additional personnel) needed to conduct media buying. Certain larger advertisers have nonetheless chosen to buy TV airtime directly [✂] or to use agencies only to perform the mechanical parts of airtime booking whilst retaining responsibility for deal negotiation in-house [✂]. Others could choose to do the same were they to consider it economically advantageous.

[✂]

8. No evidence of harm to consumers – as viewers

8.1 As Ofcom acknowledges, it is important to consider the viewer dimension in any evaluation of TV advertising. The television advertising market is a two-sided market, with significant linkages between advertising and investment in original content. Any consideration of the functioning of the trading model needs to pay close attention to the implications for consumer welfare of potential adjustments to the model.[36] Ultimately, it must be borne in mind that consumer and viewer interest is about much more than the price of television advertisements.

8.2 Competition for viewers is intense. As *Creative UK*[37] reports: "*Competition in the form of battle between channels for viewing shares between platforms and (in the commercial sector) for revenues is intense*". See also Section 1 of Annex C on the competitiveness of the viewer market – the range of home entertainment options has risen exponentially in recent years.

8.3 Broadcasters are in the business of attracting viewers. Viewers want high quality UK-originated content (see Section 2 of Annex C – over 80% of Ofcom survey respondents agreed or strongly agreed that it is important that the main TV channel provide UK-made programmes that reflect life in the UK). It is therefore in the interests of broadcasters to invest in such content.

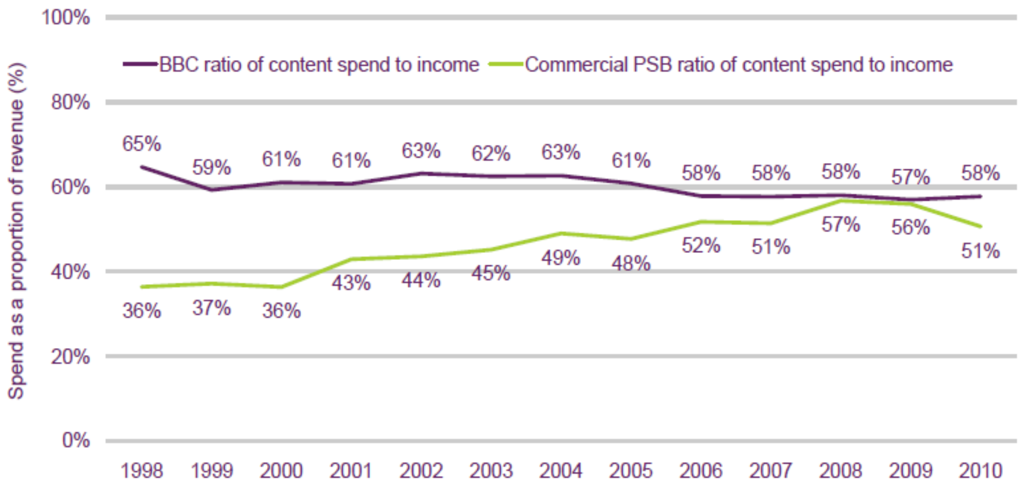
8.4 The competition between platforms for programming rights is therefore also intense and the UK is a leading generator of content and formats (see Sections 3 and 4 of Annex C). The intensity of this competition is illustrated for example in the level of originated content spend of the commercial PSB channels (see paragraphs 3.5-3.6 of Annex C) which are of a similar level to the licence fee funded BBC. Figure 8.1 shows also how commercial PSBs have significantly increased their ratio of spend on first run originated programming to revenue to a similar level to that of the non-profit making BBC.

---

[36] See also Section 6 of Annex C – the current trading model does provide broadcasters with a strong incentive to invest in programming. This is in turn reflected in high levels of original content and consumer satisfaction.

[37] *Creative UK* is the April 2011 report prepared by the Communications Chambers.

Figure 8.1:
PSB First run origination programming spend – ratio of spend to revenue



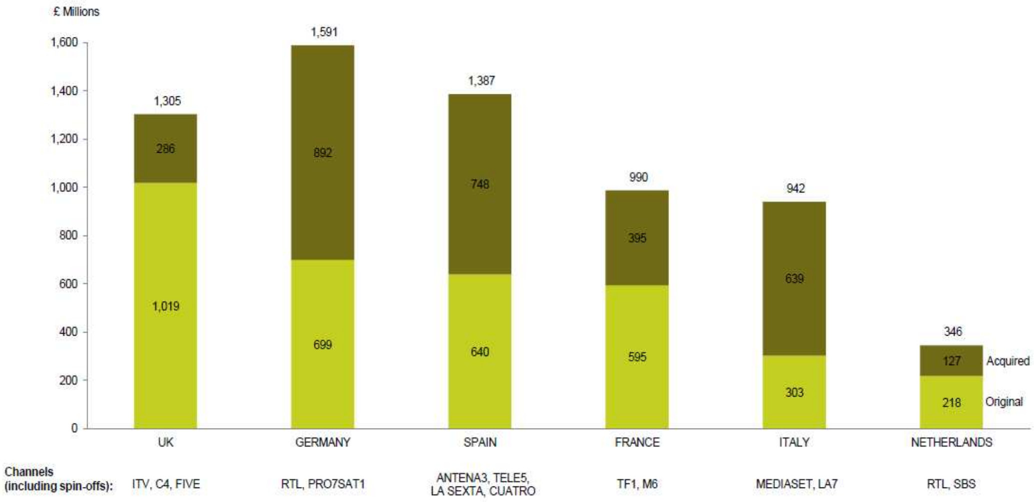
Source: *Broadcasters and Ofcom estimates drawing on data from the BBC's Annual Reports and Accounts.*

Notes: [1] Spend is all day, all genres. It includes all spending on networked output by the BBC, ITV1, Channel 4 and Five. It also includes BBC, stv, ITV1 and UTV spending on programmes for viewers in the nations and regions and the BBC's spend on programmes for S4C and BBC Alba.

[2] BBC income is based on Ofcom estimates of total licence fee revenue that is spent on TV-related services which include content, distribution, and infrastructure spending, and a proportionate share of remaining overheads.

8.5 This level of investment in original content by commercial broadcasters is not a feature of all markets. Figure 8.2 shows that the UK's main commercial advertising funded network groups spend more on original indigenous programmes than their peers in all major European markets.

Figure 8.2:
Leading TV originated content markets by commercial broadcaster, 2009

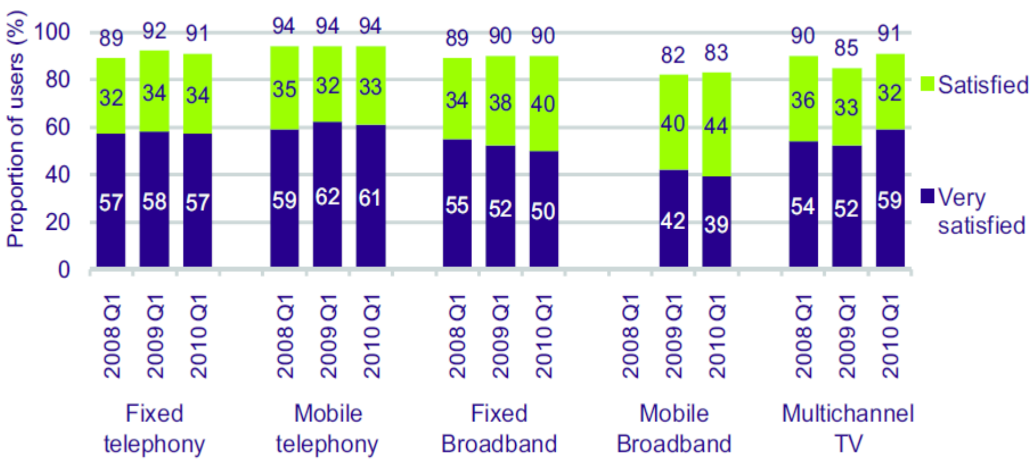


Source: *OBS, SNL Kagan, Company report, Oliver & Ohlbaum analysis.*

Note: Data exclude spend on news and syndicated programming.

8.6 This competitive situation means that viewers are well served currently. The existing trading model has resulted in creative, diverse and high-quality television programmes. By way of illustration, Figure 8.3 shows that the vast majority of TV viewers are "satisfied" or "very satisfied" with multi-channel TV. (See also paragraphs 11.7-11.9 which show that the UK fares well in terms of originated content spend compared to international markets.)

Figure 8.3:
Overall satisfaction with communication services Q1 2008-Q1 2010



Source: *Ofcom research.*

Note: Includes only those who expressed an opinion. Base: those with multichannel TV 2010 n=8121; 2009 n=5318.

8.7 Any changes to the model which damage – or even threaten to damage – broadcasters' advertising revenues will be likely to have detrimental knock-on consequences for investment in originated content particularly given that advertising-funded broadcasters already face higher content costs and lower revenues (see Figure 5.1 of Annex C).

8.8 A Market Investigation into TV advertising will also have a disproportionate effect on certain players in the markets for viewers and content (namely ITV and Channel 4 and Five) than on others who do not rely on advertising revenues to the same extent (BBC and Sky) (see further Section 16) and may have the effect of a downward spiral in terms of content investment and innovation (see Section 3 of Annex C).

9. No evidence of harm to consumers – as purchasers of advertised goods

9.1 Ofcom appears to assume (Consultation at paragraph 1.6 and 6.89) that the cost of TV advertising airtime will have a direct relationship with consumer prices. In fact, there is no firm evidence that there is any direct relationship between the costs of advertising and consumer prices. As outlined below, economic theory predicts that changes in the cost of TV advertising may indirectly affect the prices of consumer goods either positively or negatively (e.g. by affecting consumers' willingness-to-pay for the advertised products or by affecting the cost of information acquisition regarding the advertised products).

Advertising as a sunk cost

9.2 In the academic economic literature, advertising is often characterised as a sunk cost (i.e. a fixed cost of production which cannot be recovered once it has been incurred).[38] Microeconomic theory suggests that firms do not take account of sunk costs in short-run pricing decisions. Rather, those pricing decisions are based on ensuring that sales prices are greater than marginal costs (as this allows the firm to remain in business and make a positive contribution to profit) and that the mark-up over marginal costs reflects prevailing market demand characteristics. On this basis, changes in advertising prices will not change the price at which firms are willing to supply their goods or services, or the quantity they are willing to supply in the short-run. A change in the relative price of TV advertising will, however, change the amount of advertising which firms purchase, within the same total advertising budget.

The impact of advertising on product prices

9.3 Advertising features in a range of economic models that examine the effect of advertising on product market structure, prices and competition. These models do not provide an unambiguous prediction on the existence (or magnitude) of any effect that advertising costs have on consumer prices.

---

[38] See for example Sutton, J, (1991), *Sunk Costs and Market Structure*, MIT Press. Sutton distinguishes "exogenous sunk costs" which are necessarily incurred by all firms in order to compete in the market (e.g. advertising which is necessary to inform the consumer of the product's existence), and "endogenous sunk costs" which increase consumers' willingness to pay for a firm's product/service.

9.4 For example, applying the characterisation of persuasive vs. informative advertising:[39]

(i) Persuasive advertising may (indirectly) lead to higher prices if it increases perceived product differentiation (and therefore consumers' willingness to pay) and allows firms to charge a higher price for their products.

(ii) Conversely, informative advertising (especially when it is focused on product prices) tends (indirectly) to result in lower product prices by providing information on price and non-price product characteristics of the product, which enhance market competition.[40]

9.5 Higher TV advertising prices (which result in firms advertising less) could lead to lower product prices by reducing perceived product differentiation in the former case, but higher product prices as a result of reduced competition in the latter. Identification of which effect dominates is ultimately an empirical question.

<u>Advertising as a barrier to entry</u>

9.6 Advertising can arguably be a barrier to entry if increased advertising expenditure leads to increased industry concentration and higher prices.[41] A number of academic papers have explored additional mechanisms through which this effect could arise, for example in examining how advertising could be used by incumbent firms to deter entry into product markets. However, advertising expenditure would only be a barrier to entry if larger firms have better access to capital to finance their advertising campaigns, or if incumbent firms enjoy a "first mover advantage" as a result of having already established a strong brand image. It appears unlikely that an increase in the price of TV advertising (given the deflation observed over recent years in the cost of TV advertising – see Chart 3.12 of the Consultation) could have any significant impact on industry structure or the strength of entry barriers present.

9.7 While an increase in the price of TV advertising could increase the fixed costs of entering product markets, this effect is unlikely to be significant in practice as an increase in the price of TV advertising is likely to induce advertisers to alter their media mix by shifting their marketing budgets away from TV advertising towards other media. Further, even if there were a significant increase in advertising expenditure, this is only a proportion of the total marketing budget (which would also include the costs of creative agencies, auditors and commission paid to buyers and planners). In turn, marketing is itself only a proportion of a firm's fixed costs, and is therefore unlikely to change fixed costs by such a significant degree to affect outcomes in product markets.

---

[39] Informative advertising conveys information to consumers on the availability, price and other characteristics of goods. Persuasive advertising seeks to alter consumers' tastes or preferences. Advertisers generally use a combination of these two types of advertising to increase sales of their products.

[40] Stigler G. J. (1961), *The Economics of Information*, Journal of Political Economy, 69, pp. 213-225.

[41] Kaldor, N. V. (1950), *The Economic Aspects of Advertising*, Review of Economic Studies, pp. 18, 1-27.

10. The current trading model

10.1 The current trading model is not broken. ITV accepts that it possesses a number of idiosyncrasies but the fact is that the model has broadly worked well, and continues to do so, for the majority of industry participants. In its latest UK Media Yearbook, ZenithOptimedia appends the following comment to its overview of the UK television advertising trading model:

"*This must all seem dangerously vague to the curious bystander. It does indeed tend to leave a bit of tidying-up when a campaign is over, when the predicted variables of impacts and revenue are finally known. An advertiser may find he has to pay more than he expected to the TV company, or perhaps the TV company owes him viewers, for instance. But such differences are minimal in well-managed campaigns, and the market actually works quite smoothly*".[42]

10.2 In assessing whether the current trading model causes harm, it cannot be assessed in isolation. Rather, it must be assessed against realistic alternatives (in particular as adopted in other markets). As we show in this Section 10 and in Section 11, against that yardstick, the model works well.

10.3 We consider below particular features of the current trading model:[43]

(i) Share of broadcast ("**SOB**") mechanism;

(ii) Station average price ("**SAP**");

(iii) Bundling;

(iv) Umbrella deals;

(v) Transparency; and

(vi) CRR.

10.4 The following sections explain why (notwithstanding some idiosyncrasies) there are no reasonable grounds to suspect that the current trading model prevents, restricts or distorts competition. Moreover, the current trading model allocates risk in an efficient way (see paragraph 10.34-10.49) such that any perceived adverse effects are outweighed by the efficiencies it generates. These efficiencies also explain the relative stability of the current model. Ofcom observes at paragraph 1.13 of its Consultation that *"it could also be the case that the trading model has not evolved because the current*

---

[42] UK Media Yearbook 2010, p. 37.

[43] ITV broadly agrees with Ofcom's overview of the way TV advertising is traded. It is however important not to lose sight of the efficiencies generated by that system (see further paragraphs 10.5-10.31) and of the fact that alternative models may not represent an improvement (see further Section 11 and paragraphs 14.2-14.3).

airtime trading system was already reasonably efficient, delivered what advertisers want and is sufficiently flexible to accommodate changes going forward". We show below that this is indeed the case.

SOB mechanism

10.5 The vast majority of contracts between media buyers and broadcasters specify a SOB commitment from a media buyer in exchange for a discount off the price of airtime and access to advertising at particular times of day or particular programme breaks. The SOB commitment and associated discounts are the key focus of the annual deal round. The SOB mechanism also underpins the operation of CRR.[44]

10.6 The SOB mechanism is functioning well for the television advertising market, for the following key reasons:

(i) It does not induce undue loyalty towards broadcasters as media agencies are increasingly in a position of power during SOB negotiations (see paragraph 0). This is especially the case given the high number of television channels now available to agencies (see paragraph 6.4) and the growing constraint from, in particular, online advertising (see paragraphs 5.12-5.20).

(ii) The SOB mechanism allows agencies and their advertiser clients to flex spend, at any point in time e.g. to reflect changes in the financial climate or industry conditions. This means that agencies and advertisers are able to manage their risk. Under the current SOB mechanism it is the broadcasters who bear all the revenue risk, since it is not known what a commitment to a certain SOB equates to in financial terms. If the negotiation round were to focus instead on monetary amounts, the system (advertisers and agencies in particular) would lose a significant degree of flexibility (see also paragraph 14.2(i)).

(iii) The SOB mechanism facilitates switching of agencies by advertisers – under the current trading model, advertisers easily can and frequently do switch media agencies in order to take advantage of the best available deals (see paragraphs 7.3-7.13). Competition between the agencies to "poach" clients is fierce – the SOB mechanism enables agencies to flex their spend and to pass on their discount to attract clients.

(iv) The market is transparent (see further paragraphs 10.20-10.31) and the SOB mechanism does not restrict that transparency.

(v) [✂]

[44] The existence of CRR does not prevent alternatives – if the market were to prefer a trading mechanism which does not fit within the current CRR framework, CRR would not prevent that switch from occurring. Rather, CRR would simply become increasingly less relevant and eventually obsolete.

(vi) Market participants are familiar with the SOB mechanism – any change would bring additional costs and uncertainty.

SAP

10.7 SAP is a notional benchmark price. A key feature of SAP is that it is calculated at the end of each month, i.e. SAP varies on a monthly basis depending on the impacts delivered by the channel against each demographic and the amount of overall revenue received by the sales house from media buyers.

10.8 Prior to the adoption of SAP, television advertising was sold according to a pre-emptive system. This was unpopular with media agencies and advertisers, because of the uncertainty when a campaign was booked over the number of impacts that would be generated or if the advertising spots would be transmitted. In addition, they had no real benchmark for their buying performance. The pre-emptive system was also very labour-intensive. SAP developed over time as a market-led response to the inefficiencies of the pre-emption model and a reflection of two readily available (see paragraphs 10.23-10.25) pieces of information: revenue and audience.[45]

10.9 SAP is an important and appropriate element of the current trading model, for the following key reasons:

(i) SAP functions as an efficient clearing mechanism in circumstances where both demand and supply are unknown at the time of deal negotiation. SAP operates in such a way that no broadcaster is undersold or oversold, and media agencies can always obtain airtime when required. It allows the market to adapt to revenue and/or audience fluctuations.

(ii) Market participants understand and acknowledge the utility of the SAP mechanism – SAP is accepted by industry participants as a *"useful market indicator",* given that *"it is impractical for a television company to predetermine a single price at which all its spots will be sold, regardless of demand"*.[46] Any change would bring additional costs and uncertainty.

(iii) Any opacity in the market is the result of inherent features of any airtime trading mechanism (in particular that the volume of viewers is not known in advance), not the SAP mechanism. Rather, the SAP mechanism aids transparency, in that it is based on data available to buyers (audience and revenue figures). SAP also provides transparency vis-à-vis an agent's/advertiser's relative position (in contrast to a spot market where there is broad scope for inflating

---

[45] Ofcom's belief (Consultation at paragraph 5.66) that the evolution to the current ex-post SAP-based pricing system reflected a desire to reduce transaction costs and a management of risks on both the sales house and buyer sides is broadly right. It is also a reasonable conclusion reached at paragraph 5.67 that *" the move to trading impacts may have been at least in part driven by advertiser desire for greater certainty about achieving campaign goals"*.

[46] ZenithOptimedia, UK Media Yearbook 2010, p. 35.

ratecards beyond actual revenue growth in order to mask what the competitive price would be).[47] In any event, the UK market is transparent (see further paragraphs 10.20-10.31).

(iv) SAP functions as a useful comparator – SAP is used throughout the industry and provides a useful mechanism for making comparisons across channels.

Bundling

10.10 Ofcom describes (at paragraph 5.46) how the effect of the negotiation of broad annual deals is that *"airtime is essentially bundled together across a channel's schedule"*.

10.11 At the outset we note that the fact that certain impacts are more desirable to advertisers than others does not necessarily imply that there is some inherent difference in the "quality" of the impact or the quality of the viewer watching that impact, but rather that the impact makes a more targeted contribution towards that advertiser's campaign objectives in terms of reach and frequency.

10.12 Ofcom is concerned (at paragraphs 6.52 and 6.53) that the bundling of airtime across schedules and channels, may allow broadcasters to leverage any potential market power in the supply of certain types of impacts to other types of impacts.

10.13 As Ofcom notes (at paragraph 6.52), "bundling" of itself is not necessarily a competition issue. Bundling may in fact generate cost efficiencies due to economies of scope, reduction of transaction costs, the assurance of quality and/or convenience of consumers.

10.14 The practice of bundling is particularly useful in the sale of TV airtime because the bundled products (i.e. impacts), all form part of the same relevant market. Advertisers often require a mixture of peak and off-peak, and weekday and weekend impacts to deliver their campaign goals. Moreover, all broadcasters in the market compete over bundles and media buyers are sophisticated enough to make informed decisions when purchasing these bundles.

10.15 As Ofcom notes, this "bundling" allows broadcasters to optimise traded impact delivery. This is efficient for the broadcasters (who are thus able to ensure that a given slot is sold against the most appropriate demographic). Ofcom also recognises the benefits of flexible schedule access and avoidance of planning transactional costs.

10.16 However, the flexibility for broadcasters is not as absolute as suggested by Ofcom. In particular, it is not the case that *"all impacts [with the exception of "Specials"] (for a*

[47] We note for example comments in the ZenithOptimedia, UK Media Yearbook 2010 at page p. 65 regarding national press advertising sales: *"Ratecard prices are usually nothing more than the starting point for haggling: rates are a public statement of policy as much as anything else….People often ask why ratecards consistently exaggerate market prices. As with circulations, psychology plays an important role"*.

particular demographic) within a given channel are essentially treated as identical"[48] as this ignores the fact that advertiser and agency contracts will specify numerous parameters which limit the freedom of a broadcaster to treat all impacts identically.

10.17 Advertisers recognise that it is harder to achieve high levels of reach (1+ coverage), as each time an advert is broadcast it is likely to reach fewer and fewer unique viewers. The "quality" parameters are therefore about ensuring a higher probability of reach within the relevant target audience. The types of quality measure include:

[✂]

<u>Umbrella deals</u>

10.18 Umbrella deals are just one available contracting model – a number of media agencies and advertisers choose to use line-by-line contracts and there is nothing to prevent the industry adopting this model more widely were it considered more desirable. Similarly, advertisers could choose to bypass media agencies altogether and instead contract directly with media owners (see paragraph 0). Advertisers will choose how to contract with broadcasters according to which of the available options is most beneficial to their individual circumstances. As described at paragraphs 7.3-7.13, advertisers often switch between agencies and between types of contracting (direct, line-by-line agency deal or umbrella deal).

10.19 Looking specifically at umbrella deals, they are a useful and appropriate aspect of the current trading model:

(i) Umbrella deals enable media agencies to compete strongly for new clients – the fierce competition between media agencies for advertisers' spend (see paragraphs 7.3-7.13) is fuelled by the opportunities afforded by umbrella deals. Agencies are able to manage their overall discount and to offer attractive rates to potential customers in an effort to "poach" clients from competitors.

(ii) Umbrella deals allow smaller advertisers to benefit from the scale of the media agency – if all contracts between media agencies and broadcasters were negotiated on a line-by-line basis, smaller advertisers would be likely to face significantly higher prices for television advertising than their larger rivals.[49] Umbrella deals allow such advertisers to leverage the scale of their media agency.

(iii) As Ofcom notes at paragraph 5.70, umbrella deals allow for savings on transaction costs – the umbrella contract mechanism significantly streamlines negotiation between broadcasters and media agencies.

---

[48] Ofcom Consultation at paragraph 5.46.

[49] Contrary to the agencies' view described at paragraph 5.70 of the Consultation, ITV considers that all media buyers have a degree of negotiating power with respect to the broadcasters.

(iv) Umbrella deals reflect strong competition between broadcasters for volume from media agencies – there is increasing pressure on broadcasters to offer significant discounts as part of an umbrella deal to retain the agencies' SOB commitments. This pressure is mounting as a result of the media agencies' escalating countervailing power during the deal round (see paragraph 0).

(v) The market is becoming increasingly transparent – the growth in the role of media auditors can be understood as a market-led solution to any perceived lack of transparency arising from the existence of umbrella deals (see paragraphs 10.26-10.31).

(vi) Market participants are familiar with the umbrella deal system – any change would bring additional costs and uncertainty. Under the French system (where umbrella deals are banned), both agents and advertisers receive invoicing information directly from broadcasters. This duplication of effort is likely to lose some of the efficiency savings of agency contracting.

(vii) Regardless of whether an advertiser buys airtime through an umbrella or line-by line deal, they may receive direct information from broadcasters (see paragraph 10.23 regarding client services).

<u>Transparency</u>

10.20 Ofcom notes at paragraph 6.15 that full transparency *"could actually provide a focal point for collusion and so distort competition between broadcasters"* and that its *"benchmark for thinking about pricing arrangements is therefore not complete price transparency but rather the ability of economic agents to be able to make meaningful and informed comparisons of the prices from different sellers on a regular basis and to be able to adjust their purchasing decisions on the basis of that information"*.

10.21 As we explain below, the market already meets this benchmark level of transparency.

10.22 [✂] Channel 4 and Five release their channel data in very much the same way as ITV. BSkyB typically releases data across their channels. Channels which quote their SAP as a % of the ITV1 SAP would not normally further publish their data as they are simply a reflection of ITV1.

10.23 ITV and other broadcasters are also proactive in developing their relationships directly with advertisers notwithstanding that the airtime purchasing may be through media agencies. The broadcasters foster these direct relationships in order to build the profile of TV generally and their own channel(s) specifically to try to maintain/grow spend (see paragraph 5.5 *et seq.*). In doing so, they will discuss their forthcoming programming strategy and how that strategy fits with the brand's marketing objectives. [✂]

10.24 Significant volumes of data are also available to industry participants. In particular, BARB (Broadcasters' Audience Research Board) is responsible for providing the "gold standard" measurement of UK television audiences and provides:

(i) Estimates of the number of people watching television, split by which channels and programmes are being watched, when they are watched and the type of people who are watching at any one time.

(ii) Viewing data collected second-by-second and delivered on a minute-by-minute basis for channels received within the UK. The data are then processed to incorporate numerous weighting and grossing variables before being released to the industry as "overnight" minute-by-minute television viewing data at 9.30 each morning. This includes any recorded material played back on the same day as the original transmission, referred to as "VOSDAL" (Viewing-On-Same-Day-As-Live). PVR, DVR and VCR playback and catch-up VOD viewing via TV set-top boxes is reported if it takes place within 7 days of the original broadcast. This viewing (known as timeshift viewing) is then added to the live data to produce the final, minute-by-minute consolidated audience, available 8 days after the original transmission date.

(iii) The data are available for reporting nationally and at ITV and BBC regional level.

10.25 In addition, advertisers and agencies can refer to performance monitoring tools such as those offered by NMR and Thompson:

(i) NMR: Nielsen measures audiences, advertising expenditure and creative advertising across 40 countries. In the UK, their Ad Dynamix[50] system monitors TV, National and Regional Press, Consumer and Business Magazines, Internet, Radio, Outdoor, Cinema, Direct Mail and Door Drops. This includes a dedicated TV reporting tool called Monitor. TV data are reported by channel, region, advertiser and agency, and are available down to precise time and commercial break level. NMR is a cross-media tool which enables some comparison between media.

(ii) Thomson Media: provides similar data to NMR but is updated daily and tends to focus on offering market-specific cuts of the data (e.g. Tesco would buy Thomson data which are specific to its sector).[51]

---

[50] Described by Nielsen as *"the most powerful advertising expenditure and creative monitoring tool available, using cutting edge technology to bring you 5 year data plus creatives online. Easily create reports, view and download a comprehensive archive of creatives across all media. Email creative alerts ensure our clients are the first to know when, where and what competitors are advertising. Dynamic reporting for power users enables fast, flexible and precise analysis of trends, brands and campaigns across all media and sectors"*.

[51] Described by Thomson as *"We collect and analyse competitor creatives and advertising spend data from over 70 countries. Our media monitoring means we can provide you with the necessary data and insights to continuously improve your advertising ROI: More efficiently set your advertising budget; More effectively develop your creative and media strategies; Better understand and react to competitor price changes; Keep of abreast of ad trends and get creative inspiration from beyond your sector; Protect your brand from being misused"*.

10.26 In addition to the substantial amount of data available to industry participants through the channels outlined above, media auditors provide a significant amount of information to advertisers. In the Consultation Paper (see e.g. paragraph 6.64), Ofcom underestimates the role media auditors play in enabling advertisers to make meaningful and informed comparisons between different media agencies.

10.27 The role of a media auditor, put simply, is to collect and to analyse a wide range of data (particularly performance data), in order to assess the buying efficiency and overall service provided by a media agency. A media audit is typically carried out for this purpose on either a biannual or annual basis.

10.28 The proportion of television advertising spend in the UK which is reviewed by media auditors is high: approximately 58%. The use of media auditors is increasing across the industry and their remit has expanded as media auditors are employing increasingly sophisticated benchmarking methodologies in order to provide their clients with the clearest possible picture of how their media agency is performing.

10.29 This level of scrutiny further enhances the transparency of the industry, revealing as it does, among other things, how agencies are performing relative to their competitors, whether agencies are providing their clients with media plans which meet the advertiser's objectives, and whether the services they provide are in line with best market practice.

10.30 The information supplied by a media auditor therefore enables an advertiser to establish how the deal it has with a media agency compares to the arrangements in place between other advertisers and agencies.

10.31 Acting on information provided by a media auditor, an advertiser is able to punish an underperforming media agency and/or adjust its purchasing decisions in the following main ways:

(i) By exercising a performance-related fee mechanism, which is a standard feature in contracts between advertisers and media agencies. These typically impose a financial penalty on an agency which misses an agreed benchmark (which might relate to the levels of coverage achieved over the course of a campaign, or which might be referenced to a standard supplied by the media auditor). More serious instances of underperformance can trigger an obligation on the part of the agency to return value to the advertiser or even put the agency on notice to terminate the contract.

(ii) By using the media auditor's report as a lever to exert downward pricing pressure during renegotiation of the contract – this is occurring with growing frequency in the industry, as media auditors are increasingly perceived as a function of an advertiser's procurement process.[52]

---

[52] As recognised by Ofcom at paragraph 6.25 of its Consultation.

(iii) By switching to another agency – as explained at paragraphs 7.4-7.13, advertisers can and often do switch agencies.

CRR

10.32 ITV continues to believe that CRR is no longer necessary and moreover that it has unintended adverse consequences (as acknowledged by the House of Lords Communications Committee in their report of February this year).

10.33 ITV recognises that having a CC Market Investigation could represent one potential opportunity for a review of CRR [✂]. However, a CC Market Investigation is not a prerequisite for a review of CRR which in the future could be undertaken separately.

10.34 [✂] In this context, ITV considers that CRR does not provide a sufficient justification for a prolonged CC Market Investigation which would create serious risks for viewers and for the industry as a whole (see in particular Sections 15 and 16).

Efficient risk allocation

10.35 As with any advertising, it is a feature of the sale of TV advertising airtime, that neither the seller nor the purchaser can know in advance exactly how many people will view an advert. Therefore, regardless of the mechanism through which that advertising is sold, a degree of risk is inherent in the sale and purchase of advertising capacity. The main risks relate to the level of advertising spend, the price of advertising, and the commitments contained in the longer-term agreements between broadcasters and buyers.

10.36 We consider below how the current UK trading model allocates these risks between broadcasters and advertisers/agents, taking account of the features considered above. The allocation of risk is important as it can have implications for overall economic efficiency. In particular, we highlight that broadcasters face considerable revenue risk. This is because the commitments from agents in the annual deal rounds relate only to a share of spend and not to any absolute level of spend. From the advertisers' perspective, this is efficient as it enables them to respond to short-term changes in economic conditions.

10.37 Furthermore, as broadcasters commit to providing advertising at a particular discount, the broadcasters effectively take the risk of their schedule not delivering as expected. This is an efficient allocation of risk, as broadcasters (rather than agents) are best placed to mitigate that risk.

Risks – the level of advertising expenditure

10.38 Under the UK trading mechanism, broadcasters and agents negotiate annual agreements containing commitments from agents in relation to their SOB, and from the broadcasters in relation to the discount off SAP.[53]

10.39 The annual agreement does not impose any absolute financial or volume obligations on buyers. Rather, buyers must ensure that across the year as a whole, their advertising spend is allocated in accordance with the deals they have agreed with broadcasters. Broadcasters therefore face a degree of short-term risk in relation to the absolute levels of revenue they receive as their spend on content will be committed well in advance of it being broadcast. Broadcasters need and are well placed to balance this shorter-term risk against the longer term risk (which applies to broadcasters regardless of how advertising is traded), to maintain the attractiveness of television (and their channels in particular) through investing in content that will attract the audiences that advertisers want to reach.

Risks – the price of advertising

10.40 However advertising is traded, there is an inherent uncertainty about the volume (and demographic mix) of impacts advertisers will obtain when they purchase advertising capacity. This cannot be known until the advert has been aired. At the time of booking a campaign, UK broadcasters do not guarantee the impacts that will be delivered for any given level of spend. Therefore the risk that the budget for a particular campaign does not deliver the expected impacts lies with the advertiser. As the UK system is based on SAP, the price will be affected by total advertising spend in the market.

10.41 The risk that a particular level of budget will not deliver on a campaign's objectives would equally exist under a slot-trading mechanism, albeit that under a slot-trading mechanism, advertisers would be aware that prices were above expectations when the auction for each slot closes (i.e. in advance of its airing), rather than at the end of the month, as occurs under the UK trading mechanism.

10.42 While the SAP mechanism generates a degree of price uncertainty, it has the benefit of clearing the market (and of providing a relative price measure). Alternative mechanisms with fixed price commitments from broadcasters would introduce significant inflexibility into the trading mechanism, as neither broadcasters nor advertisers would be able to adjust to changing levels of demand for advertising in the short-term.[54] If, for example, demand for advertising rose, broadcasters would have to turn away potential advertisers as they would not be able to comply with their fixed price commitments. As

[53] In the UK and most other jurisdictions (e.g. the USA, Australia, and Germany), agents and broadcasters negotiate annual contracts. In others (e.g. Spain) they tend to be for a shorter duration. This has implications on the level of transaction costs in each market.

[54] Note: in Australia, Canada and the US, delivery is in terms of agreed CPT by daypart across an extended period (quarterly or seasonal).

Ofcom notes (Consultation at paragraph 6.27): *"Contracting at a fixed price in advance would be risky for both sides and the current mechanisms do appear to be one way of responding to that risk"*.

Risks – commitments from broadcasters under the long-term agreements

10.43 Under the annual agreements, UK broadcasters commit to discounts off SAP for certain target audiences, rather than to a particular price or volume of impacts. Such discounts can be understood as a commitment by the broadcaster to provide additional impacts in return for the revenue share committed by the buyer. In meeting these commitments, they take the risk of their schedule not delivering as expected.

10.44 Broadcasters must deliver the correct volume of airtime for the spend deployed in order to achieve the agreed discount off SAP. This may mean managing audience delivery in order to ensure that the correct discounts are received.

10.45 The notion of deal debt or deal credit is an important factor in the trading mechanism. If broadcasters fail to meet their contractual obligations, this will impact the amount of investment that buyers will make in the future and the conditions of sale that they expect to associate with such investment.

10.46 The current system therefore gives broadcasters a strong incentive to maintain the attractiveness of the entire (bundled) package of its content.

10.47 The broadcaster – as operator of the schedule and buyer/commissioner of the content – is well placed to bear this risk. In particular, it can take specific actions to improve the prospects of predicted impacts being delivered, for example through enhancing the level of cross-promotion or altering the schedule. It is the broadcaster that controls and plans future programme development, doing this with a view to attracting audiences that will be of value to advertisers.

10.48 Ofcom recognises the benefits of this aspect of the trading regime at paragraph 6.55 of the Consultation: *"it is possible that media buyers might accept that placing responsibility for the optimisation of the delivery of commercial impacts with the broadcaster – and thus the broadcaster taking the risk for the performance of its schedule – delivers certain offsetting benefits"*.

10.49 For markets in which slots are traded (e.g. Germany), the broadcaster simply delivers the agreed slots at the agreed price and has no responsibility for meeting individual campaign targets. Buyers therefore bear all of the short-term risk for audience delivery. In these circumstances, buyers will do their best to predict audiences and invest in optimisation capability (whether in the form of additional staff and/or automated systems) to manage this risk

11. International comparison

11.1 In terms of how TV airtime is traded, there are two key variables to be considered in every market:

(i) Is the traded currency "time" (i.e. slots) or "audience" (i.e. impacts)?

(ii) Is the trade based on a rate card valuation or a negotiated cost per unit (whether time (e.g. cost per 30” slot) or audience (e.g. cost per thousand impacts)).

11.2 Table 11.1 summarises how certain key international markets trade based on these variables. These are supplemented by paragraph 11.3. It is however important to bear in mind that the method of airtime sale is not the only difference between the markets. For example in the case of the UK, the existence of the BBC has a significant role in the competitiveness of the viewer and content markets. Other features such as the geographic nature of the market and whether there are limits on advertising time are also relevant. For example in Spain, individual commercial breaks can have 20 or even 50 different advertisements, and in an hour of programming in the US there can be 16-18 minutes of advertising.

Table 11.1:
Trading model by market

	Cost of Time	**Cost Of Audience**
Rate Card Base	- France - Germany	- Australia FTA channels - Canada
Cost Per Unit Base	- Netherlands (some STER breaks) - Some US specials	- Australia STV & DTT - Netherlands (majority of market) - Spain - UK - US most trades

Source: [✂] *using input from their local offices in each country.*

11.3 We note some further particular features of the trading models in these countries:

(i) Share of broadcast (or share of free to air broadcast) is used to some extent in other countries including Australia, Canada and France and also used for comparison purposes e.g. in the US.

(ii) The UK is unique in trading off SAP. Discounts off ratecards or costs per thousand/costs per rating point are more typical elsewhere.

(iii) Although the prominence of umbrella deals varies, agency deals are common in all countries. However in France, the “Loi Sapin” dictates that agencies cannot re-sell airtime at a different price to that at which they bought it – invoices are therefore sent directly to advertisers regardless of whether they pay the broadcaster directly.

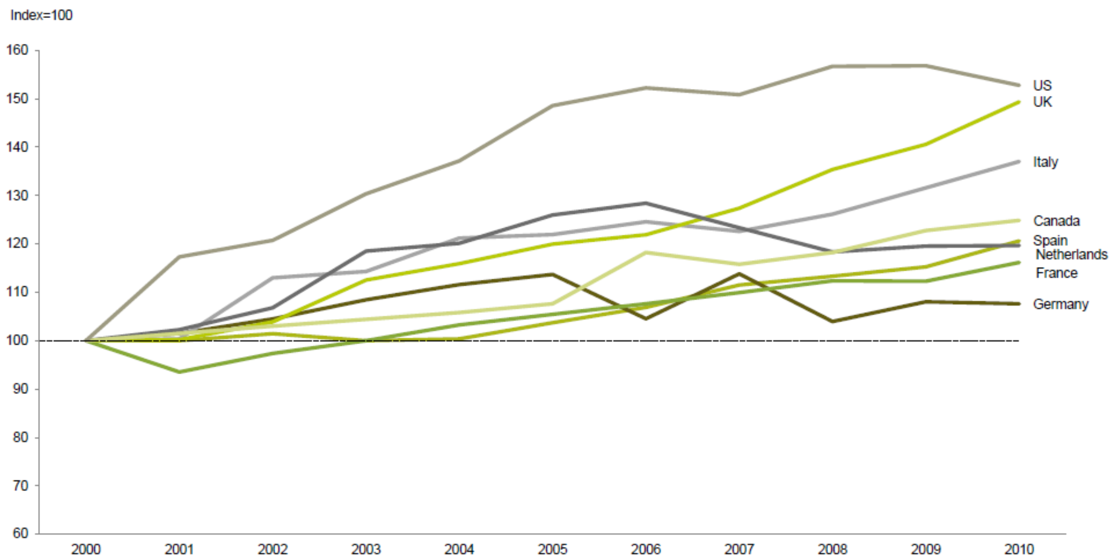
(iv) Many markets have annual deal rounds which prescribe the terms of trade between a broadcaster and a buyer. The main exception is Spain where negotiations are typically monthly.

11.4 Any review of the UK trading model needs to have regard to the alternatives. We show below how the UK fares relative to other markets on certain key metrics which further illustrate the lack of harm to advertisers and viewers in the UK.

Price

11.5 We note first that the supply of impacts[55] in all markets has grown strongly over the last decade. However, since 2005, the supply of impacts in the UK has grown more quickly than in other major developed markets. See Figure 11.1.

Figure 11.1:
Index of total television market all adult impacts sold by country, 2000-2010

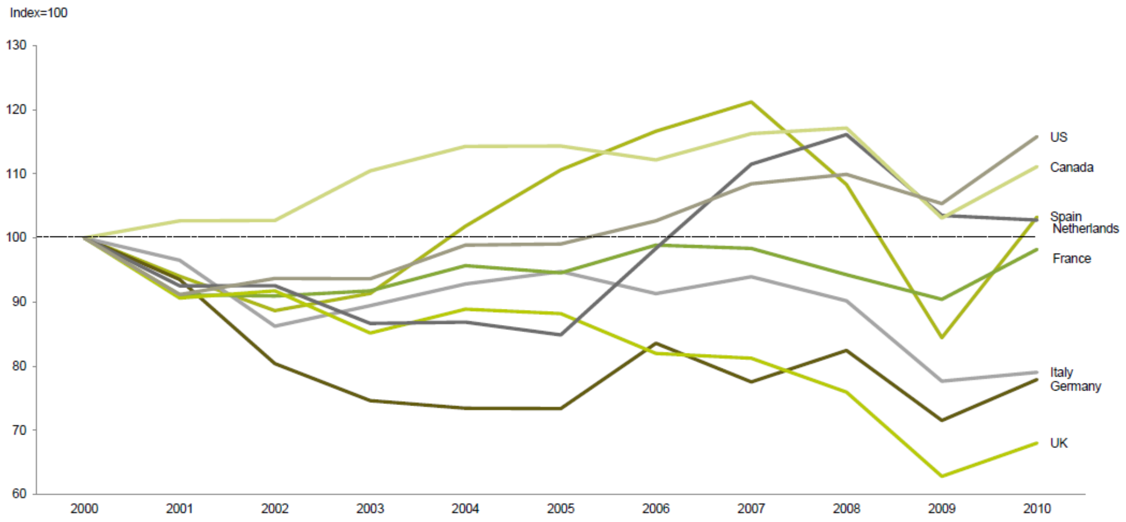


Source: *Oliver & Ohlbaum Analysis. See further* Attachment 2 *for a full list of sources by country.*

11.6 Meanwhile, the average price of television airtime in the UK fell by 32% in nominal terms from 2000 to 2010. This decline in price is greater than declines in any other major developed market (see Figure 11.2).

[55] Measured in terms of 30-second equivalent weighted adult impacts, calculated on a normalised basis for all markets assuming a 100% sell out rate.

Figure 11.2:
Index of total television market average all adults CPT by country, 2000-2010

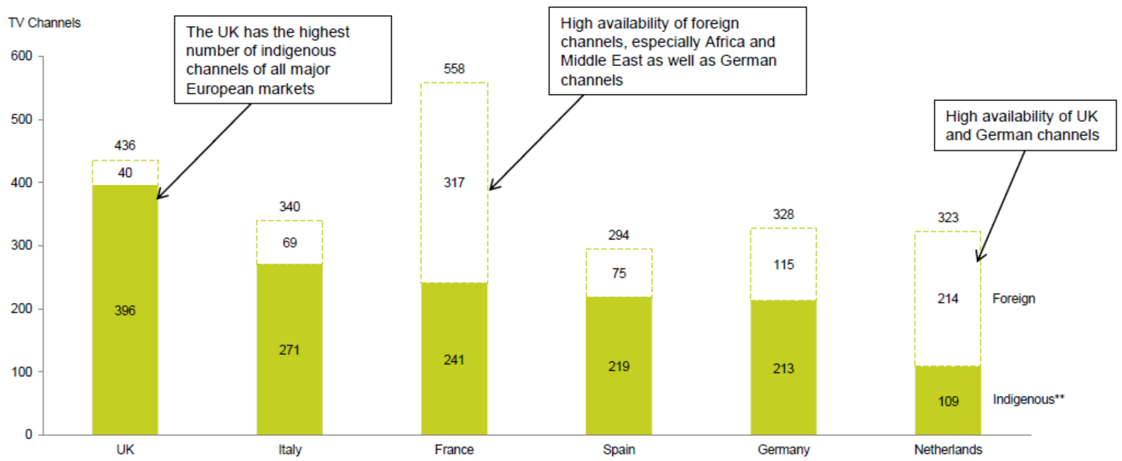


Source: *Oliver & Ohlbaum Analysis. See further Attachment 2 for a full list of sources by country.*

<u>Content investment/innovation</u>

11.7 Using a measure of the number of "indigenous channels" for comparison, we see that the UK has the highest supply of such channels of all major European markets. This illustrates the lack of barriers to entry to the UK market. See further Figure 11.3.

Figure 11.3:
Total number of TV channels by market, by type



Source: *OBS (European Audiovisual Observatory) Mavise Database, SNL Kagan TV Station Database Q4 2011, CRTC, Communications Monitoring Report 2010.*

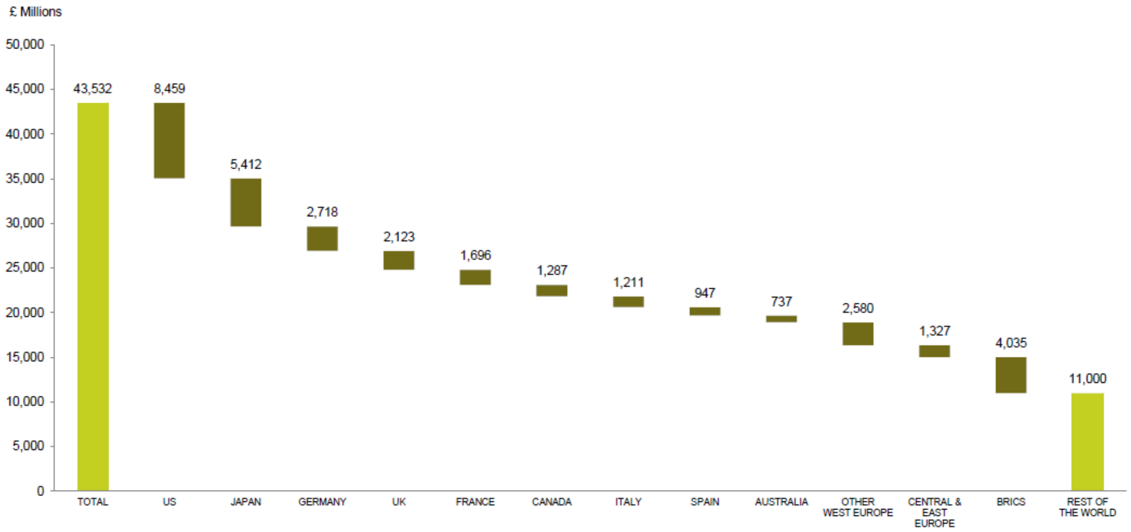
Notes: [1] Channel genres excluded: HD simulcast, timeshift (+1 etc.), adult, games, betting & lottery, home shopping & promotional, regional, local or window.

[2] The OBS Mavise Database consists of a complete survey of over 7,000 pan-European, national, regional or local channels broadcast in the EU and two candidate countries

(Croatia and Turkey). The indigenous country refers to the "main targeted country" of the channel in question.

11.8 The UK also ranks highly in terms of the total spend on original programming (see Figure 11.4) and in terms of the level of spend on original programming per capita (see Figure 11.5).

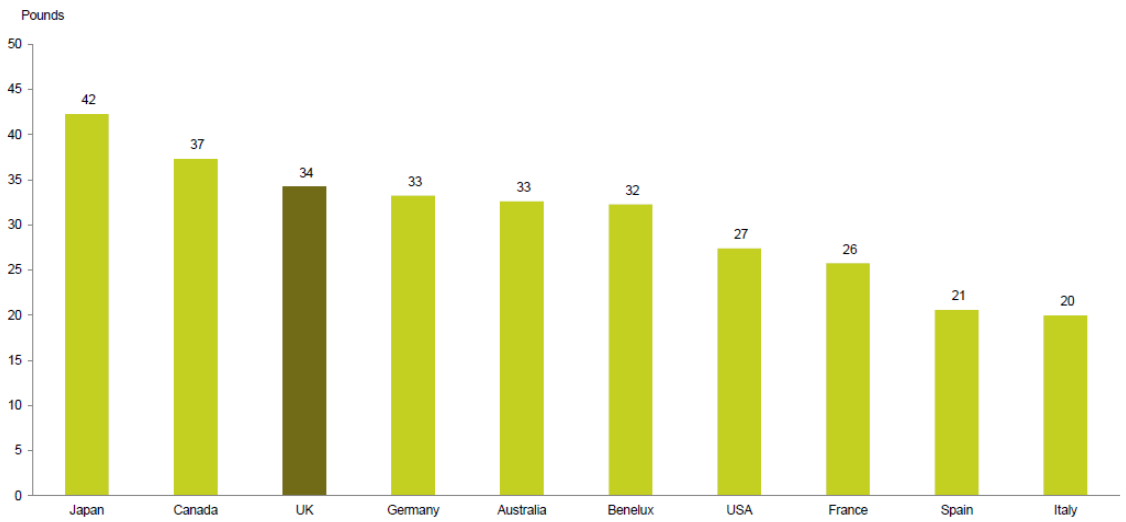
Figure 11.4:
Estimated global original indigenous TV content investment market size, 2009



Source: OBS, SNL, Kagan, Company reports, Oliver & Ohlbaum analysis.

Notes: Data excludes spend on news and sports programming, but includes syndication expenditure in the US.

Figure 11.5:
Originated TV content spend per capita, 2009



Source: OBS, SNL, Kagan, Company reports, Oliver & Ohlbaum analysis.

Notes: Data excludes spend on news and sports programming, but includes syndication expenditure in the US.

11.9 It is also important to note that the UK's positive record on content investment is not limited to publicly funded broadcasters. Rather – see Figure 8.2 – the UK's main commercial advertising-funded network groups spend more on original indigenous programming than their counterparts in all major European markets.

Profit margins

11.10 Falling advertising revenues coupled with higher content investment levels mean that UK broadcasters have lower profit margins than their international counterparts. Table 11.2 below shows how ITV's margins compare to those of similar international broadcasters.

Table 11.2:
Average profit margins between 2004 and 2010 – international comparison

	EBITDA margin
[✂]	[✂]
Five	-1.5%
M6 (France)	14.2%
TF1 (France)	13.8%
ProSiebenSAT.1 (Germany)	23.4%
RTL (Netherlands)	19.3%
Antena3 (Spain)	27.2%
Canwest (Canada)	23.8%
Discovery (various)	31.3%
Viacom (US)	40.7%
MTG (various)	19.5%
Average across comparator broadcasters	**20.8%**

Source: *Oxera analysis, based on information received from ITV and annual accounts.*

Note: [1] The comparator broadcasters used in Table 11.2 are based on those identified as comparators to ITV in Oxera's submission to the House of Lords Select Committee on Communications (2011) (page 39, Appendix 1, Table A1.2). The most appropriate comparators were identified using a three-step process. First, a broad set of comparators were identified using Ofcom's 2007 Spectrum report (which reviewed the TV markets in France, Germany, Italy, Spain, Sweden and the US) and additional companies from the European Commission's MAVISE database. Second, to ensure that the business models of comparators were broadly similar to that of ITV, companies that were either publicly funded, publicly owned or whose main activities were not in broadcasting were excluded. Third, the comparator set was narrowed further to only include companies with business and financial risk characteristics similar to those of ITV.

[2] The annual EBITDA margin for ITV Broadcasting reveals considerable variation during this period. The EBITDA margins fell significantly from 2005 to 2009 but recovered in 2010 (and the first half of 2011).

PART B - OFCOM SHOULD IN ANY EVENT EXERCISE DISCRETION NOT TO REFER

12. Ofcom discretion

12.1 For the reasons described in PART A, ITV does not think that Ofcom should have any reasonable grounds for suspicion of competitive harm regarding the UK TV advertising trading mechanism.

12.2 In any event, it would be within Ofcom's discretion[56] not to refer the case for a full CC market investigation. In this regard, we refer to certain precedent cases (see summaries in Annex D) in which the OFT (against the same test and under the same powers as those currently being applied by Ofcom) decided not to refer the case to the CC despite finding reasonable grounds for suspicion of competitive harm.

12.3 Many of the factors which drove the OFT to decide against referral in those cases apply equally to TV advertising. In particular:

(i) The CC may well find it difficult to gather the necessary evidence to enable it to assess the competitive state of the markets (see paragraph 15.4).

(ii) The CC is unlikely to find an appropriate or proportionate remedy (see Section 14). The prospective nature of the test and the fact that changes to the trading mechanism would go to the heart of the current industry dynamics mean that the CC would also struggle to assess the impact of any remedies to address any adverse effects identified.

(iii) There is no harm to advertisers (see Section 7) and there is no evidence of consumer detriment in terms of price, quality of service, choice or innovation. Rather, consumers (as viewers and as purchasers of advertised goods) are well served (see Sections 8 and 9).

(iv) Insofar as there are any problems with the market, it would be more efficient and effective for the market to resolve them itself (see Section 17). Alternatively, if Ofcom retains concerns about e.g. information asymmetry, Ofcom guidance should be more than sufficient to address these concerns.

12.4 That the TV advertising market should not be referred is also consistent with the OFT's guidance on Market Investigation References (OFT511) which notes,[57] at paragraph 2.1 that *"[Ofcom] will only make references to the CC when the reference test in section 131 of the Act [EA 2002]* *<u>and</u>*, *in its view,* *<u>each of the following criteria</u>* *have been met:*

---

[56] s.131 Enterprise Act 2002.

[57] Note 1 of that guidance provides that *"References to the OFT in this guidance are to be interpreted as applying to these [sectoral] regulators [including the Director General of Telecommunications, now Ofcom] with concurrent jurisdiction, unless the text indicates otherwise"*. Ofcom notes at paragraph 1.3 of its Consultation that it will be applying these guidelines in the present case.

- *it would not be more appropriate to deal with the competition issues identified by applying CA98 or using other powers available to [Ofcom] or, where appropriate, to sectoral regulators*

- *it would not be more appropriate to address the problem identified by means of undertakings in lieu of reference*

- *the scale of the suspected problem, in terms of adverse effects on competition, is such that a reference would be an appropriate response to it*

- *there is a reasonable chance that appropriate remedies will be available"* (emphasis added)

12.5 As we explain below, these criteria are not all met in the present case.[58]

13. Scale of the problem

13.1 We note paragraph 2.27 of the OFT guidance on Market Investigation References: *"[Ofcom] will only make a reference when it has reasonable grounds to suspect that the adverse effects on competition of features of a market are significant. In making this assessment it will consider whether these suspected adverse effects are likely to have a significant detrimental effect on customers through higher prices, lower quality, less choice or less innovation. Where it seems likely that this effect is not significant [Ofcom] will normally take the view that the burden on business, particularly in terms of management time, and the public expenditure costs of an investigation by the CC are likely to be disproportionate in relation to any benefits that may be obtained from remedying the adverse effects"* (emphasis added).[59]

13.2 This test is not met in the present case as there is no evidence that either group of customers of this two-sided market (advertisers or viewers) are suffering significant harm as a result of the current trading model and a CC investigation would impose a disproportionate burden on business:

(i) There is no evidence of any detriment to advertisers. In this regard we note in particular the falling CPTs of TV advertising airtime (see further paragraphs 6.2-6.3)) and that advertisers have significant choice in selecting their agents to secure the best deal possible (see further paragraphs 7.3-7.13). Average airtime prices in the UK have fallen further and faster than in other countries (see paragraph 11.5). Advertisers also benefit from broadcasters' continued investment and innovation in content which is valued by consumers (see e.g. paragraph 7.2 and Annex C).

---

[58] We focus on the third and fourth of the criteria referred to at paragraph 12.4 as the first should be irrelevant to this case and the suitability of the second will depend to a significant degree on the concerns, if any, which Ofcom retains regarding TV advertising. These are also the criteria which Ofcom focuses on in its Consultation (7.21-7.31).

[59] See also footnote 57.

(ii) Viewers are currently well served (see further Section 8 and Annex C). There is no evidence to support the proposition that costs associated with advertising are passed on to consumers (see further Section 9).

(iii) The burden on business of a CC market investigation would be very significant (see also Sections 15 and 16) and certainly outweigh any perceived harm to customers.

13.3 At paragraphs 7.21-7.27 of the Consultation, Ofcom focuses on the size of the market, the proportion of the market affected, and the persistence of the relevant features giving rise to adverse effects. Whilst these are described in the OFT guidance as relevant factors, it is important to determine first that there is in fact an adverse effect on customers. Given the lack of harm to consumers (or to advertisers) in the present case, consideration of the size of the market etc. become largely irrelevant.[60]

14. No reasonable chance that remedies will be available

14.1 As described at Section 10, the current trading model works well for the majority of industry participants. Critically, it is well understood by all those involved and is a market-based solution for the buying and selling of TV airtime. Given the complexities of the market and its changing nature, it is implausible that the CC would be able to find and implement a better trading model. This is a view supported by *Campaign* (a weekly advertising industry magazine) which noted in a 19 May 2011 article that:

"It's difficult to see who will really benefit from a referral of the TV ad market to the Competition Commission…Getting to the bottom of the arcane and imperfect world of TV airtime trading is one thing, but coming up with an alternative that is both equitable and implementable is quite another".[61]

14.2 Trying to re-write any (or all) of the current elements of the trading model risks losing the benefits which the current model brings to participants. By way of illustrative example:

(i) The SOB-trading system works well (see paragraphs 10.5-10.6). Forcing the industry to trade on a measure other than SOB could significantly reduce the flexibility which agencies and advertisers currently have in the volume of their spend (both overall and how it is distributed through the year). To illustrate, we note that advertisers in Germany started to give volume commitments (rather than SOB commitments) shortly before the global financial crisis. This resulted

---

[60] That the lack of harm to consumers and viewers should be Ofcom's focus is consistent with the broader policy objective of competition law (i.e. to promote consumer welfare). This is illustrated for example in the Ofcom "General duties" set out in the Communications Act 2003 (Section 3(1)): *"It shall be the principal duty of OFCOM, in carrying out their functions (a) to further the interests of citizens in relation to communications matters; and (b) to further the interests of consumers in relevant markets, where appropriate by promoting competition"*.

[61] http://www.campaignlive.co.uk/news/login/1069748/ (Media Perspective: Ofcom could live to regret lifting the lid on airtime trading, 19 May 2011).

in advertisers and agencies being committed to advertising spend at a level which they could no longer afford post crisis. SOB also gives broadcasters flexibility in slotting the adverts (i.e. bundling described at paragraphs 10.10-10.18). Although this requires additional staff on the part of the broadcasters, alternative systems (such as ratecard bookings) could simply shift that burden to advertisers/agencies who would not be able to benefit from the same economies of scale as the broadcasters or have the same ability to vary the schedule to mitigate the risk of underperformance. This in turn could increase costs across the industry.

(ii) SAP is also well understood and a market-led solution to previous concerns about the trading model (see paragraphs 10.7-10.9). SAP means that no channel is ever undersold or oversold. This is important given that, at the time of the deal rounds, volumes and values are unknown. Tying spend to a prospective measure could bring a greater degree of risk and uncertainty. SAP also provides transparency regarding relative price (see further paragraph 10.9(iii)).

(iii) Umbrella deals yield a number of advantages to advertisers (see paragraphs 10.18-10.19). Banning umbrella deals (as is the case in France) would require each advertiser to negotiate directly with broadcasters or for each media agency to do so on behalf of each client. In either case this could significantly increase transaction costs borne by the industry and likely require all parties involved (i.e. at both the agency/advertiser and at the broadcaster level) to employ additional staff. There is no evidence that particular classes of advertisers benefit disproportionately from umbrella deals.

14.3 This highlights the key reason why there is no reasonable likelihood that the CC would find suitable remedies – the lack of a clearly better alternative. For the CC to impose remedies, it would not be sufficient simply to outlaw one or more elements of the current model. Rather, for such remedies to be workable – and minimise disruption in the industry – it would need to present an alternative. Such an alternative should be at least as efficient and accepted by industry participants as the current model to warrant a Market Investigation. However, in practice, it is far from clear that the CC could either devise an equally acceptable alternative (which would in any event be subject to appeal) or that there could be sufficient consensus among industry participants to devise an alternative by means of undertakings.[62]

14.4 That the CC is not best placed to prescribe how the market should trade is illustrated by certain cases in which the unintended consequences of its remedies have later come to the fore. By way of example:

---

[62] Note for example the following quote from the 2010 ZenithOptimedia UK Media Yearbook (page 65) regarding national press advertising sales: *"Ratecard prices are usually nothing more than the starting point for haggling: rates are a public statement of policy as much as anything else….People often ask why ratecards consistently exaggerate market prices. As with circulations, psychology plays an important role"*.

(i) In its 1989 report on the supply of beer, the CC (then MMC) found there was a lack of effective competition in the brewing industry arising primarily from the extent to which the licensed premises were tied to the national brewers. It therefore ordered the sale of pubs by the brewers. The breaking of the traditional relationship between brewer and pub is widely acknowledged to have been the direct cause of the development of pub chains and of the "PubCo tie" (something the MMC failed to anticipate). Meanwhile independent wholesalers have not grown as anticipated as a result of the MMC's orders.[63] The rise of the pub chains has prompted a number of further inquiries including the 2004 House of Commons Trade and Industry Committee on "Pub Companies", the 2009 report from the House of Commons Business, Innovation and Skills Committee on the relationship between pub companies and their lessees and the 2010 super complaint to the OFT by CAMRA.

(ii) The 1995 CC (then MMC) report on the video game consoles market found that the market was dominated by Nintendo and Sega, with a combined market share of nearly 100% for consoles (hardware) and around 40% for games (software).[64] The CC concluded that *"Nintendo and Sega remain well placed to retain their dominant position in the market and derive profit from it"*. However, the report was outdated almost from the time of its publication. In the same year, Sony launched the Playstation game console in Europe which went on to sell over 100m units worldwide (only its successor, Playstation 2, has to date sold more units).[65] Several further generations of game consoles have since been developed. Microsoft also successfully entered the game console market in 2001, with Xbox, while Sega, one of the two companies found to be dominating the market in 1995, exited in 2001.

(iii) In 2000, the CC completed its investigation into impulse ice creams. One of its conclusions was that Birds-Eye Wall's ("**BEW**") (the supplier of the leading brand of wrapped impulse ice cream in the UK) should be barred from engaging in direct distribution of impulse ice creams and, although BEW would be allowed to continue to supply free-on-loan cabinets to retailers, it could only insist on 50% of the freezer space being used for its ice creams. These remedies were imposed to resolve the CC's concerns that BEW was using a variety of vertical restraints to foreclose the market and sustain its brand leadership unfairly. Had the practices which the CC outlawed been the cause of the foreclosure, post implementation of the remedy we would expect to see falls in BEW's share and gains by its competitors. However that was not borne out in practice as BEW's

---

[63] The Supply of Beer, December 2000, OFT 317: www.oft.gov.uk/shared_oft/reports/comp_policy/oft317.pdf.

[64] Monopolies and Mergers Commission (1995) *Video games: A report into the supply of video games in the UK*.

[65] Sources: http://www.scei.co.jp/corporate/data/bizdataps_e.html; and http://www.nintendo.co.jp/ir/library/historical_data/pdf/consolidated_sales_e0809.pdf

share remained flat.[66] Moreover, the restriction on the conditions of loaning retailers freezer cabinets changed BEW's incentives to invest in freezers resulting in a net decline of freezer provision. As one commentator noted: *"One might conclude that the maintenance of BEW's brand share shows that there was "no harm done." But if BEW's business practices were pro rather than anti-competitive, the concern is that the remedies might have had the unintended effect of reducing economic efficiency, lowering output and harming consumer interests"*.[67]

(iv) The CC's 2002 report into the supply of banking services by clearing banks to small and medium-sized enterprises recommended a range of measures including that the four largest clearing banks would have to pay interest on business current accounts of at least base rate minus 2.5%. However, as a 2002 article on that report notes[68] *"Regulatory intervention to "improve" the competitiveness of markets requires pragmatism. It is important to gauge what can reasonably be achieved in the light of market characteristics as well as to take account of the likely impact of intervention on the future development of competition"*. The article goes on to explain how *"to insist that the incumbent*

---

[66] *With the benefit of hindsight – the 2000 UK impulse ice cream investigation*, ECLR 2005 26(10), 533-537: *"The latest evidence on trends in brand shares, however, tells a rather different story. The AC Nielsen data on which the CC relied show a 66.4 per cent brand share for BEW in 2000, the year in which the remedies were implemented, and by 2003 that share remained at just above 65 per cent. Mars, meanwhile, had a Nielsen brand share of 14.7 per cent in 2003, only a small improvement on its position in 1998 and 1999 (respectively 14 per cent and 12.7 per cent), and the share of Richmond Foods (which comprises both the Nestlé and Treats brands) stood at under 11 per cent, several points down from the corresponding share prior to the CC inquiry. The fact that BEW's share remains little changed from the period before the CC inquiry, and that the main rival brands have seen no material growth, strongly suggests that the CC was mistaken in its belief that the exclusive vans and cabinets had a market-foreclosing effect.*

If the remedies did nothing to facilitate a boost to competitors' market shares, it is interesting to assess whether the restrictions that were placed on BEW's commercial conduct might have affected the market in other ways. Specifically, since BEW had plausible procompetitive motives for being involved in direct distribution and in the provision of cabinets, is there any evidence that consumers have been denied the benefits that flow from those factors? There is some evidence that this has been the case.

It is clear that the obligation on BEW to allow rival manufacturers to free ride on BEW loan cabinets has affected BEW's approach to investment in retail cabinets. BEW started to limit the number of new retail cabinets it loaned to retailers shortly after the cabinet remedy was introduced, and today it no longer makes this offer available to retailers. In place of these loan activities, BEW has increased the number of cabinets it sells to retailers, but the number of new cabinets subject to this sales option remains well below the rate of loan provision that existed in 1999.

The wrapped impulse ice cream segment has also suffered a significant decline in volume in the period since the CC remedies were implemented. Nielsen data show that the total market volume fell by 14 per cent between 1999 and 2000. After applying the "weather index" that BEW uses to normalise market aggregates for the impact of good and bad summer weather on aggregate sales, this translates to a 10 per cent drop in volume in the first year of the CC remedies, and a weather-adjusted market volume in 2003 that was more than 20 per cent down on the 1999 level. The CC's remedies might not be the sole determinant of aggregate volume changes, but these declines are striking, and justify at least a reasonable suspicion that the UK regulatory authority's actions have had the perverse effect of reducing investment and output levels, ultimately harming consumer interests."

[67] *With the benefit of hindsight – the 2000 UK impulse ice cream investigation*, ECLR 2005 26(10), 533-537.

[68] *The SME banking report*, ECLR 2002 23(9) 454-456.

banks also pay interest on business current accounts must have a detrimental effect on viability of new entry…by making incumbent banks pay interest the gain from switching to a new entrant is reduced, undermining the incentive of the SME to switch. Many commentators view this as a classic example of the "law of unintended consequences". Redistributing a large chunk of the allegedly "excessive" profits of the incumbent banks to SMEs appears to have undermined the viability of entry of their potential rivals".

14.5 The risk of "unintended consequences" is especially acute here where the CC would (i) be seeking to impose a remedy that goes to the heart of how the market trades, (ii) in a fast moving market.

15. Prolonged uncertainty

15.1 Section 137 of the Enterprise Act provides a statutory limit for a CC Market Investigation of 2 years. This represents a long period of uncertainty for any industry and particularly so for one like TV advertising which is already experiencing considerable uncertainty over the impact of the significant changes happening both in and around the industry (see further Section 17, Annex B and Attachment 1). Moreover, in practice, industry uncertainty would almost certainly stretch well beyond that time as the statutory limit does not include a period for the consideration and implementation of any remedies and does not reflect appeal periods (which occur in about a third of cases).

15.2 On average CC Market Investigations have taken 3 years and 4 months from start to finish (i.e. from referral to remedies, including appeals) with individual cases taking up to 58 months.[69] The complex nature of the television advertising market suggests that it would fall at the lengthier end of the scale, particularly if any remedies are proposed.

15.3 During this time, not only are relevant businesses subject to considerable uncertainty, they also have to devote significant resources to working with the CC. That the time taken for cases to complete is lengthy and *"can involve significant burdens and costs to industry"*[70] including *"legal, administrative, management time and delays in completing cases"*[71] is acknowledged by the Department for Business, Innovation & Skills ("**BIS**") in its recent consultation on Competition reform. Indeed, one of the means by which the Government is seeking to achieve its "overarching objective" (to maximise the ability of the competition authorities to secure vibrant, competitive markets that work in the interests of consumers and to promote productivity, innovation and growth) is to

---

69 Based on a review of all Market Investigations referred to the CC since 2004 but excluding two recent referrals which are yet to reach a conclusion. As regards remedies/appeals timing, please note: (i) in *Domestic Bulk Liquefied Gas*, the second remedy (on "metered estates") has been used; (ii) in *Groceries Markets*, the appeal to the CAT and the CC remittal decision have been taken into account; (iii) in *Payment Protection Insurance*, the appeal to CAT and the CC remittal decision have been taken into account; and (iv) in *BAA Airports*, appeals to the CAT, the Court of Appeal and the Supreme Court have been taken into account.

70 *A Competition Regime for Growth: A Consultation on Option for Reform*, BIS, March 2011, paragraph 3.26, page 27.

71 A Competition Regime for Growth: A Consultation on Option for Reform, BIS, March 2011, paragraph 4.18, page 36.

"*improve speed and predictability for business – building on the regime's ability to take the timely, proportionate and predictable actions that limit burdens on business and that provide for the certainty that enables business to invest and innovate with confidence*" (emphasis added).[72]

15.4 ITV is in no doubt that the TV industry (from the perspective of broadcasters, agencies, advertisers and viewers) would suffer from such a protracted and expensive period of uncertainty. Moreover, the scope for the CC to garner a comprehensive view of the market will be severely curtailed by industry participants seeking to second guess or "game" the regulatory process.

[✂]

16. Disproportionate impact on advertising funded broadcasters

16.1 The longer term risks of market intervention by the CC would be felt disproportionately by ITV (and other advertising-funded broadcasters) vs. two of its main rivals (the BBC and Sky) in the markets for viewers and for original content. As described at Section 8 and Annex C, viewers are currently well served for original content and benefit from healthy competition in these markets. In circumstances where a CC-imposed solution (or even the CC investigation itself) weakens ITV's position in these markets (whether directly or indirectly), viewers will be worse off. See further Annex C which describes how a CC Market Investigation could also create a downward spiral in content investment by weakening the competitiveness of the advertising-funded broadcasters in the markets for viewers and content.

16.2 The BBC and Sky are funded in a very different way to ITV:[73]

(i) [✂]

(ii) 72% of BBC Group's 2010 revenues came from licence fees (75% in 2009) (these figures rise to 97% each year if only the UK PSB Group is considered).[74]

(iii) BSkyB plc's 2010 income was 85% subscription revenue (82% in 2009). Advertising meanwhile accounted for only 5.4% of its 2010 revenue (and 5.7% of 2009).[75]

16.3 Moreover, these rivals have enjoyed rising revenues in recent years while TV advertising revenues have been flat or declining – see Figure 16.1.[76]

---

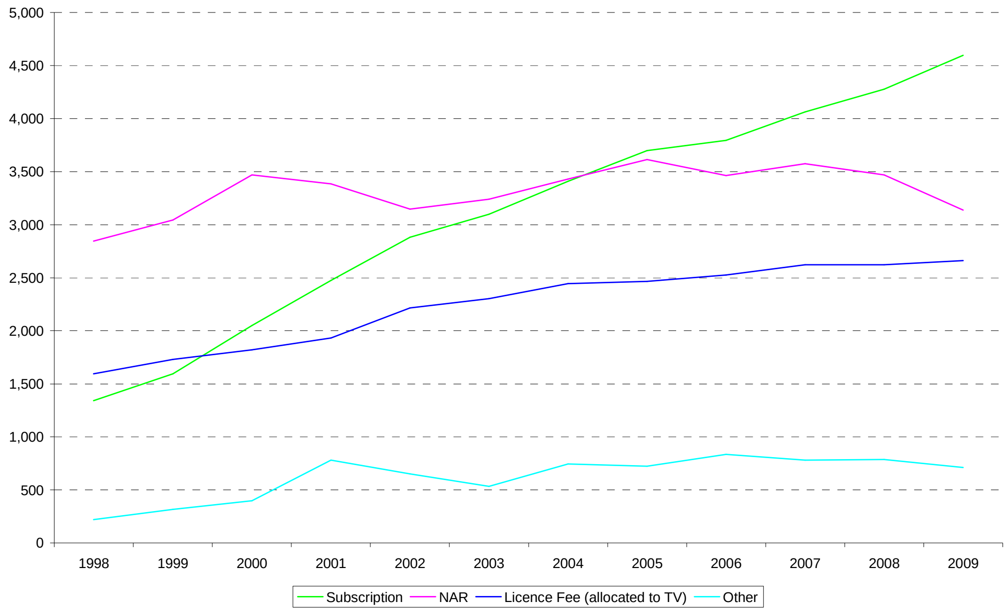
[72] A Competition Regime for Growth: A Consultation on Option for Reform, BIS, March 2011, Executive Summary, page 5.

[73] See also paragraph 3.13 of Annex C regarding the BBC's and Sky's plans for increasing content investment.

[74] The BBC recently agreed a new licence fee settlement pursuant to which its funding is stable through to 2017.

[75] This is notwithstanding that advertising revenues are a disproportionately profitable part of Sky's business.

Figure 16.1
Total TV industry revenue, by source



Source: *Ofcom/broadcasters.*

Note: Figures expressed in nominal terms. "Subscription revenue" includes Ofcom's estimates of BSkyB, Virgin Media, BT Vision, TalkTalkTV, Setanta Sports (until its closure), ESPN and Top Up TV television subscriber revenue in the UK (Republic of Ireland revenue is excluded). It also excludes revenue generated by broadband and telephony. 'Other' includes TV shopping, sponsorship, interactive (including premium-rate telephony services), programme sales and S4C's grant from the DCMS. The BBC restated licence fee revenue in 2008. Totals may not equal the sum of the components due to rounding.

16.4 A multi-year investigation into the TV advertising market (ITV's main source of revenue) therefore has a disproportionate effect on ITV and other commercial broadcasters vs. those rivals in particular such that the risks of a CC investigation would not be borne evenly by participants in the wider markets for competition for viewers and content.

16.5 It is clear that advertising revenues are critical for broadcasters like ITV for whom such revenues are the primary source of income. This remains the case notwithstanding the increasingly global nature of the content market which allows ITV and other content producers to take advantage of a broader pool of revenue streams.

16.6 This is illustrated by considering the economics of high quality drama with a production cost of £1m per 1 hour episode.[77] The secondary market (which provides revenues beyond the initial advertising-funded broadcast window) is only unlocked – particularly

---

[76] Note: only published Ofcom data used for this chart. It is predicated that the equivalent 2010 data will show that TV advertising has increased somewhat. The longer term trend is nonetheless one of decreasing advertising revenues.

[77] Note: production costs will vary according to the precise nature of the programming in question. However, high quality dramas typically cost in the region of £1m per episode to make.

for international programme sales – when a critical mass of episodes is achieved. ITV has found that drama programming sales do not gain traction internationally until there are around 12 hours of content available. Therefore, in order to secure returns via international distribution, around £12m of programming investment is required in a given title.

16.7 This is particularly challenging given the high risk nature of drama commissioning. Most dramas only tend to make a return in the broadcast window when repeat revenues are included. But the number of repeated drama titles is small, and the number of re-commissioned titles even lower:

[✂]

16.8 Long-running returnable dramas – such as Lewis, Doc Martin and Midsomer Murders – are more likely to be repeated, but the challenge for ITV lies in finding new returnable dramas. As illustrated above, [✂]

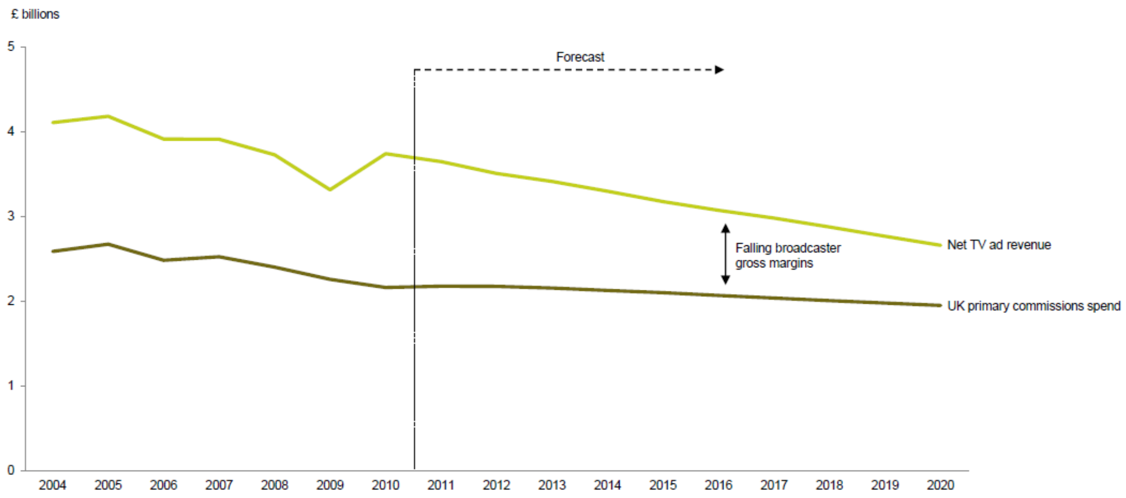
16.9 Moreover, for those broadcasters which rely upon advertising revenues for investing in programming, the reality they face is that the value of advertising slots has decreased over recent years while the costs of production have increased (see [✂]).[78] In other words, each individual viewer is more expensive to attract.

[✂]

16.10 The pressures to find alternative revenue streams in order to retain current levels of content spend will only grow as TV advertising spend falls. Figure 16.2 shows how primary commissions spend is forecast to remain broadly flat whilst TV advertising revenue falls dramatically over the next 10 years.

[78] [✂].

Figure 16.2:
UK television gross advertising expenditure and total expenditure on UK original television programmes (in real terms at 2011 prices)



Source: *Advertising Association / WARC (June 2011), ONS, Ofcom Communications Reports, Company Reports, BARB, Oliver & Ohlbaum Analysis*

Note: ONS deflators used to calculate historical data at 2011 prices and average of deflators 2000 to 2007 used to convert forecast data.

16.11 That the advertising-funded broadcasters are able to continue investing – which relies upon advertising revenues – has broader ramifications for the creative industries (including the independent production sector in the UK and – see further Annex C – the competitiveness of the viewer and content markets).

17. Timing is wholly inappropriate – market is changing anyway

17.1 Ofcom notes at paragraph 1.9 of its Consultation that *"[previous reviews of the way UK TV advertising is bought and sold] have also taken place against a background of significant wider sector developments such as changes in viewing patterns, the growth of the internet as an advertising medium, volatility in advertising revenues following the economic downturn and changes in ownership on both sides of the sector. In addition, there have been a number of technological developments within the sector (e.g. video on demand, IPTV, targeted advertising) which, while currently in their infancy, have the potential to influence the way in which TV advertising (and advertising more generally) is traded in the future".*

17.2 In ITV's view such wider market developments have more than just "the potential" to change the way TV advertising (and advertising more generally) is traded. When and precisely how such potential will be realised however is difficult to predict. Fundamental changes to the mechanics of TV advertising trading may not be evident in the next few years but over the next 5–10 years more seismic shifts are likely. Given the timeline for a CC investigation and for any CC-imposed remedies to take effect (see Section 15), the disruption and potential harm such review could cause in the meantime (see Sections 14 and 16) and that it may stifle the changes which are otherwise happening in this sector (see this Section) it is clear that now is not the time for a CC investigation.

17.3 ITV is not alone in thinking that now is not the time to act. By way of example, we refer to Jim Marshall's (former Executive Director of the media agency Starcom) online Medital article: *"For me, Ofcom needs to spend its time managing a market which is evolving very quickly. And it will best do that, not by introducing new rules, but by letting existing regulations apply until such a time <u>when the market decides</u> that they are obsolete and no longer relevant"* (emphasis added).[79]

17.4 In the last ten years online and mobile have experienced incredible growth and change, largely driven by consumer demand. Significantly, major established broadcasters are beginning to be challenged by companies such as Google and Facebook. These global brands with massive audiences are capable of transcending national markets through an offer of international reach. Their digital focus allows them not only to capitalise on the latest trends, but also to define what those trends are.

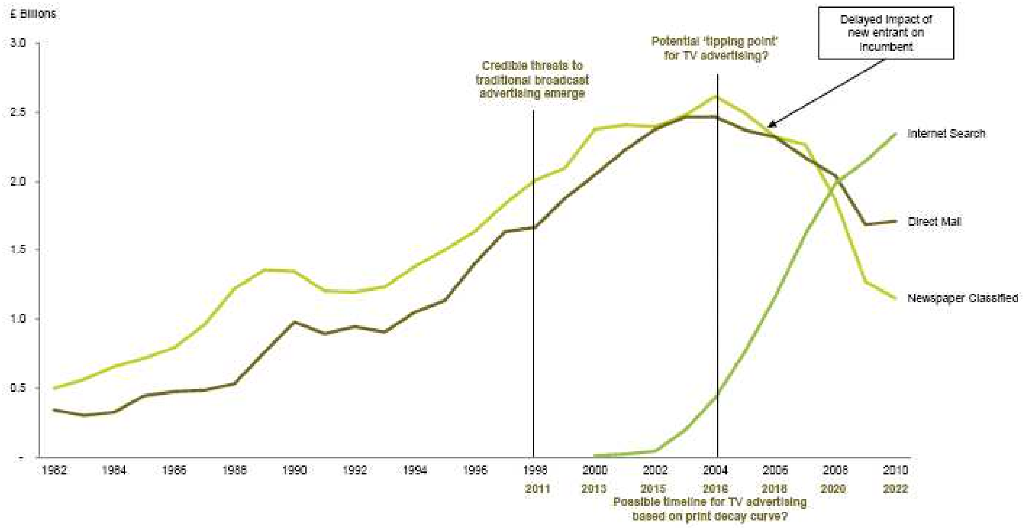
17.5 We note that some of these have been features of the market for some time. That they have not yet resulted in significant changes in the structure of the TV advertising trading model does not mean that this will not happen in due course. In this regard it is important to remember that technical change often outpaces its impact on the market (so-called "demi-Moore's law")[80] and to note the pace at which traditional models (such as printed press and music) have already been destroyed. If other traditional media owners do not adapt to this change (or are hampered in doing so), they run the risk of losing audiences and subsequently advertising revenues. Figure 17.1 shows how the spend on direct mail and newspaper classified advertising has fallen whilst internet search advertising has grown, and shows the rise of internet search advertising. It also illustrates Oliver & Ohlbaum's analysis (see also Attachment 1) of where in the direct mail and newspaper evolution television currently sits. We see that the TV advertising industry may have reached the point that the print advertising industry approached in 1998 – suggesting a "tipping point" around 2016.

---

[79] http://mediatel.co.uk/newsline/2011/06/14/ofcom-trading-review-a-little-too-late/ (*Ofcom trading review: a little too late?*, 14 June 2011).

[80] "Moore's law" tells us how quickly computing power doubles. However, the pace with which such improvement in technology translates into real impact in the market happens – as a rule of thumb – only half as fast, hence "demi-Moore's law".

Figure 17.1:
UK direct mail and newspaper classified advertising expenditure (nominal terms)

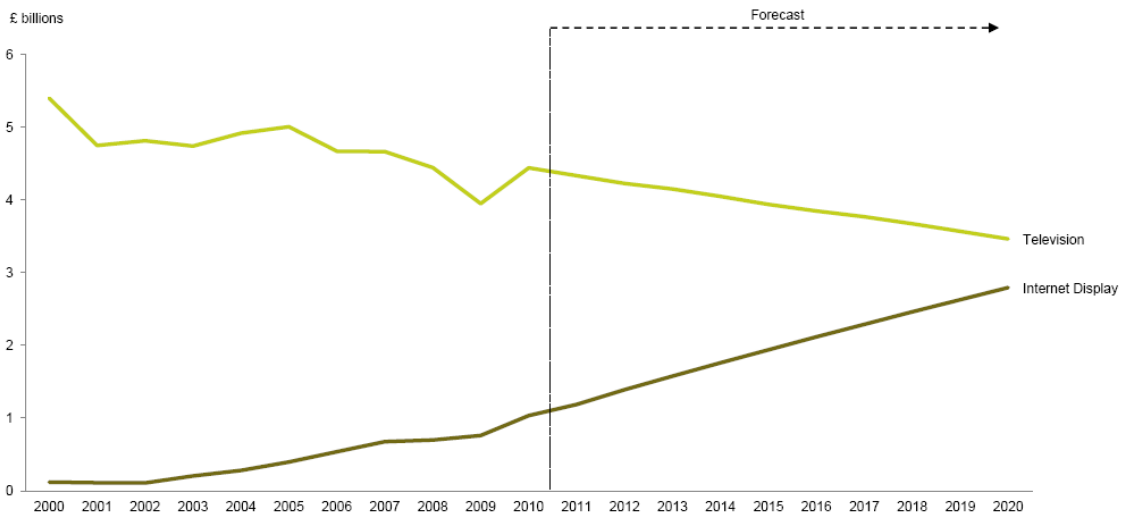


Source: *Advertising Association / WARC.*

Note: All data in nominal terms (current prices).

17.6 Oliver & Ohlbaum analysis also suggests that spend on TV advertising could drop by 25% over the next decade as advertisers switch online (see Figure 17.2).

Figure 17.2:
UK television gross advertising expenditure
(in real terms at 2011 prices)



Source: *Advertising Association / WARC (June 2011), OECD, Oliver & Ohlbaum*

Note: [1] Forecast assumes that total advertising expenditure grows at 3% per year in nominal terms to 2020 and that the proportionate switch from display to response continues at the same compound annual rate as from 2000 to 2008.

[2] OECD GDP deflators/inflators used to convert data to 2011 prices (2000 to 2010 actual and 2011 and 2012 OECD forecasts).

[3] Average of OECD deflators 2000 to 2012 used to convert 2013 to 2020 forecast data to 2011 prices (2.5%).

17.7 Although the precise impact (and timing) of the various factors highlighted in Annex B (and in Attachment 1) is unpredictable, the direction of travel is clear: online and digital have emerged as transformative forces and will become even more important in future. We note in particular:

(i) The roll out of superfast broadband will take the UK to a new level of content delivery and consumption.[81] BT and Virgin are rolling out superfast broadband, and the Government has committed to making the UK a world leader in the digital space and ensuring that superfast broadband is available to the majority of homes by 2017. In addition, the Government is seeking to improve accessibility to technology through "Race For Online".[82]

(ii) These developments in broadband technology and take-up will drive significant further change. Convergence will increasingly become the norm, with PCs, mobiles and TVs increasingly merging. A host of new devices will enable access to a global library of information and data. Seamless media access and consumption will be a richer and deeper, more tailored, experience.

(iii) Just as the fundamental dynamics of the music and print industries have been reinvented in the past few years, so over the next few will many parts of the media industry. Changes in technology and consumption are likely to force a significant shift in the role of scheduled TV programming as we currently know it. In the TV industry, media companies will increasingly provide viewers with access to a recommended repertoire of content drawn from their own and other companies' catalogues. Similar to the way in which online businesses make recommendations based on purchases or browsing history so too will TV recommend other programmes individual viewers want to watch.

(iv) It is also clear that connected televisions (which bring the internet to the TV screen) will also bring significant change. As recently stated in the Financial

---

[81] As Ofcom's recent data (from its August 2010 Communications Market Report) show:

(i) Internet take-up is now at almost three-quarters of UK households, with broadband in 73% of homes;

(ii) The internet is no longer solely the preserve of the young – with almost 60% of internet users now aged over 35;

(iii) Social networking sites – with Facebook as the market leader – now account for nearly a quarter of all time spent online; and

(iv) Internet usage is driving changes in advertising markets – online advertising grew through the economic downturn to reach £3.5bn in 2009. Separately, the Internet Advertising Bureau has found that online advertising revenues now exceed those of TV broadcast advertising, and that the gap between online and TV looks set to continue. Online advertising comprises a greater share of total UK advertising spend than in other major markets. TV's share of all advertising has fallen further in the UK than in other markets.

This is inconsistent with Ofcom's view at paragraph 3.14 of its Consultation that the current level of internet penetration in the UK restricts it attractiveness for FMCG or any other advertisers. This is also borne out, for example, by the list of top 20 internet advertisers (Consultation at Table 4.2) which shows that FMCG companies have embraced the use of internet advertising. We refer also to the examples (at paragraph 4.13 of Annex B) of FMCG products which have used internet marketing to "brand build".

[82] A Government-funded group headed up by Martha Lane Fox (Founder of LastMinute.com) has been tasked to ensure that all UK residents have access to broadband by 2015.

Times (on 17 September 2010): *"The competitive challenge is steep: the world's largest technology companies, including Google, Apple and Sony are all targeting the living room. This week Sony announced that its new Bravia sets will incorporate the BBC iPlayer, a key attraction of YouView".*

(v) A number of other internet connected services are developing rapidly. In many cases these developments are being undertaken by global companies who are able to take advantage of resources and scale efficiencies well beyond the means of traditional national broadcasters. For example:

(a) Samsung and Sony have rolled out web applications on their connected screens;

(b) Tesco has acquired the video-on-demand service Blinkbox, heralding the retailer's move into the audiovisual space;

(c) Amazon has acquired LoveFilm, which is transitioning itself from a DVD rental to a connected VOD business; and

(d) In the US, a number of web technology companies including Google, Yahoo and Apple, are reported to be considering a bid for the video streaming service Hulu. Such an acquisition would enable these players to expand their presence in the connected TV space.

17.8 Perhaps even more profoundly, Apple and Google are also rapidly expanding their presence in the TV space. Apple's iTunes store is a key player in the on-demand content space, its iPod, iPhone and iPad devices carry a number of VOD apps in the UK and internationally, and closer integration of Apple's mobile and tablet devices with its Apple TV connected set top box will increasingly bring Apple distributed content to the TV screen. Google meanwhile is seeking to build on its leading global position in online advertising, seeing content as a key source of value for the future. It has launched Google TV in the US, and is seeking to enhance the YouTube proposition through increasing investments in long form content. YouTube apps are already integrated into virtually all connected TV propositions.

17.9 ITV is committed to meeting the challenge of the digital world and has in particular sought to diversify its product offer and to launch new channels, online services and VOD services (see paragraph 6.7). ITV is also looking to a broader range of commercial revenue sources to compensate for the declines in TV advertising and has restructured its sales team to increase the focus on other revenue streams (in particular online and sponsorship). As detailed in the context of its Transformation Plan, ITV is seeking to diversify further its revenue base beyond TV advertising by exploiting its content across multiple pay and free platforms. Nevertheless, ITV will continue to be heavily reliant on broadcasting revenues.

17.10 The changing landscape has put – and will continue to put – pressure on TV advertising. We describe below certain changes which ITV foresees likely to result from this pressure in the near future. The current trading model has not to date stood in the way of change and would not prevent these changes from taking place. Were (elements of) the current model to become unfit for purpose in the changing world, a market-led response would be the best solution:

(i) **Data:** as described at paragraph 5.23-5.26, there is increasing demand for uniform data to track advertising performance. As “reach” data used for different media become more comparable, there will be pressure for different media platforms to become more comparable in their trading mechanisms and prices.

(ii) **Partnerships:** as digital media companies look at innovative ways to increase their share of spend, traditional media owners will need to break from their established advertising products and funding models and shape new ways of communicating with audiences. Many online businesses offer consumers content which is not only free, but also compelling for viewers.

(iii) **Ease of trading:** the speed with which business can be conducted online is proving incredibly attractive within the industry. It is straightforward for individual users to set up a Google AdWords[83] programme on their own site. The net result is that advertisers can deliver highly targeted communications at the click of a button. Traditional media channels need to be able to move quickly and flexibly in order to deliver targeted advertising tools, otherwise their ability to compete will be compromised.

(iv) **Movement of ad spend:** according to IAB/PwC, online adspend has increased every quarter since being recorded in 2003. This trend is predicted to continue. In particular, GroupM predict TV to grow +3% in 2011 while online will grow +8%. It is unlikely that overall advertising spend will increase dramatically, meaning internet money will continue to cannibalise other spend. Traditional media owners must continue to be agile and seek to capitalise on new ways of trading and delivery advertising products to market.

18. Conclusions

18.1 It is important that the TV advertising market is considered in context:

(i) Commercial broadcasters rely on advertising revenues to attract audiences through content investment and innovation.

(ii) The UK television market is changing beyond all recognition. The arrival of intense digital competition has reduced the price of advertising on television in the UK but also increased the cost of attracting audiences.

[83] See e.g. paragraph 3.4 of Annex B.

18.2 There are no reasonable grounds to suspect that the TV trading model in the UK prevents, restricts or distorts competition:

(i) TV airtime trading should not be considered in isolation as it is faces other pressures on both the advertising and viewer sides.

(ii) In any event, the TV advertising market is highly competitive.

(iii) Moreover, there is no evidence of harm to customers on either side of the TV markets: advertisers or viewers. There is also no evidence of harm to consumers of advertised goods.

(iv) The current trading model can only sensibly be assessed against the counterfactual of realistic alternatives. Against that yardstick, albeit that it has some idiosyncrasies, it works broadly well.

18.3 Ofcom should in any event exercise its discretion not to refer the market to the CC:

(i) There is no evidence of significant advertiser or consumer harm.

(ii) There is no reasonable likelihood that the CC would be able to impose remedies that would work better than the current trading model.

(iii) For the duration of a CC investigation, the advertising and viewing markets would be subject to uncertainty and distortion.

(iv) The burdens of a CC investigation would fall disproportionately on advertising-funded broadcasters (such as ITV and Channel 4) vs. their key rivals in the markets for viewers and content (in particular Sky and BBC).

(v) The TV advertising market – and the broader advertising and media markets – are changing. A CC investigation now creates an even greater risk of unforeseen consequences and may stall – or even thwart entirely – what would otherwise be market-led responses to those changes.

508948521

Annex A – Cross reference table to responses to Ofcom questions

Ofcom Consultation Question		Cross-reference to response
1.	**Do you think we have captured all the relevant market developments which might have had an impact on competition in the sector?**	There are a variety of factors which have had/are likely to have an impact on competition in the TV advertising sector. See in particular Section 17, and Attachment 1
2.	**Are there standard measure systems being developed for tracking the effectiveness of internet display advertising? If so, are they likely to affect widespread take up of internet display advertising (and over what timescale)?**	See paragraphs 5.23-5.26 and paragraph 4.3-4.9 of Annex B
3.	**Do you agree with our conclusion that, at present, internet advertising does not constitute a sufficiently strong competitive constraint on TV advertising? Is this likely to change in the foreseeable future?**	See Section 5, Annex B and Attachment 1
4.	**Do you agree with our market definition? Have we considered the appropriate market developments in forming our view?**	See Section 5, Annex B and Attachment 1
5.	**Do you agree with our overview of the way TV advertising is traded? Are there any other characteristics of trading that we should consider?**	See footnote 43
6.	**Do we understand correctly that the market has essentially operated in the same way since the early 1990s? Does our analysis of why the market evolved from a slot traded ratecard model accurately reflect reality?**	See paragraph 10.8 and footnote 45
7.	**Are there any other benefits associated with the current system of trading which we have not factored into our analysis?**	There are numerous benefits of the current system as highlighted in Section 10. We note also the lack of consumer/advertiser harm (see Sections 7, 8 and 9)
8.	**Can we draw any conclusions from features of TV advertising trading models in other countries about whether features in the UK market prevent, restrict or distort competition?**	See Section 11
9.	**How transparent is the pricing of TV airtime? Does it enable advertisers and media buyers to make informed decisions about the purchasing of TV advertising on different broadcasters?**	See paragraphs 10.20-10.31
10.	**To what extent do advertisers switch between media buyers? What factors influence the decision and how easy is it to switch media buyers?**	See paragraphs 7.3-7.12, 10.18-10.19 and 10.26-10.31
11.	**To what extent do any benefits associated with these features of the market offset or even outweigh the potential detriment?**	See paragraphs 10.2-10.4
12.	**How has the recent consolidation in the market altered the relative bargaining relationships between sales houses and media buyers?**	See in particular paragraph 0 and footnote 28
13.	**To what extent has consolidation resulted in sales houses having a strong market position in relation to particular audience demographics?**	See in particular paragraph 0 and footnote 28

Ofcom Consultation Question		Cross-reference to response
14.	**What might be the implications of consolidation for competition e.g. in terms of media buyers switching between broadcasters?**	See paragraph 0
15.	**To what extent does the bundling of commercial impacts across channel schedules and between channels constrain the ability of media buyers/advertisers to switch expenditure between broadcasters?**	Bundling does not prevent switching between broadcasters. In any event, there are numerous constraints on broadcasters' freedom to "bundle" – see further paragraphs 10.10-10.18
16.	**How important are the possible benefits to advertisers, media buyers and sales houses from the bundled sale of airtime across a schedule? Are there other benefits that we have not considered?**	The ability to "bundle" is key to broadcasters' optimisation. This has knock on benefits to agents/advertisers who are able to buy the most efficient airtime (see paragraph 10.11)
17.	**To what extent does the interaction of umbrella deals and annual SOB deals act to prevent, restrict or distort competition in the market for TV advertising?**	See Section 10 (and in particular paragraphs 10.5-10.6 and 10.18-10.19)
18.	**To what extent does the ability of advertisers to switch between media buyers serve to impose an effective constraint on media buyers' behaviour?**	See paragraphs 7.3-7.13
19.	**To what extent does the way in which media buyers are remunerated help to align incentives between advertisers and media buyers? Does it have any adverse effects?**	See paragraphs 7.3-7.13, 10.18-10.19 and 10.26-10.31. ITV is not party to agreements between advertisers and agencies so is only able to give an overall view of the competitiveness of those contracts
20.	**To what extent do the benefits of umbrella deals and annual SOB deals outweigh any concerns?**	See Section 10 (and in particular paragraphs 10.5-10.6 and 10.18-10.19)
21.	**Do respondents agree that CRR has had an effect on contract negotiations and/or innovation in the way airtime is traded?**	See footnote 44 and paragraphs 10.32-10.34 and paragraph 6.8 of Annex C
22.	**To what extent do the new methods of distributing and consuming content require the development of alternative trading arrangements? Can the market adapt and develop under the current trading mechanism? Is the current trading model likely to prevent other possible developments in the sector?**	See in particular Section 17, Annex B and Attachment 1
23.	**To what extent have broadcasters become more risk averse when considering acquiring or commissioning new programming? Is this the result of the operation of the current airtime trading mechanism?**	See Annex C
24.	**To what extent have media buyers/advertisers been restricted or prevented from experimenting with new marketing approaches as a result of the current airtime trading mechanism?**	See in particular Section 5, paragraphs 10.6(ii) and 10.6(v) and Annex B
25.	**Are there any offsetting benefits of the current trading mechanism for viewers?**	See Section 8 and Annex C
26.	**In light of the OFT's guidance on factors to take into account in considering a market reference, what is your view about the proportionality of a reference?**	See Sections 13, 15, 16, 17 and Annex C
27.	**What are your views of the availability of possible remedies to address concerns?**	See Section 14

Annex B – The Growth of Digital Marketing

1. Introduction

1.1 Television was once the main screen with which consumers (and therefore advertisers) engaged. Today, TV is just one of a trio of screens vying for attention, with personal computers and mobile phones also competing directly for viewers' attention.

1.2 In this Annex B, we summarise ITV's assessment of the growth of digital marketing and how that has changed advertisers' behaviour. ITV's assessment has been informed by analysis prepared by Oliver & Ohlbaum which focuses on the potential future drivers of change in the industry. Oliver & Ohlbaum's analysis is however separate to ITV's and should be read in parallel (see Attachment 1). In this Annex B we consider in particular the trends in digital marketing in terms of:

Key technological changes that have facilitated changing consumer behaviour including:

(i) The improvements in the digital infrastructure and the level of daily use of the internet by all demographics (see paragraphs 2.1-2.4 and 2.6 of this Annex B); and

(ii) The take up of communication devices and services (see paragraphs 2.5-2.6 of this Annex B);

Key features of consumer usage of online and mobile technology and how that has changed advertiser behaviour:

(i) Internet search (see paragraphs 3.1-3.5 of this Annex B);

(ii) Internet display (see paragraphs 3.6-3.8 of this Annex B);

(iii) E-mail and text messaging (see paragraphs 3.9-3.10 of this Annex B);

(iv) Mobile (see paragraphs 3.11-3.14 of this Annex B);

(v) Social networking (see paragraphs 3.15-3.16 of this Annex B);

(vi) E-commerce (see paragraphs 3.17-3.19 of this Annex B);

(vii) Video sharing and UGC content (see paragraphs 3.20-3.21 of this Annex B); and

(viii) Multi-screen viewing (see paragraphs 3.22-3.25 of this Annex B);

Key implications of these changes in behaviour:

(i) Mass reach – the online space provides advertisers with a wealth of new ways to achieve mass exposure (see further paragraphs 4.1-4.2. of this Annex B);

(ii) Targeting and engagement – online advertising is more targeted and as a result its interactive nature also more engaging (see further paragraphs 4.3-4.5 of this Annex B);

(iii) Online advertising offers heightened efficiency (see further paragraphs 4.6-4.9 of this Annex B); and

(iv) The countless success stories of online advertising (see further paragraphs 4.10-4.14 of this Annex B).

1.3 In order to respond to these challenges, traditional media (including advertising-funded TV broadcasters) have started – and will continue – to break away from established advertising-funding models and shape new ways of communicating with audiences.

1.4 Whilst these shifts may – to date – not have fundamentally undermined how TV advertising is sold in the UK, the pressure to do so will increase in the coming years. It is not possible to predict accurately the timing and extent of the changes to TV advertising which will be brought about by the digital world's evolution. However, we are confident that the risks to TV advertising are real and will drive further change in the market.

2. Technological changes

2.1 In 2000, the UK was lagging behind other countries in terms of digital infrastructure and adoption of digital communication devices and services. The costs of getting online were approximately £20 higher than in other leading countries, with broadband practically non-existent. Fewer than 1 in 10 households were surfing the Web and the online population was predominantly young, rich and male: online users included only 9% of the over-65s, 3% of the lowest income and 39% of females.

2.2 Since 2000, there has been a paradigm shift in UK media consumption. The internet is now an integrated and normal part of people's working and social lives in the UK. The UK now has over 46 million active internet users, with 30 million going online at least once a day.[84]

2.3 Table 2.1 of this Annex B shows how the UK internet audience now extends across all demographic groups and that time spent online extends across a multitude of different activities for each age group.

---

[84] Internet Advertising Bureau/IAD Online Behaviour Research 2010.

Table 2.1
Online activities by age group, 2010

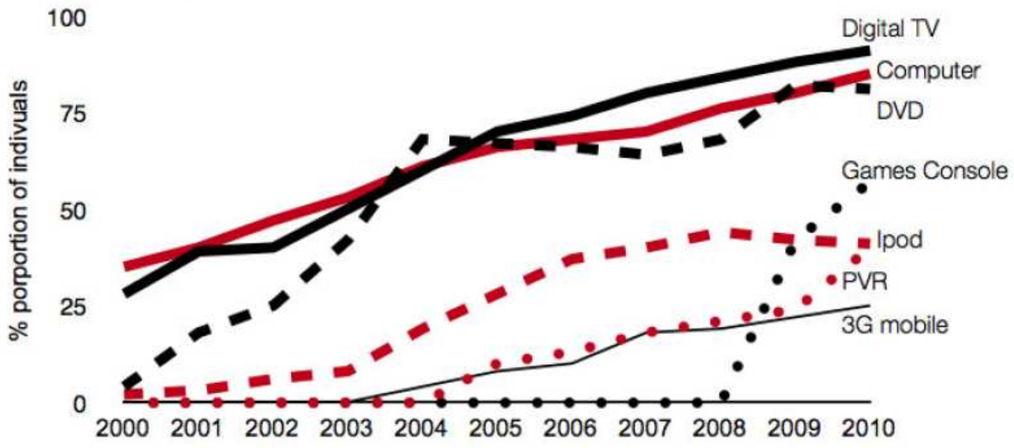
	16-24	25-44	45-54	55-64	65+	Total
Sending/receiving e-mail	88%	90%	89%	91%	87%	90%
Finding information about goods & services	64%	76%	80%	83%	72%	75%
Using services related to travel & accommodation	50%	64%	70%	72%	62%	63%
Internet banking	45%	63%	54%	53%	34%	54%
Reading or downloading online news, newspapers, magazines	52%	53%	51%	47%	40%	51%
Listening to web radio or watching web TV	59%	47%	45%	34%	24%	45%
Posting messages to chat sites, blogs, newsgroups, etc	75%	49%	31%	19%	8%	43%
Playing or downloading games, images, films or music	61%	43%	32%	24%	17%	40%
Seeking health-related information	27%	42%	39%	44%	36%	39%
Uploading self-created content	50%	43%	28%	29%	22%	38%
Consulting the internet with the purpose of learning	47%	34%	34%	30%	27%	35%
Looking for information about education, training or courses	47%	36%	27%	19%	7%	32%
Downloading software	35%	34%	23%	27%	18%	30%
Looking for job or sending job application	38%	32%	23%	11%	1%	26%
Selling goods or services over the internet	16%	28%	20%	18%	9%	21%
Donating to charities online	10%	13%	15%	13%	7%	12%
Doing an online course	11%	8%	7%	5%	3%	8%

Source: *Office for National Statistics – UK Internet Access 2010, Households and Individuals.*

2.4 The increase in online usage is in turn reflected in the rise of online offerings including Google, YouTube, Netflix, Facebook, Twitter and BBC iPlayer as well as the introduction of new devices such as netbooks, Internet Protocol TV, smartphones, tablet computers and personal video recorders ("**PVRs**").

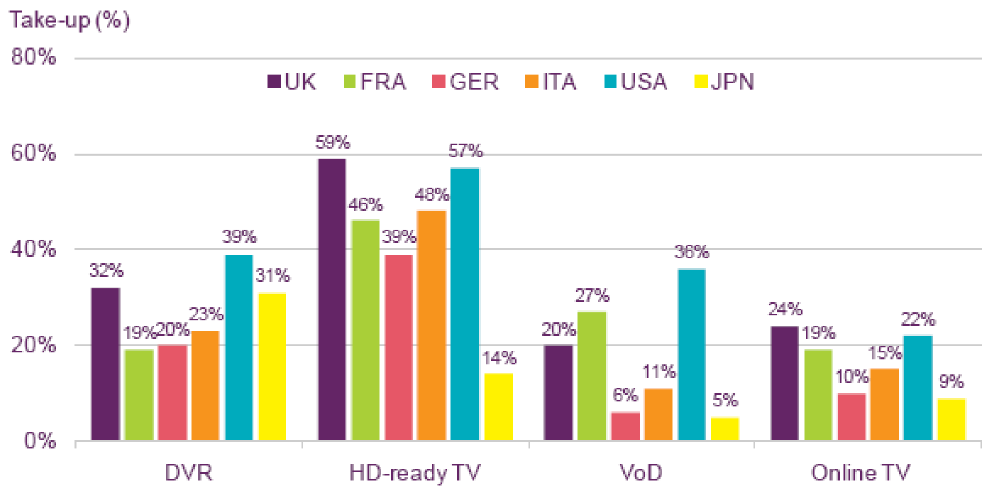
2.5 The dramatic growth in internet related services is driven by consumer take up which in turn relies on and is encouraged by infrastructure investment (to create reliable and affordable networks) and the creation of attractive and affordable (often free) online products through service innovation. The adoption of digital devices has been rapid both in absolute (see Figure 2.1 of this Annex B) and relative terms (see Figure 2.2 of this Annex B).

Figure 2.1
Take up rates of communication devices and services



Source: *Ofcom research Q1 2010 based on claimed ownership of devices.*

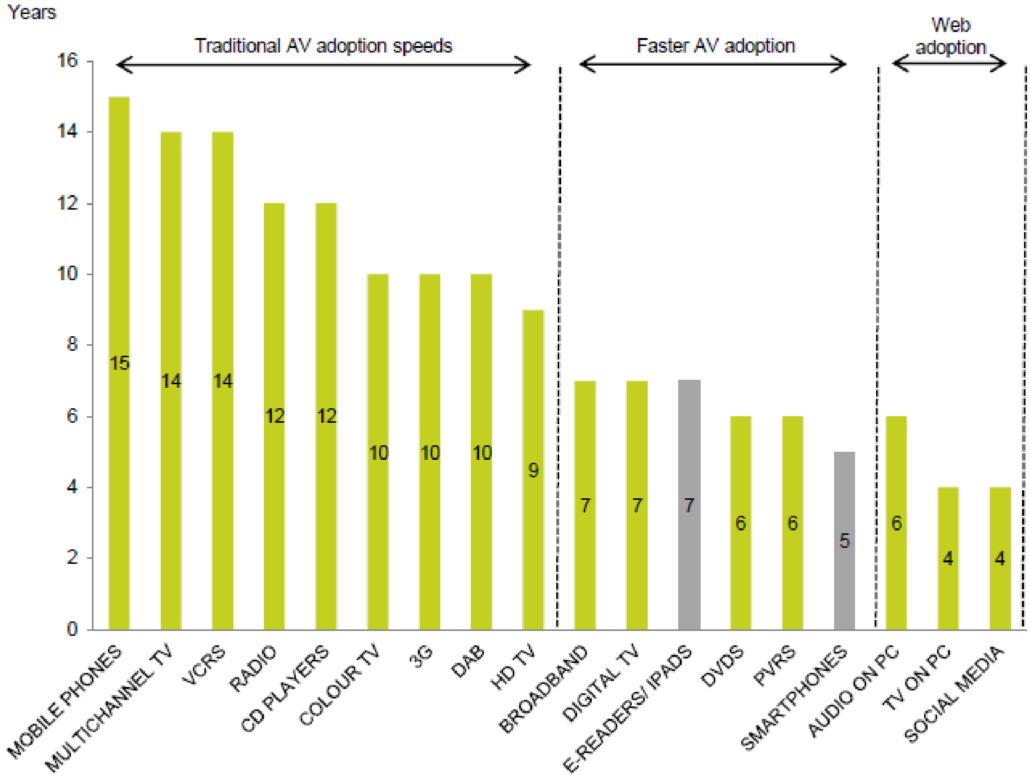
Figure 2.2
Adoption and use of key audio-visual services



Source: *Ofcom consumer research, October 2010, for all adults 18 – 64. Base sizes: UK=1016, France=1017, Germany=1014, Italy=1002, USA=1017, Japan=1001.*

2.6 Moreover, the pace of change has accelerated as shown by Figure 2.3 of this Annex B as consumers become increasingly aware of new technology and willing to invest in it. Figure 2.3 shows that smartphones and iPads/e-readers (which will encourage take up of online TV viewing and mobile advertising) are likely to reach 50% penetration of the UK market in 2012 and 2016 respectively. This explosive adoption of communication devices and services has been facilitated by heavy investment in digital infrastructure (mainly broadband and 3G connectivity) which have given the UK a world-leading position in digital TV, a top ranking in mobile connectivity, and a strong position in the take up of affordable broadband.

Figure 2.3
Number of years taken to reach 50% penetration of relevant universe, by device/application in the UK



Source: *Oftel, Screen Digest, ITC, BVA, BBC Audience & Consumer Research, Lexis Nexis, The Slow Pace of Fast Change, Bhaskar Chakravorti.*

2.7 A further technological development likely to expand in the coming years is "visual search" which uses image recognition technology (on smartphones and tablet computers in particular) to allow consumers to search for information about products or services. Examples of recent UK advertising campaigns which have made use of this technology include:

(i) Consumers being able to watch the trailer for the film *Bridesmaids* simply by pointing their smartphones/tablet computers at print adverts for the film.

(ii) The Financial Times ran an advertisement for a collaboration with Wally yachts in June 2011 which, when viewed using an iPad app, turned the still image into a film of the boats racing. If consumers then touched the screen, they were taken directly to the Facebook page for the promotion.

2.8 Google has promoted similar "visual search" services (under the name Google Goggles) in the US and is reported to have trials with Buick, Disney, Diageo, T-Mobile and Delta Air Lines to use the technology.[85]

3. Key features of consumer usage of online and mobile technology and information services

Internet search

3.1 The internet allows consumers to search for anything and everything, whenever and wherever they want to. In the UK, Google (the world's largest search engine)[86] accounts for 85% share of all searches, Bing (Microsoft) and Yahoo account for 12% between them, with the remaining 3% being made up of other smaller companies.[87]

3.2 Internet search has created opportunities for brands to insert advertising onto the search pages themselves, targeting consumers who search for particular words. This targeted and measurable offer means that search has become the largest category of online advertising – accounting for around 60% of all online advertising spend in 2009.

3.3 Search technology provides instant access to a range of sources and information that are matched closely to whatever is on a consumer's mind, and search results can also drive consumers to branded websites. In particular, a consumer looking for a particular product would typically be directed to "sponsored links" (i.e. links that have been paid for by advertisers), the manufacturer's own website, and to the websites of retailers selling that product.

3.4 The growth of search has been assisted among other things by Google's AdWords technology which enables advertisers to insert sponsored links onto Google search pages.[88] Advertisers with sponsored links have agreed with Google that their adverts

---

[85] Source: Welcome to a new reality, FT 26 July 2011 (http://www.ft.com/cms/s/0/e559dcd2-b6f5-11e0-a8b8-00144feabdc0.html#axzz1TCR1dCAb).

[86] In the UK, Google alone accounts for 4.1 billion search page views per month, 30.7 million individuals (Source: GID) and 98.29% of all mobile search queries (Source: Pingdom). Google's UK advertising income is expected to exceed that of ITV this year, with present growth rates of around 25% per quarter. Once traffic acquisition costs have been excluded, Google's total UK advertising income in the year may reach £2.55bn, well beyond the £1.7bn that ITV is expected to achieve (Source: Google's UK ad revenue to overtake ITV, Guardian Unlimited, 15 April 2011, http://www.guardian.co.uk/media/2011/apr/15/google-uk-ad-revenue-itv). Google has also leveraged its brand value (it is the world's 4th biggest brand) into other areas of advertising other than online search and online display. In particular, Google can now also deliver brand communication on mobile, social networks, video and maps.

[87] Experian Hitwise: Top Search Engines (All Categories) Sept 2010

[88] Google also offers a product called "AdWords Conversion Tracker" which allows advertisers to analyse the cost of a sale as it happens. It provides advertisers with the ability to change media spend in real-time based on consumer reactions. For example, Brand A owns an online business that sells eBooks. They know how many clicks their AdWords campaign gets, but would like to know specifically which keywords are converting to sales. With basic conversion tracking, they can get this valuable information. With customised conversion tracking, they can also report the monetary value of each sale and get the total revenue generated by each of their keywords as compared to the total cost of the keyword. With conversion statistics, Brand A discovers that the keyword "independent eBooks" has a

appear alongside or above the relevant search results. The advertisers then pay Google only if users click on the links. Advertisers are therefore able to drive users towards their brands (by anticipating what key search words are of particular interest to their potential customers), and to do so without "wastage" as they only pay when a user in fact clicks on the link.

3.5 Search is not simply replacing classified advertising. Rather, most major companies are now using search to establish, grow and maintain their brands. The importance of search has led many of the UK's top advertisers (BT, Ford, P&G, Nestle, Unilever, Vauxhall) to create "search teams" who are responsible for the day-to-day management of search and related advertising spend.[89]

<u>Internet display</u>

3.6 As described at paragraph 5.17 of PART A, expenditure on internet display advertising in the UK has grown rapidly in recent years.

3.7 Facebook (which has 28 million users in the UK alone – see further paragraphs 3.15-3.16 of this Annex B) is the UK's largest display advertising publisher[90] and is expected to be the world's largest online display advertising company by revenue this year with a forecast revenue of £2.1bn.

3.8 Display advertising is meanwhile reported to have become one of Google's fastest growing businesses as advertisers such as Ford, Kodak and Armani have embraced it. 99% of Google's largest US advertisers now run campaigns on the Google Display Network, which includes websites such as Rolling Stone and the Food Network.[91] Google's \$3.1bn purchase of DoubleClick in April 2007 was designed to unlock a vibrant advertising business for banners, videos, and other display ads. Google's display business is set to rise, from £1.6bn in 2010 to in excess of £1.9bn in 2011.[92] Its launch of Google+ (the Google social network) will only strengthen its potential in online display advertising.

ROI of 500%. Consequently, the campaign is optimised by increasing the spend on that keyword, thus maximising the ROI.

[89] Nielsen Media Research 2009

[90] Special Report: Facebook began as a geek's hobby. Now it's more popular than Google: Half of all those online have visited the social networking site. Soon it may become synonymous with the web itself, The Guardian, 4 January 2011, http://www.guardian.co.uk/technology/2011/jan/04/faceboook-mark-zuckerberg-google?INTCMP=SRCH.

[91] International Herald Tribune, 23 September 2010 p21

[92] Facebook set for display ad lead, FT.com, 10 May 2011, http://www.ft.com/cms/s/2/d4f537d2-7a65-11e0-af64-00144feabdc0.html.

E-mail and text messaging

3.9 As consumer usage of e-mail and text messaging has grown, so has the use of e-mail and messaging as marketing tools – they provide a highly cost effective means of communicating directly with interested consumers, an option which does not exist for traditional media channels such as TV broadcasting.

3.10 E-mail and texting have created an extremely cost efficient means for advertisers to communicate directly with consumers. They help to create awareness of a brand, proactively provide sales promotion messages to consumers, and enable communication with existing customers.

Mobile

3.11 2.1% of UK adults used the mobile web to shop in 2009[93] and mobile advertising grew 32.2% in 2009 from the previous year to £37m.[94] While this may appear small, it is worth noting that the spend volume is already higher than online was at the same level of maturity and that mobile advertising is expected to grow dramatically in the near future (see also Attachment 1 regarding increasing mobile internet speeds).

3.12 Future growth of mobile advertising will come through a number of areas. Analysis Mason[95] predicted in August 2010 that non-voice and non-text content and applications will comprise the main source of mobile revenue growth in Europe, growing from €12 billion in 2009 to €25 billion in 2015. In this area, m-commerce options such as the Ocado and Amazon applications (which enable consumers to order goods using their smartphones), will increase in importance.

3.13 According to Analysis Mason, most of the growth in mobile content and applications revenues will be accounted for by internet browsing and data access, as a result of the wide availability of "data bundles" which give subscribers almost unlimited mobile internet access, increasing data capacity and speeds, and the improved smartphone browsing experience. Therefore, as mobile browsing and access to mobile content and applications increases, so mobile advertising will grow.

3.14 Apple is one of the leaders in the mobile advertising space, and its innovations will also promote growth. On the back of the successful iPhone launches, Apple released the iAd platform in the UK in October 2010. The iAd platform allows advertisers access to the entire UK iPhone audience (approx. 6.4m users at the end of 2010) (see further paragraph 4.14(iii) of this Annex B).

---

[93] Verdict Research.

[94] Internet Advertising Bureau – Mobile Advertising Expenditure Study 2009

[95] See Analysis Mason, Mobile content and applications in Europe: forecasts and analysis 2010–2015, 24 August 2010.

Social networking

3.15 Social networking has been another area of explosive growth. Sites such as Facebook and Google+ offer a novel and unrivalled opportunity for people to network and socialise online. This can present advertisers with an ability to develop engagement with their brands and products – as users of social networks engage in discussions about the products and services that matter to them.

3.16 UKOM[96] reports that an average UK internet user spends 25% of their internet time engaged in social networks, a growth of 16% over the last 2 years.[97] Given the amount of time users spend engaging with social networks, they create very significant opportunities for advertisers.

E-commerce

3.17 E-commerce – through online shopping sites such as Amazon – has grown exponentially. As consumers increasingly purchase products online, online becomes the most obvious place to try and influence purchasing decisions as it is as close as possible to the retail transaction. E-commerce also offers significant marketing opportunities through sophisticated targeting based on observed behaviour (e.g. shopping recommendations based on recent purchases and browsing activity).

3.18 Between 2007 and 2010, the number of monthly online buyers rose from 19.7 million to 27.2 million.[98] eMarketer (an aggregator of Digital/Online Research which covers 4,000 industry sources) estimated that over two-thirds of UK internet users aged 14+ bought something online at least once per month in 2010.

3.19 Online sales growth will continue to outpace growth in overall retail sales, as more shoppers use the web to save time, benefit from the cheaper (and readily comparable) prices, and buy items not readily available in nearby physical stores.

Video sharing and UGC content

3.20 One of the most significant areas of online growth relates to the explosion in production and consumption of user generated content. Video-sharing websites such as YouTube[99] (now the third most visited website behind Google and Facebook) give users the ability to upload, share and view videos.

---

[96] UKOM APS (Audience Planning System) is the audience measurement system for UK Online Media.

[97] Comscore/GSMA MMM April 2010, UKOM July 2010

[98] Forrester, UK ecommerce Forecast 2006-2011

[99] Founded in 2005 and owned by Google since November 2006. The site has grown exponentially since its official launch in November 2005. 48 hours of video are uploaded every minute (i.e. 8 years per day). Source: http://youtube-global.blogspot.com/2011/05/thanks-youtube-community-for-two-big.html.

3.21 Although YouTube was originally the domain of individuals uploading user-generated content, it is increasingly being used by corporate entities as a source of revenues. For instance:

(i) A number of content owners – including Channel 4 and Five – have agreed content deals that involve the broadcasters' content hosted in full on YouTube.

(ii) YouTube and other video sites are used increasingly by brands and advertisers for "viral marketing". The networking effect of the internet makes such techniques particularly useful as promotional video clips are easily shared by individual users and are linked to by other websites. They are also measurable in terms of reach.

(iii) In a recent article, Business Review Europe noted the particular successes of viral marketing (citing examples from notable campaigns by international brands such as Volkswagen, Microsoft Xbox 360 and Levi's):

"*Video marketing is so popular with advertisers and companies owing to its relatively low cost, its ability to spread quickly and its organic nature. Via social media platforms consumers often share the message and publicise a good video campaign for you and therefore it feels less manufactured. Many marketers and brands are now stepping up their use of video content as a means of increasing awareness amongst their target audience. Business Review Europe and Verridian – a professional services company that facilitates improvements in business performance – teamed up to present some of the best examples of successful online video campaigns and looks into the reasons they went viral*". [100]

(iv) Many brands are now experimenting with "YouTube Brand Channels" – a new advertising platform that allows advertisers to create their own brand channel. This enables advertisers to create and share their own films, advertisements, retail offers and broadcast whatever they want and represents an innovative move away from the traditional 30 second TV advert. Such brand channels may for example allow consumers to choose which films (i.e. adverts) they want to watch, get specific warranty information or follow the brand on Facebook and Twitter as well as linking to the manufacturer's website.

Multi-screen viewing

3.22 The internet is also coming to the TV screen itself. YouView will bring internet-delivered content to the TV screen and a number of other internet-connected services are set to revolutionise the TV viewing experience (see e.g. paragraph 17.7(v) of PART B).

---

[100] *How to make your advertising campaign 'go viral' online* (http://www.businessrevieweurope.eu/marketing/viral/how-to-make-your-advertising-campaign-go-viral-online).

3.23 BIGresearch (a leading online market intelligence and internet market research company) has found evidence both of multi-screen use and of consumers accessing content through multiple devices. Specifically, they state the following:[101]

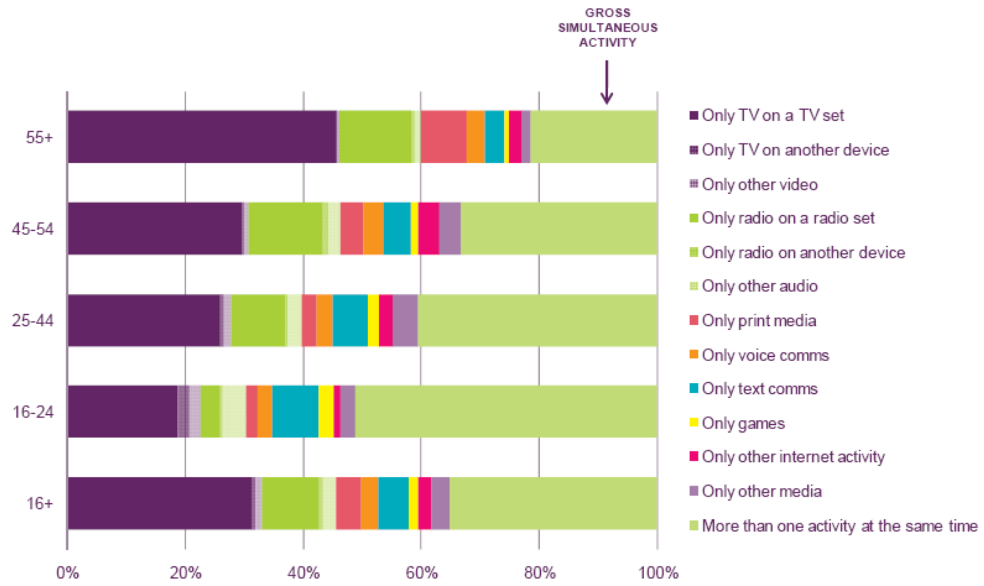
(i) 79% of media users consume more than one medium at a time.

(ii) 69% of UK sports fans used their laptop, whilst watching a World Cup game.

(iii) In the past year the number of people watching TV online has grown by 600%.

3.24 This is consistent with Ofcom research (see Figure 3.1 of this Annex B) regarding media use split by different types of activity, and whether they were carried out on their own or concurrently with other media activities. We see that a significant proportion of people (at least 20%) in each demographic use two or more media simultaneously.

Figure 3.1
Proportion of all media used, split by individual solus activities and all simultaneous activity

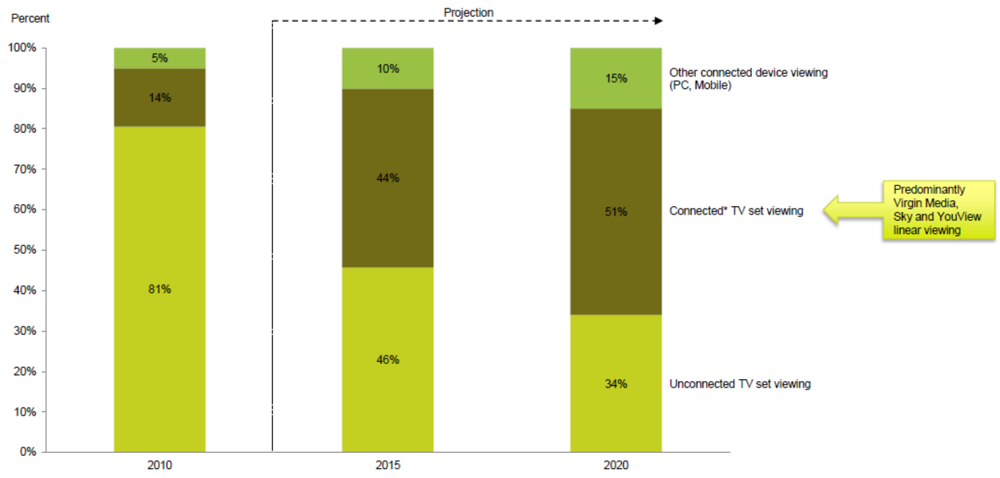


Source: *Ofcom research, base = All respondent days: 16+ = 7966; 16-24s = 1106; 25-44s = 3003; 45-54s = 1484; 55+ = 2373*

3.25 Multi-screen viewing is set to increase. By 2020, around two-thirds of all UK television viewing will be to a broadband-connected TV set. This compares to just under 20% today (see Figure 3.2 of this Annex B).

[101] BIG Research – Simultaneous Media Survey Report 2009

Figure 3.2
Total UK audiovisual viewing hours by type of connectivity



Source: *Oliver & Ohlbaum Analysis*

Note: Connected TV sets are TV sets / set-top boxes directly connected to a broadband internet service enabling the direct delivery of on-demand content to the TV screen via an EPG.

4. Key implications of these changes

Mass reach

4.1 In 2000 the only mass-reach media were TV, print media and radio. Now, many popular websites (including Google, Facebook and YouTube) reach global audiences and have mass reach in individual countries. The online space therefore offers advertisers a wealth of new ways to achieve mass exposure.

4.2 Table 4.1 of this Annex B illustrates how internet platforms and services are now achieving mass reach (see also paragraph 4.13 of this Annex B for examples of specific advertising campaigns which were able to reach mass audiences using only online tools). This has had a profound impact on the way that major brands and advertisers use the online space.

Table 4.1
Top 20 Web Brands in the UK, Ranked by Unique Visitors

Web brand	Rank (Jul 10)	Unique Audience (000)
Google	1	33,924
MSN/WindowsLive/Bing	2	27,704
Facebook	3	25,054
Yahoo!	4	21,255
BBC	5	20,199
eBay	6	17,256
YouTube	7	17,032
Microsoft	8	16,751
Amazon	9	15,021
Wikipedia	10	13,920
Apple	11	11,372
Ask Search Network	12	9,699
The National Lottery	13	9,396
AOL Media Network	14	8,304
Associated Newspapers	15	7,991

Source: UK Active Online Unilever 39,119K; Source UKOM APS, July 10 (Internet Applications Included, Home & Work)

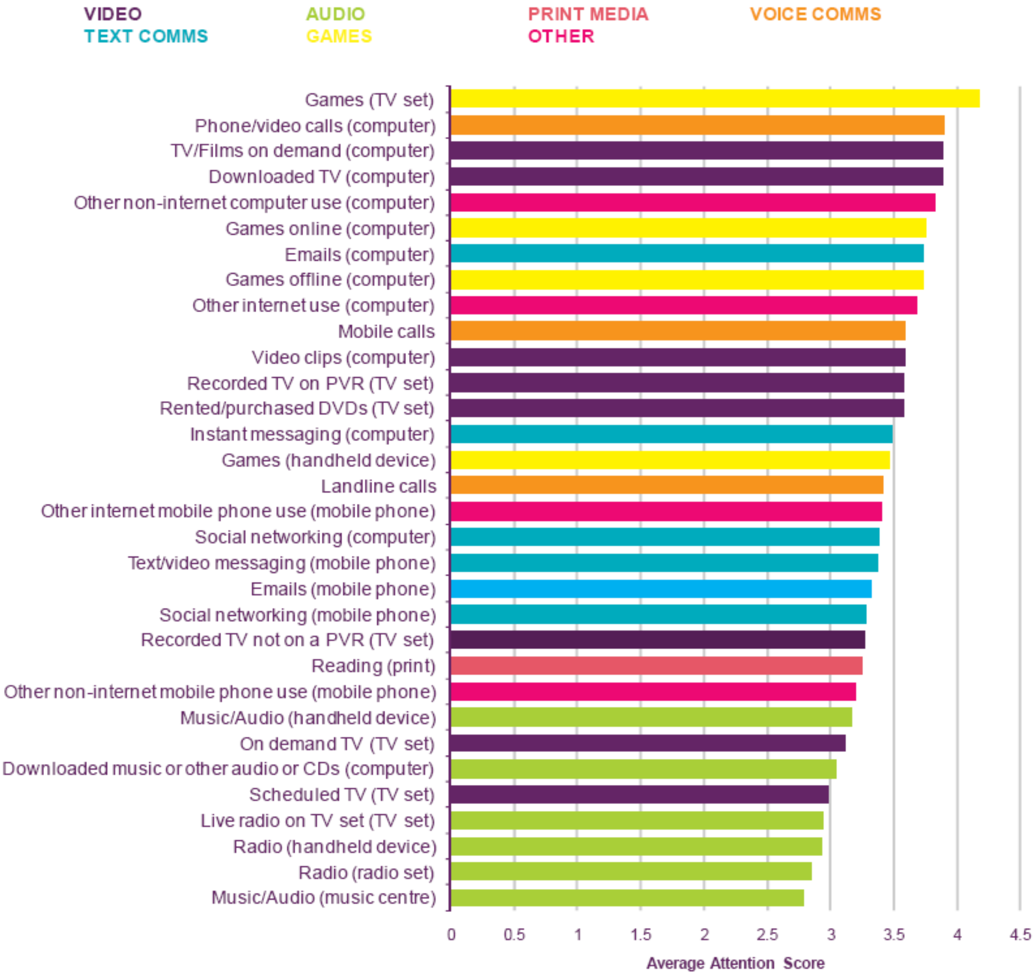
Targeting and engagement[102]

4.3 Online advertising is far more targeted than broadcast advertising as adverts are delivered to individual users based on behavioural or demographic data. As a result of the interactive nature of the internet, online advertising is also inherently more engaging. It provides advertisers with a "return path" by which the consumer can directly communicate with the advertiser and with immediate tracking statistics to tell advertisers exactly how consumers are engaging with their adverts.

4.4 That consumers are more engaged when online is also borne out by Ofcom research which shows that, in terms of attracting attention, PC-based activities generally attract more attention that TV (other than when TV is used for gaming) and that scheduled TV sits near the bottom of the levels of engagement (see Figure 4.1 of this Annex B).

[102] Note: this section shows that the levels of engagement with internet advertising are in fact very high. This contrasts with paragraph 3.13 of the Consultation which refers to anecdotal thinkbox quotes as evidence for the proposition that *"TV viewers also considered to have a higher level of emotional engagement with TV than any other media"*.

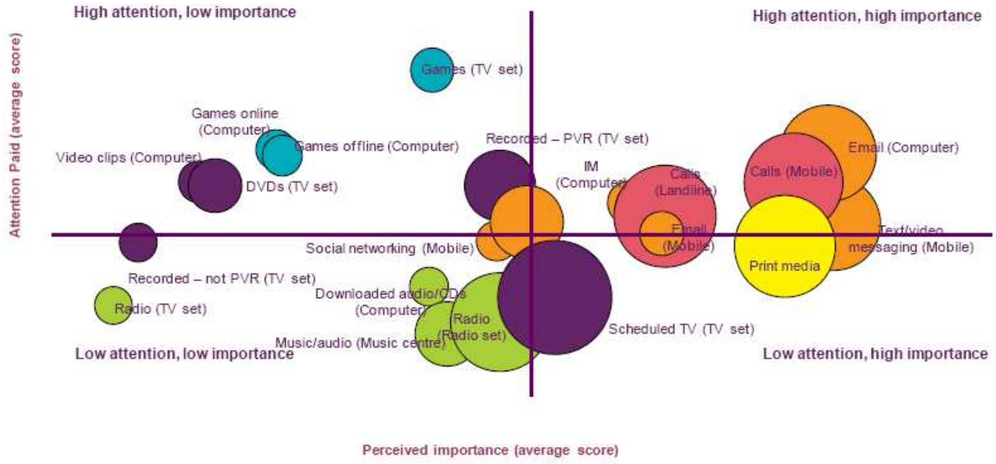
Figure 4.1
Attention level by activity, based on mean scores



Source: Ofcom research, activities with base>50 respondent days.

4.5 Despite relatively low attention levels, TV is nonetheless considered important (see Figure 4.2 of this Annex B), but again ranks lower than e.g. email or text/video messaging.

Figure 4.2
Importance and attention of activities – based on mean scores



Source: *Ofcom research, base = all respondent days: 7966, all activities with base>50 respondent days for attention and base>50 respondents for importance; base: all who ever do activity and have undertaken it in week of research, size of bubble proportional to weekly reach.*

Note: Area of bubble proportionate to weekly reach of activity

<u>Heightened efficiency</u>

4.6 The impact of advertising is notoriously difficult to quantify. As John Wannaker (1838-1922) famously stated "*half my advertising is wasted, I just don't know which half*".

4.7 Advertisers and media buyers have nonetheless sought to measure the reach of their advertising as accurately as possible. Media companies which are able to provide reliable data are therefore attractive to advertisers. TV has traditionally been in a strong position *vis-à-vis* being able to provide data. Online is however starting to surpass that.

4.8 The online world provides advertisers with revolutionary means of allocating their spend, as targeting and tracking consumers has become increasingly more sophisticated and accurate. Advertisers are now able to track a consumer in real time throughout their "digital journey", providing the opportunity for customised advertising messaging. The ability to target advertising spend far more effectively has encouraged spend online and has provided digital media owners with the confidence and knowledge that performance-based advertising charging arrangements are profitable models, and are ones that traditional media owners will have difficulty in replicating.

4.9 In addition, the simplicity of online advertising provides a more efficient model than traditional broadcast advertising. Online advertising is therefore comparatively cheaper whilst still securing the necessary mass reach.

Impact of online advertising

4.10 The benefits of online advertising outlined above have attracted huge numbers of advertisers – including some of the world's largest companies – to spend more on digital. By way of example:

(i) In early 2009 General Motors announced that it would be spending US$1.5 billion (37% of its global budget) online.[103]

(ii) GM announced they would double their online advertising spend. As Joel Ewanick, VP Marketing of Hyundai put it: *"Online is getting to the point where it may be more important than the 30 second TV spot."*[104]

(iii) P&G (the world's largest advertiser) announced that digital spend would be increased from 2% to 20% of total advertising budgets (including in the UK) within two years.[105] [106]

(iv) In June 2010 Keith Weed (Unilever CMO) announced that digital spend was to double with immediate effect[107] and organised a digital brand brainstorm trip for the top 30 Unilever marketers where they spent time with internet companies understanding the changes afoot and the opportunities they provided. That trip resulted in a global multi-million dollar media deal with Apple and its new iAd platform.

4.11 The growth in online advertising in the UK is again consistent with the broader technological landscape (see Figure 2.2 and Figure 2.3 of this Annex B). In particular, it is striking that the UK leads the way in the rise of internet advertising and in the decline of television's share of all advertising revenues. These trends are illustrated below in Figure 4.3 of this Annex B.

[103] As reported in Advertising Age March 2009

[104] As reported in AdAge 2010.

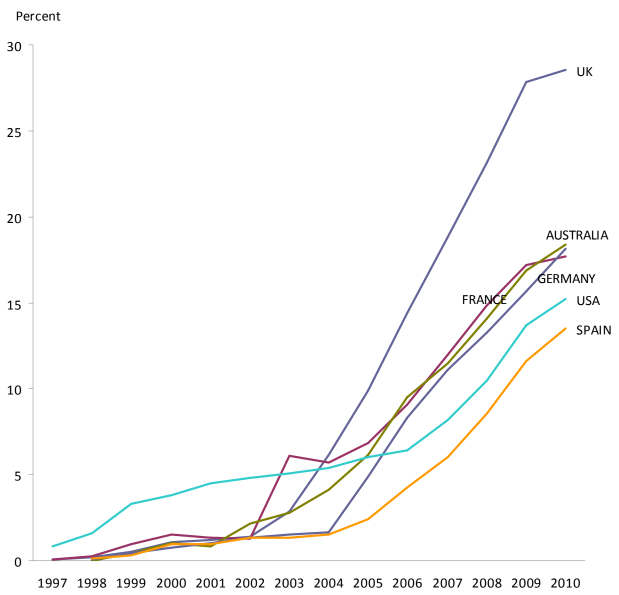
[105] As reported in AdAge 2009.

[106] We note also that Google has a job share scheme with P&G which allows secondments in both directions; further demonstrating the commitment that new media companies are willing to make in their quest to gain advertising monies.

[107] Reported in Advertising Age June 2010.

Figure 4.3

Internet advertising spend as a proportion of all advertising, 1997 to 2010 (%)



Percentage point change in TV as a proportion of all advertising, 1997 to 2010 (%)

Source: *ZenithOptimedia October 2009, Oliver & Ohlbaum Analysis. Note: all underlying data is in local currency in nominal terms.*

4.12 This movement is due not only to the advantages that digital media provides in terms of targeting and effectiveness (and therefore ROI) but also the realisation that internet channels can be used to build brands efficiently and effectively.

4.13 By way of illustration of the impact of online advertising sales:

(i) **Old Spice:** Old Spice had for many years been seen as a dying brand despite numerous attempts by P&G over the last two decades to resurrect the brand using traditional media platforms. In 2010, P&G decided to re-launch the brand, using digital (and specifically social) media. The aim of the campaign was to engage both men and women and generate conversation around body wash. When it was launched online, the campaign managed to capture 75% of all conversations in the male hygiene category (measured by analysing all internet mentions that relate to male hygiene (blogs, YouTube, search, etc.)). But the campaign didn't stop there. Over 3 days, a team of creatives, digital strategists, developers and producers filmed 180 hours of footage, around the clock, creating videos and responding directly to fans and celebrities in near real time. The results of that strategy are summarised below:

(a) On day 1 the campaign received almost 6 million views

(b) On day 2 Old Spice had 8 of the 11 most popular videos online

(c) On day 3 the campaign had reached over 20 million views

(d) After the first week Old Spice had over 40 million views

(e) The Old Spice twitter following increased 2700%

(f) Facebook fan interaction was up 800%

(g) Oldspice.com website traffic was up 300%

(h) In the first 3 months since launch, sales were up 55%. Old Spice became the #1 body wash brand for men[108]

(ii) **Marmite:** Unilever used online channels to recruit Marmite advocates (called "Marmarati"), to taste test and develop new product variants that could be launched under the Marmite brand. This digital involvement generated noise and support for the brand that resulted in a highly successful new product extension which launched without any TV advertising support. Unilever reported that there were 650,000 people engaged in the campaign from an initial 30.[109] The Marmite brand now has over half a million Facebook fans that continue to interact with the brand on a daily basis.

(iii) **Burger King Whopper:** In 2009, Burger King launched its first 100% online campaign, centred around the BK Whopper (at the time experiencing declining sales). The campaign partnered with Facebook and invited users to demonstrate what was more important to them, a friend or a BK Whopper, by "unfriending" 10 friends in order to receive a free Whopper. Within 24 hours the campaign had achieved its targets, well ahead of expectations, and was the beginning of the BK Whopper resurgence. Facebook and Burger King closed the campaign when 250,000 consumers had qualified for a Whopper, only 7 days after launching.[110]

(iv) **Study for Nestle by the Internet Advertising Bureau (UK Trade Body for online and Mobile):** Demonstrated that mobile advertising increased brand awareness of KitKat by 36%.

4.14 Digital media companies are also actively promoting their offer in new and innovative ways to encourage additional spend by advertisers. By way of illustration:

(i) Google trains brand teams on Google products in order to foster direct relationships. This includes a "Google AdWords Online Classroom" which guides advertisers on how to plan, buy and measure search campaigns.

---

[108] Wieden & Kennedy Case Study Results – August 2010

[109] As reported by Contagious Magazine issue 22 - Case Study

[110] Whopper Sacrifice Case Study; Crispin, Porter & Bogusky BK Advertising Agency

(ii) Publicis Group (including Starcom and ZenithOptimedia), the largest buyer of digital media[111] fostered a joint partnership with Google, centred around advertising analytics and performance. This partnership gives Publicis unique access to all of the Google initiatives, providing advertisers with knowledge about consumer online behavioural patterns, and offering a new level of consumer intelligence based on user actions and interactions online.

(iii) Digital media companies are also beginning to offer production alongside and often inclusive of the media deal. For example, Facebook offers production support for designing brand pages, Google provides technical support for their suite of products, and Apple has started to provide technical engineers to build the iAd advertising for brands – these services are offered direct to the advertiser, rather than via agencies. [112]

(iv) Partnerships are also starting between the big players (including Google, YouTube, Facebook, Apple, Microsoft Advertising) and global advertisers. For example: Facebook and P&G have just created a global strategic alliance which extends a traditional advertising arrangement to include creation of and access to shared behavioural data, joint development of creative execution and commitment to explore new business models such as e-commerce within the Facebook environment – a first for the industry. Google and Heineken have also recently signed a multi-million Euro partnership to collaborate on digital advertising. This is the first such long-term agreement between Google and a large brand but Google expects more brands to *"take the opportunity to lever partnerships with [Google] to build their capability and innovate"*.[113]

---

[111] Publicis Group Annual Report 2009.

[112] iAd allows advertisers to deliver a brand experience to an individual or to a global audience at the click of a button. Entry level media spend on iAd is between £1 million-£10 million. It is currently oversubscribed.

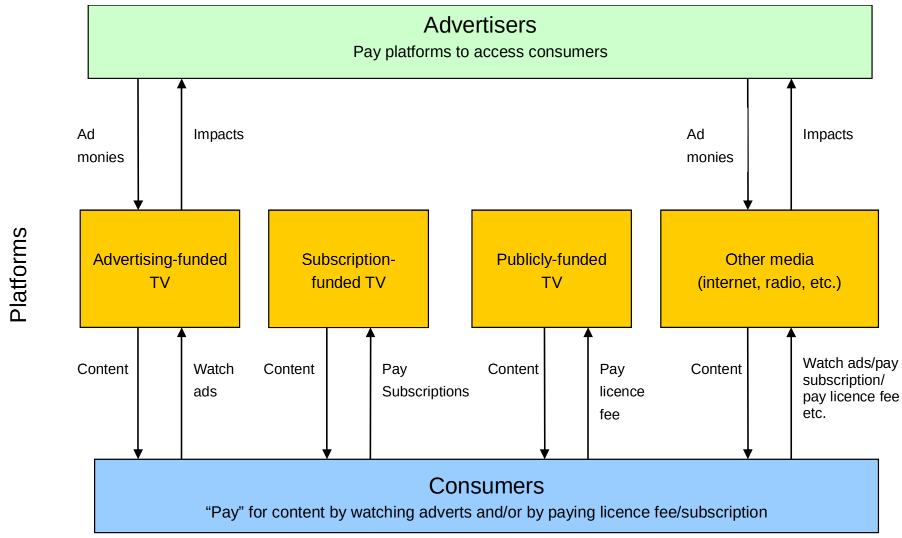
[113] *Google and Heineken seal ad partnership*, 30 June 2011 (http://www.ft.com/cms/s/0/55f81cd8-a297-11e0-83fc-00144feabdc0.html#axzz1Ro0RUuTx).

Annex C – The Markets for Viewers and Content

1. The UK market for viewers is highly competitive

1.1 The success of advertising-funded TV channels lies in their viewers: they need to attract audiences in order to attract advertisers. In considering any intervention into the advertising-funding of TV, it is therefore crucial to take account of this two-sided nature of broadcasters' businesses. How advertisers use broadcasters and other content platforms to reach consumers is illustrated in Figure 1.1 of this Annex C:

Figure 1.1



Source: *ITV.*

Note: Some platforms receive funding from a combination of sources.

1.2 Content providers are essentially competing with each other for a share of the leisure time of viewers. The number of options that viewers have for home entertainment has increased exponentially in recent years. For example:

(i) The number of TV channels has increased dramatically (see paragraph 6.4 of PART A);

(ii) The internet has developed as a medium of education, information and entertainment;[114]

(iii) Gaming has increased; and

[114] Ofcom Communications Market Report 2010: the average person spends over four hours per week watching non-linear / on-demand audiovisual content across a variety of platforms and devices (17% of all viewing).

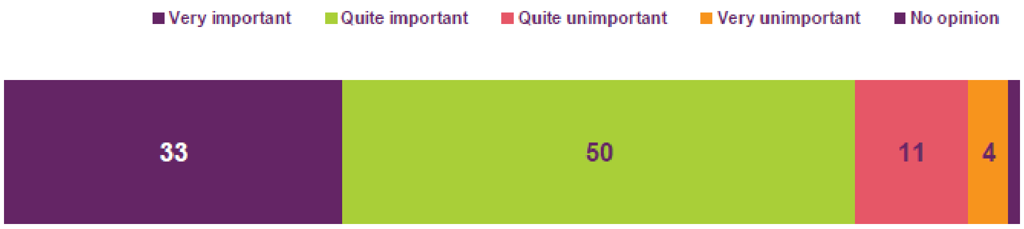
(iv) VOD and PVR have been developed.[115]

1.3 As competition for viewer attention develops and strengthens, investment in high quality content becomes increasingly important to attract viewers, and therefore to provide value to advertisers. Without an ability to attract viewers a platform's value to advertisers will decrease.

2. Viewers particularly value original UK TV content

2.1 The importance of UK-originated content to both viewers and policy-makers has been clearly recognised by Ofcom. Specifically, the PSB Review research showed that viewers value high quality UK-originated content, and that they associate such content with PSB channels. As Figure 2.1 of this Annex C shows, 83% of people either agree or strongly agree that it is important that the main TV channels provide programmes made in the UK that reflect life in the UK.[116]

Figure 2.1:
Ofcom survey: responses to *"How important is it that the programmes that are made in the UK and reflect life in the UK are shown on the main TV channels as a whole?"*



Source: *PSB Review Phase 1 quantitative survey among 2,260 people aged 16+ in the UK.*

2.2 Expanding on the above, Ofcom's research also found that:[117]

(i) Participants felt that programmes made in the UK better reflected life in the UK – without UK programmes, UK cultural identities may be lost (e.g. perceived "Americanisation" of language).

(ii) Although support for imported programmes has risen since 2003,[118] the majority of people still want UK-made and UK-focused programmes on the main TV

---

[115] Ofcom Communications Market Report 2010: time-shifted television viewing accounted for 5.9% of all viewing in 2009, more than three times the amount in 2006; and in Q1 2010 around 30% of adults with internet access watched catch-up TV, up from 23% a year earlier.

[116] Ofcom's Second PSB Review Phase 2 consultation document, Figure 3.

[117] Source: slide 87 of the research annex published alongside Phase 1 of Ofcom's second PSB Review.

channels. That is broadly consistent with viewing figures: PSB-owned channels are still the most popular.

(iii) UK content was felt to be particularly important for certain programme types (in particular news, current affairs, factual and learning programmes, children's programmes and drama).

(iv) The onus for content to reflect UK identities was seen to fall particularly on the BBC, but also on the others PSBs. Over three quarters (77%) agree it is important for the BBC to show a high proportion of programmes which reflect life in the UK (compared to 65% for ITV1, 57% for Channel 4 and 48% for Five).

2.3 The very significant importance of originated content to viewers has also driven Ofcom and Government's policy thinking. For example, Ofcom has stated that in future the primary public service role of commercial networks such as ITV1 should be *"through sustaining a substantial investment in high quality UK programming, providing competition to the BBC, Channel 4 and the digital market"*.[119]

3. Competition for quality is a key feature of UK broadcasting

Importance of quality recognised by broadcasters

3.1 Given that viewers value high quality UK-originated content it is not surprising that in a competitive market there are a number of broadcasters who cater effectively for this viewer preference.

3.2 As noted in *Creative UK*:

"Rising competition for audience attention at home and abroad means that content providers must continually strive to produce something exciting, new and different to attract audiences. High value productions are an important means of differentiating TV content from the vast volumes of user generated content available on the internet.

Often this means investing more in content, not less. More lavish production budgets for dramas, costly location filming for natural history films and expensive talent for entertainment shows. It may mean that more programmes have to be piloted, at greater cost, to find those elusive successes. For every stand out hit, like Downton Abbey, there are several others no less expensive, which fail to make their mark with demanding audiences".

---

[118] Many participants believed that there is a place for high quality programming from overseas which provides increased diversity and choice and different perspectives of the world (naming programmes such as CSI, Six Feet Under, The Sopranos and The Simpsons as examples).

[119] Paragraph 1.57 of Ofcom PSB Review final statement, January 2009.

3.3 The importance of maintaining high quality programming is also evident from broadcasters' investment strategies. For example ITV has minimised cuts in programme expenditure. Between 2005 and 2009, in real terms, ITV cut its non-programming costs by 29%,[120] but its programming costs by only 13%.

Competition between broadcasters

3.4 A notable feature of the UK television market is the significant state intervention in the form of a publicly owned and funded BBC and a publicly owned Channel 4.

3.5 The BBC has a 33% share of viewing[121] and (via the licence fee) a secure source of funding which allows it to invest in high quality UK programming. This in turn incentivises competing broadcasters (particularly close competitors such as ITV1 and Channel 4) to invest in the same high quality UK programming in order to avoid losing viewers to the BBC. Ofcom analysis shows that in 2010 total programming spend by PSB networks was £2.9bn. Of this, £2.5bn was originated content (split £1.3bn by the BBC and £1.1bn by commercial PSBs) and £0.4bn was acquisition/repeats (split £0.1bn by the BBC and £0.3bn by commercial PSBs).

3.6 The result of this continual investment by UK commercial PSB broadcasters in order to increase, or even just maintain, their viewership, has been a significant increase in the ratio of their spend on first run originated programming to revenue which has now reached a similar level to that of the non-profit making BBC (see Figure 3.1 of this Annex C). As Ofcom noted in its recent PSB Annual Report: *"the commercial PSB channels increased spend as a proportion of revenue from 36% in 1998 to 56% in 2009; the ratio declined to 50% in 2010, primarily as a result of rising commercial income brought about by the television advertising recovery. The BBC's ratio fell from 62% in 1998 to 57% in 2009, rising to 60% in 2010"*.[122] Ofcom suggests a number of factors which may have influenced this trend including: rising expenditure on non-content costs (e.g. new digital platforms); and content spending strategies not yet catching up with declining advertising revenue.

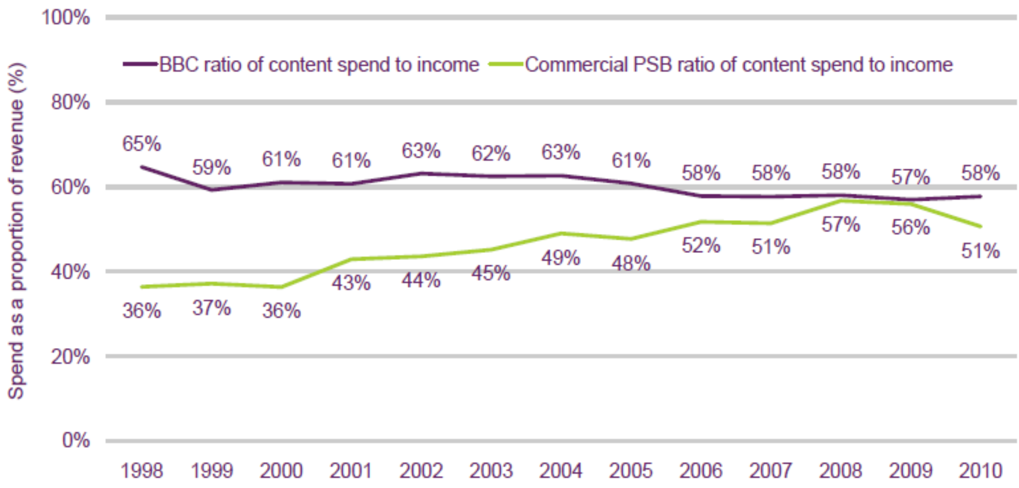
---

[120] These include the non-programming costs of news and regional programmes, regulatory costs/licence fees, industry costs, transmission and other costs, as well as marketing costs.

[121] BARB. Figure relates to 2010.

[122] Ofcom Public Service Broadcasting Annual Report 2011 at page 8 (http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/psb-review/psb2011/psb-summary-A.pdf)

Figure 3.1:
PSB First run origination programming spend – ratio of spend to revenue



Source: *Broadcasters and Ofcom estimates drawing on data from the BBC's Annual Reports and Accounts.*

Notes: [1] Spend is all day, all genres. It includes all spending on networked output by the BBC, ITV1, Channel 4 and Five. It also includes BBC, stv, ITV1 and UTV spending on programmes for viewers in the nations and regions and the BBC's spend on programmes for S4C and BBC Alba.

[2] BBC income is based on Ofcom estimates of total licence fee revenue that is spent on TV-related services which include content, distribution, and infrastructure spending, and a proportionate share of remaining overheads.

3.7 Moreover, increases in content investment have also been seen outside the PSB-owned channels. As noted in a March 2011 report for the Commercial Broadcasters Association ("**COBA**")[123] between 2008 and 2009 the content investment of COBA members increased from £2,158m to £2,345m (an increase of 8.7%). As the report goes on to note: *"Of the 2,345 million spend by COBA members, 70% or £1,639m, was invested in the UK in 2009 through fully funded originations, co-funded originations, production and acquisitions/rights/payments to third party channels. This represents an increase of 5.8% in total UK content investment compared to £1,549m in 2008"*.[124]

3.8 Ofcom recognises the pressure the BBC puts on commercial broadcasters to invest at paragraph 3.21 of its Consultation: *"the greater the quality of programming on the BBC, the more commercial broadcasters will be incentivised to invest in their own quality programming to ensure viewers do not switch away"*.

---

[123] COBA *"is the UK industry body for commercial broadcasters who are independent of public funding or incentives. Its members include all of the major non-public service broadcasters, as well as smaller broadcasters who provide targeted programming to niche audiences"*.

[124] The Commercial Broadcasters Association's Content Investment – A report by Deloitte for the Commercial Broadcasters Association. 17 March 2011 at page 4.

3.9 However, this is only half the story – the incentive to invest cuts both ways as Ofcom itself has recognised in the past when it described the relationship between the BBC and the commercial broadcasters as creating effective "competition for quality" in the UK television market. As Ofcom observed in the first PSB Review: *"the BBC kept ITV honest; ITV kept the BBC on its toes"*.[125]

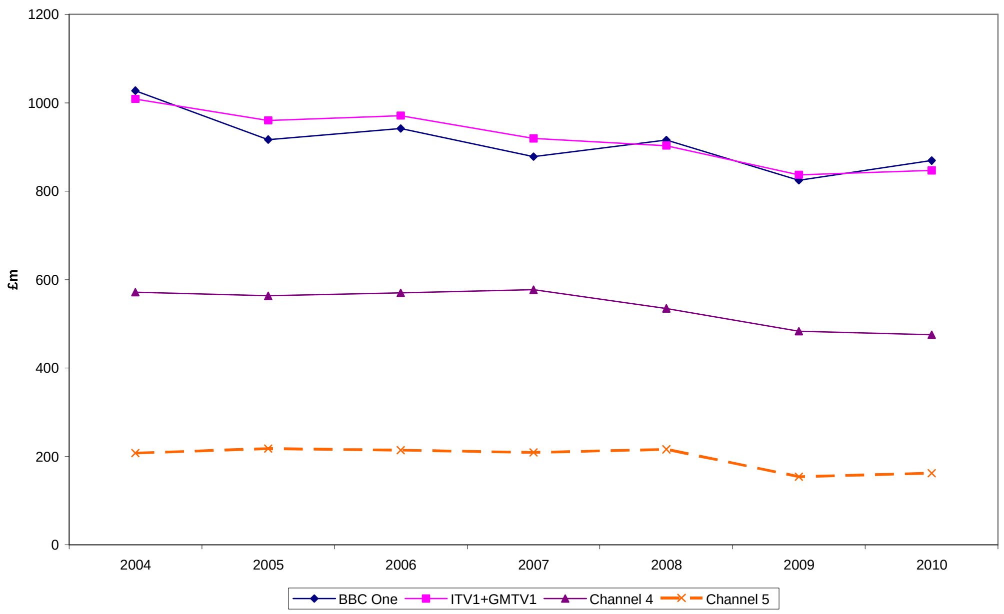
3.10 Looking specifically at the close competition for viewers between BBC1 and ITV1, we see that the level and trajectory of their programme expenditure is similar. For example:

(i) In 2004, ITV1 spent £982m (in 2009 prices), compared with BBC1's £1,001m.

(ii) In 2009, ITV1's spend had fallen to £810m (18% down on 2004), compared with the BBC1's £799m (20% down on 2004).

3.11 The similarity in the trajectories of programme spend by BBC1 and ITV1 indicates that each is reacting to the other and hence, each acts as a competitive constraint on the other (see Figure 3.2 of this Annex C).

Figure 3.2:
Network programming spend by channel,
2004–10 (£m 2010 prices)



Source: *Ofcom PSB Annual Report 2011.*

[125] *Ofcom Review of Public Service Television Broadcasting. Phase 1 – Is Television Special?* (April 2004)

Investment more and more costly for commercial broadcasters

3.12 However, as [✂] of this Annex C shows, ITV1's costs of reaching viewers (measured in terms of the costs of achieving each percentage point of SOCI) have been rising since 1995. At least in part, this reflects the continued increased competition for viewers. In order to remain competitive with the BBC in the markets for viewers and for content, ITV needs to recover these additional costs (principally from advertisers).

[✂]

3.13 Moreover, the pressure on commercial broadcasters is set to intensify as both the BBC and Sky plan to increase their own focus on programming investment:

(i) As stated in the BBC's recent Strategy Review:

"By 2012/13, many of the BBC's current major infrastructure projects – including digital television switchover – will be complete. This will allow the BBC to redirect a higher proportion of the licence fee to its core mission of providing high-quality programmes and services and delivering them to audiences. The BBC should commit to spend from 2013/14 at least 90p in every licence fee pound on the creation and distribution of high-quality content, cutting its overhead and infrastructure costs (which have reduced by 50% in the past decade) by a further quarter by the end of the Charter in 2016. Within that 90p guarantee, at least 80p in every licence fee pound should be spent on content creation itself". [126]

(ii) Sky has made public its strategy to invest in *"standout content"*, including more original UK productions and a multi-year partnership with HBO, reflecting a focus on high quality drama in the schedule.[127] More generally, Sky has recently changed its strategy of broadcasting mainly US imports, sports and films by committing to increase its spend on UK originations from £380 million in 2011 to £600 million in 2014.[128] This provides further support for the proposition that viewers value UK content; as a rational profit-maximising firm, Sky would only invest more in UK content if it considered that it would increase the total willingness to pay for its services. We note for example a recent comments by Jeremy Darroch, CEO of BSkyB:

"The motivation is very simple and, again, it is driven by a purely commercial mindset. Home-grown content resonates strongly and we believe we can both

---

[126] BBC (2010), 'BBC Strategy Review: BBC Executive's Summary', p. 8.

[127] Sky (2010), Sky results as at 30th June 2010.

[128] Sky 2011 Annual Report.

bring more quality and value to existing customers, while also reaching out to more people who haven't yet chosen pay TV".[129]

"As a company, we believe in the value of content. Our business was founded on the belief that viewers would respond to increased choice and would be prepared to pay for it. That still holds true today. It's why we expect to spend more than £2 billion on-screen this year, two-thirds of which will be spent in the UK. In the last three financial years, that figure has grown by £300 million and we expect it to grow by at least another £300 million by June 2013. Putting that in context, over that period we'll have grown our on-screen investment by more than Channel 4's annual programme budget. And, again, most of that extra money will flow to the UK." [130]

3.14 The healthy competition between the commercial broadcasters and the BBC to attract viewers by investing in content cannot be taken for granted. The ability of advertising-funded broadcasters to maintain that degree of competition and innovation in content depends on being able to generate sufficient revenues from advertisers. If commercial broadcasters become less able to attract those revenues, their ability to compete with the BBC and Sky – and thus to incentivise the BBC and Sky to continue their own investment – will be curtailed. The potential for a downward spiral in content investment and innovation should be a critical factor in any regulatory intervention into TV advertising.

3.15 That the competitive position in UK TV cannot be taken for granted is illustrated by the current position in UK radio where the BBC is significantly better funded than the commercial sector as a whole and achieves a substantially higher audience share than the commercial sector. The lack of direct competition to the BBC is particularly acute in national radio where listening to national services (58% of total listening) is split 80:20 (BBC:commercial radio).

3.16 Moreover, and again in contrast to TV, entry and innovation in the radio market appears to be limited. So, for example, the growth of DAB digital radio has been slow as has the growth in digital listening as a proportion of total listening. Indeed, such has been the slow pace of growth that the target for digital switchover in radio appears to be receding into the distance (in contrast to TV that will complete switchover next year).

3.17 There has been little success with new station entry either. For example, of the eight new national commercial radio services launched on the first national commercial multiplex D1 (launched in 1999) only one, Planet Rock, is still on air. Services that closed included Bloomberg News, ITN News, One Word, Primetime, Capital Life, Core and The Jazz (the last three owned by the major radio operator GCAP). The proposals

---

[129] In a speech entitled "Investment, growth and policy for the creative industries", delivered on 8 June 2011.

[130] ACT *Content & Consumers – How Commercial Broadcasters Have Updated Their Business Models For The Online World* page 31.

for a variety of new national digital radio stations on the D2 multiplex (licensed to the 4 Digital Group) offered the prospect of significant increase in choice.[131] However, Channel 4 decided to withdraw in the face of financial pressures and none of the other third party channels continued with their launch plans even though there was capacity on the D1 multiplex.

4. UK does better at meeting viewer preferences

4.1 The UK has a strong record on quality and original content investment when compared internationally (see further Attachment 2).

4.2 We note in particular that:

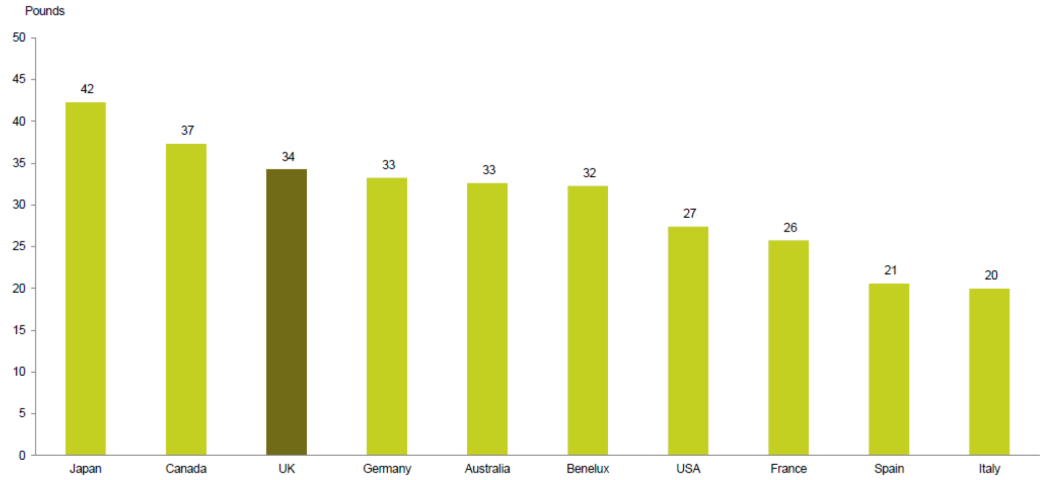
(i) The UK has an especially high level of spend on originations per capita, relative to other major developed markets (see Figure 4.1 of this Annex C).

(ii) 48% of all original content investment in the UK is by advertising funded commercial network channels – this is a higher proportion than all markets apart from the US and Spain (see Figure 4.2 of this Annex C).

(iii) The UK's main commercial advertising funded network groups spend more on original indigenous programmes than their peers in all major European markets (see Figure 4.3 of this Annex C).

[131] Lord Gordon of Strathblane (the former CEO of Scottish Radio Holdings CHECK) said that "*A successful application by Channel 4 would breathe life into a somewhat moribund commercial radio market. By contrast, simply more of the same would be an absolute disaster for an industry already suffering from fragmentation and a lack of distinctiveness*".

Figure 4.1:
Originated TV content spend per capita, 2009



Source: *OBS, SNL Kagan, Company report, Oliver & Ohlbaum analysis.*

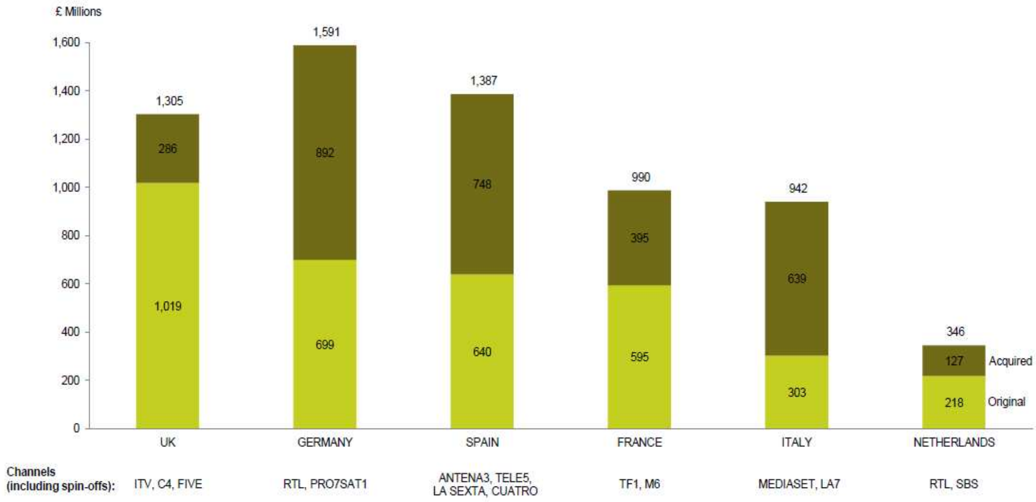
Note: Data exclude spend on news and syndicated programming.

Figure 4.2:
Leading TV originated content markets by type of broadcaster, 2009

Source: *OBS, SNL Kagan, Company report, Oliver & Ohlbaum analysis.*

Note: Data exclude spend on news and syndicated programming.

Figure 4.3:
Leading TV originated content markets by commercial broadcaster, 2009



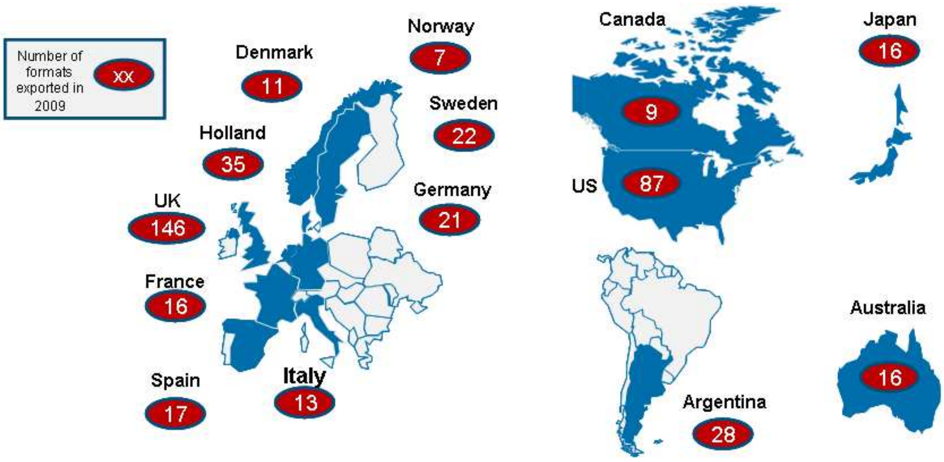
Source:	*OBS, SNL Kagan, Company report, Oliver & Ohlbaum analysis.*
Note:	Data exclude spend on news and syndicated programming.

4.3 On a number of other measures the UK is a highly successful TV market. So, for example, off the back of high levels of investment and competition for quality, the UK is a leading exporter of TV around the world – about a third of exported formats originate in the UK (see Figure 4.4 of this Annex C). In 2009, the international sale of UK programmes and related activities was worth £1.3bn; more than eight times the size of its French counterpart and 38 times that of Spain. Even in the economic downturn, the value of UK TV exports increased by 9% between 2008 and 2009.[132]

---

[132] *Ofcom International Communications Market Report 2010* at page 62.

Figure 4.4:
Number of formats exported in 2009



Source: *The Frapa Report 2009: TV Formats to the World.*

5. There are high levels of satisfaction with UK television overall

5.1 That the investment which broadcasters have undertaken is meeting viewer demands is illustrated by the fact that total TV viewing is still very high, despite options for media consumption rapidly proliferating:

(i) Ofcom research shows that average TV viewing per head was 4hrs2mins per day in 2010, up from 3hrs36mins in 2006.

(ii) Ofcom's Digital Day research (published in December 2010) found that TV is the most-used device for media consumption amongst all adults (albeit that 16-24s use computers more).[133]

(iii) Scheduled television reaches over 80% of all adults every day – with daily reach standing at 69% for 16-24s, and rising to 91% for those aged 55+.[134]

(iv) Ofcom's PSB Review research showed that:

(a) Quality is seen by viewers as the most important of the PSB characteristics;[135]

(b) UK origination plays a vital role in delivering PSB purposes;[136] and

---

[133] Ofcom Digital Day chart pack at Figure 15.

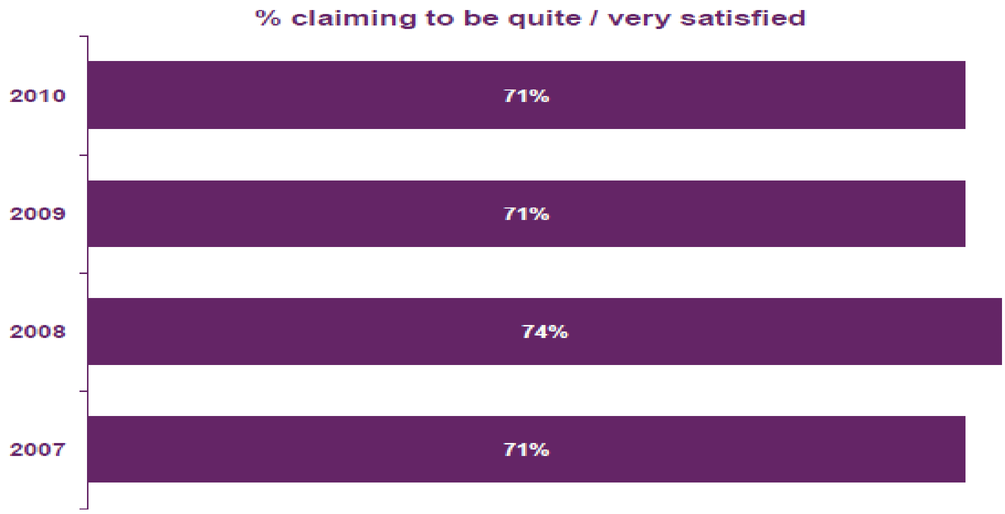
[134] Ofcom Digital Day chart pack at Figure 27.

[135] Ofcom second PSB Review final statement, January 2009 at Figure 2.

(c) Each of the main PSB channels is valued by viewers (with ITV1 rated highly for news, nations/regions news, and high quality dramas and soaps).[137]

5.2 According to Ofcom's PSB Annual Report, more than 70% of UK viewers are satisfied with the PSBs as a whole (see Figure 5.1 of this Annex C). Ofcom's research has also found that viewer satisfaction is consistent across all digital platforms, and regardless of whether or not viewers consume non-linear services. Moreover, viewer satisfaction is even higher among 16-24s than other age groups.[138]

Figure 5.1:
Levels of satisfaction with all the main channels



Source: *Ofcom PSB Tracker, GfK NOP.*

Notes: [1] Main channels means BBC1, BBC2, ITV1, Channel 4 (S4C), Channel 5, BBC3, BBC4, BBC News and BBC Parliament.
[2] Base: all who ever watch any PSB channel.

5.3 This is a hit and miss business: not all investments will in practice attract viewers. ITV has however continued to invest in new content in a bid to attract viewers (see also paragraphs 16.7-16.9 of PART B regarding the challenges of recouping investments). Some examples of recent successful new ITV drama programme launches are:

(i) ITV1 broadcast the most watched new drama in 2010: Downton Abbey. It launched with 9.3m viewers on 26 September, growing to 10.8m viewers for the

---

136 See paragraph 3.5 of Ofcom second PSB Review final statement, January 2009.

137 See paragraph 3.8 of Ofcom second PSB Review final statement, January 2009.

138 See further PSB Report 2011 Information Pack at http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/psb-review/psb2011/psb-audience-opinions-D.pdf.

final episode on 7 November. Downton Abbey was also a VOD success: it was downloaded by 3m VOD viewers in 2010.

(ii) Scott and Bailey (a six-part detective drama) attracted an average of nearly 8m viewers making it the most successful new drama of 2011 so far.

(iii) Marchlands (a five-part drama) averaged over 7m viewers and is the second most successful new drama broadcast in 2011 so far. It has subsequently been released on DVD and to date has sold 25,000 units in the UK.

5.4 Other recent drama productions for ITV which did not live up to expectations include [✂]

6. Does the trading model affect incentives to invest in content?

6.1 All the evidence above shows that ITV and the other commercial PSBs have strong incentives to invest in content (and in particular original UK content) to compete effectively and meet the expressed wishes of viewers and also therefore advertisers.

6.2 In its Consultation at paragraph 6.85 Ofcom argues that the incentives to invest in content are blurred/diminished as a result of the trading mechanism and in particular the bundling of impacts and the lack of transparency over the value of any specific programme.

6.3 Under the annual deal rounds:

(i) The broadcaster commits to a delivery of discount versus SAP, together with the promise of other elements of value (for simplicity, we focus here on the discount).

(ii) In return, buyers commit to spending a share of the money they spend on television advertising with that broadcaster (with no commitment on the level of that spend).

6.4 Broadcasters therefore have to ensure that the quality of their schedule is sufficient to meet the obligations to which they are contractually committed. Schedules are therefore devised and modified that seek not only to ensure delivery of their discount and other commitments to buyers in that given year, but also to maintain or strengthen the broadcaster's bargaining position in the subsequent year's negotiations.[139]

---

[139] In this regard, it is important to recognise that the value of any specific programme is not related just to the impacts that it delivers. Rather, it may generate externalities that can benefit the channel more broadly. For example, certain genres (e.g. sports) may not be profitable when looked at in isolation, but they may attract a more diverse audience than would otherwise watch a channel, thereby increasing the broader appeal of that channel to advertisers.

6.5 [✂] In order to meet the broadcaster's obligations, it is necessary for both the pre-committed and new commission elements of the schedule to perform.

6.6 The risk of underperformance of any element of the schedule therefore lies with the broadcaster. Once the annual commitments are set, it is for the broadcaster to deliver on those. If it does not, it would be in "deal debt", which means giving advertising capacity for free to that buyer, and/or weakening its negotiating position for the subsequent deal round. This allocation of risk generates efficiencies as broadcasters have greater control over their audiences as they can optimise the programming schedule to mitigate the risk of overtrading and "deal debt".

6.7 The current trading model therefore provides broadcasters with strong incentives to invest in programming and to innovate in order to attract and maintain audiences (and hence also advertisers). Broadcasters – in contrast to advertisers – also consider more fully the long term implications of not innovating in programming. Buyers are inherently more risk averse as to the types of programming they would commit their advertising money to in advance. Changing the trading model so that buyers would be responsible for allocating all of their spend to particular slots would likely have a chilling effect on the level of innovation in content in the UK. Given the current competitive interplay between the advertising-funded channels and the BBC and Sky, any diminution in the compulsion for innovation on the part of the advertising-funded players would be likely to have a chilling effect across the market.

6.8 ITV accepts that the ratchet mechanism under CRR focuses a degree of attention on achieved SOCIs. However, there is no guarantee that other trading mechanisms (such as an auction or ratecard system) would lead to reduced risk aversion, and indeed it is quite possible that other models might actually drive a greater degree of risk aversion. Moreover, ITV notes the evidence provided above showing its continued investment in new formats and new content.

Annex D – OFT cases deciding against referral

- **Newspaper and magazine distribution**

In its September 2009 decision, the OFT confirmed that there were reasonable grounds for suspecting that the conduct of publishers and wholesalers prevented, restricted or distorted competition but that it had decided not to make a market investigation reference. In particular, the OFT did not consider that the market features at issue were likely to persist[140] and thought that the CC would be unable to gather the necessary evidence to enable it to assess the competitive state of the markets and the impact of any remedies to address any adverse effects identified.[141]

- **Isle of Wight ferry services**

In its February 2009 decision, the OFT concluded that there were reasonable grounds for suspecting that barriers to entry and the fact that routes can only support one operator are features of the market which prevent, distort or restrict competition. The OFT nonetheless exercised its discretion not to refer in particular because it considered that there was limited evidence of consumer detriment in terms of price, quality of service, choice or innovation. Further, there did not appear to be a remedy which was appropriate or proportionate to the detriment identified.

- **Equity underwriting**

In January 2011, the OFT found that the market was not working efficiently and identified certain features which provided reasonable grounds for suspecting that competition was being prevented, restricted or distorted. However, the OFT considered it questionable whether these features would persist. The OFT noted that the equity underwriting market had potentially been through an exceptional period, and that it was therefore difficult to assess how it was adjusting as it returned to more typical conditions. The OFT was of the view that the analysis in its report should raise companies' and institutional shareholders' awareness of many of the issues identified in the equity underwriting market and that this increased understanding may incentivise greater shifts in the conduct of companies and institutional shareholders. The OFT identified a number of options for actions by companies and shareholders to drive greater competition. The OFT considered that it would be more efficient and effective for the market to resolve the problems itself.

---

[140] Industry participants had been engaged in self-assessment of their agreements. Where they contained provisions that were not compatible with competition rules, the OFT expected parties to rectify this in line with its 2008 Opinion. Furthermore, as a result of that Opinion, many publishers retendered their distribution agreements and awarded new contracts.

[141] In particular, the OFT felt that the then-existing period of flux meant that it would not be feasible for the CC to obtain the requisite evidence to assess properly how the supply chains were likely to evolve in the short term, and hence the impact and effectiveness of any remedies.

- **Outdoor advertising**

In its February 2011 decision, the OFT concluded that rebate payments[142] between outdoor advertising media owners and specialist buyers have the potential to distort advertising campaigns and increase the price that advertisers pay. The OFT therefore encouraged advertisers to engage more directly with media buyers and seek greater transparency. In particular the OFT urged advertisers to explicitly require pass on of rebates. The OFT declined to refer the market to the CC because: (i) there was an ongoing investigation into street furniture contracts; (ii) the OFT provided guidance to tackle the asymmetry of information between advertisers and specialist buyers and media agencies, and advertisers could use their negotiating power to mitigate the adverse effects from the asymmetry of information; and (iii) the limits on the powers of the CC to make decisions and formulate remedies which may affect trade between member states.

[142] Under agreements between media owners and specialist buyers, the latter receive end of year rebate payments based on gross spend. Media owners also typically negotiate a retrospective, tiered structure to rebate agreements (“rollback”), in which higher volumes are rewarded with higher percentage rebates applying to all the specialist buyer’s spend.

Attachment 1 – The fast pace of change in UK media, a report by Oliver & Ohlbaum

[attached separately]

Attachment 2 – Oliver & Ohlbaum comparison of international television advertising markets

[attached separately]