Submission to the Productivity Commission's inquiry into Australia's broadcasting legislation

Written and Authorised by Andrew Reid for
Victrix Media Pty. Limited

A.C.N. 086 024 277

Submission to the Productivity Commission's inquiry into Australia's broadcasting legislation

Written and Authorised by Andrew Reid
For Victrix Media Pty. Limited

1.0 Introduction

A period of rapid and fundamental economic and social change is undoubtedly underway. Yet though the novelty of 'convergence' and 'digitisation' has dissipated to some extent, the exuberance resonating around new media has not. Some see the direction of change all too confidently while others too readily applaud the hubris and castigate the na-sayers. Critical evaluation is sometimes just a distant annoyance.

Victrix Media welcomes this opportunity to present its own interpretation on the spectacular wave of innovation now sweeping through the existing communications regime. These overwhelming changes will either send organisations into oceans fertile with commercial opportunity or against the shore, crashing into barren rocks. Corporate survival is ultimately determined not only by the skill of the navigator at the company helm but by government policy as well.

The Productivity Commission's issues paper opens up many points for discussion. Victrix Media, however, addresses only a select number of these concerns.

The primary focus of this submission will be to comment and provide evidence where necessary relating to three areas of importance.

1] Issues associated with the economics of broadcasting, particularly as they pertain to the advertising model and the splintering of those revenues across an increasingly diverse range of media.

2] The issue of ownership and control will be addressed; clearly the most sensitive component in any review of media regulation. Here the commercial interests of media groups supported by concepts like convergence, economies of scale and globalisation, crash head-on with public policy issues such as concentration of ownership and editorial independence.

3] Finally, this submission addresses several issues associated with digital convergence and its implications for incumbents and potential entrants alike.

2.0 The Isoquantic Shift

A period of rapid re-invention is sometimes accompanied by jargon just as impressive so as to emphasise the weight of events pressing upon current practices, whether in the workplace, in the home or the very principles which bind social actors like government and community together.

Former Chairman and CEO of Apple, John Scully, addressing the American National Association of Broadcasters in 1993 spoke of an 'isoquantic shift' occurring within the computing sector, but progressively moving towards the domain of analogue communications.

"There is a theory in high technology called the isoquantic shift which refers to a significant technological advancement that dramatically changes the way people do things and completely reorients people's concepts of how things are done."[1]

The fractional horsepower electric motor was an isoquantic shift from steam engines in the 19th Century, while the development and diffusion of the microprocessor was another.

Scully was illustrating the undeniable fact that digitisation was at that time expanding beyond computer operating platforms and software applications towards the linear world of analogue communications, such as telecommunications, broadcasting and publishing. Concurrently, the Internet was emerging as a communications medium with an unrivaled digital pedigree, unconstrained by any historical baggage of analogue development.

Almost seven years on and the imminent diffusion of mainstream digital broadcasting combined with the proliferation of Internet use, both within the workplace and household, is bringing to realisation the public policy consequences of this latest isoquantic shift in human endeavor.

2.1 Developments in the broadcasting, telecommunications and Internet industries – a short to medium-term outlook

The development of any consumer product occurs on two levels. The first is with the organisation, where research and development surrounding the product is concentrated. Stunning technological breakthroughs may be achieved here, without much inquiry as to whether these developments are warranted by consumer demand. The second level of development occurs with the product's eventual diffusion into the marketplace. Here, goods and services are put under the test of consumer choice. If the product fails at this level, then despite all the technological development in the labs, the product is considered not to have developed at all.

What eventually dominates consumer's demand for media, particularly electronic broadcasting or narrowcasting, will have more to do with consumer lifestyle patterns and changes in community demographics than what occurs in the media labs of AT&T or Telstra and their multi-million dollar resources.

Companies behind the development of technologies such as interactive television (e.g. Microsoft's Web TV) may eventually learn that despite providing the household with the technical capability to watch a cricket match from a choice of seven camera angles or downloading ingredients from cooking program onto a shopping list which is then transmitted to the local supermarket for delivery, consumers will not be prepared to have their passive engagement with television change to an active one.

Yet until these two levels of development (corporate and household) are synchronised by way of demand pulling innovation rather than innovation pushing demand, developments in the area of digital communications will continue unabated, despite a lack of a return on investment. An issue all too familiar for 98 per cent of all Internet operations.

A leading catalyst for this development in delivery platforms is the digitisation of content. Digital content gives both the provider and receiver the capacity to manipulate content in a similar way to a document written on a computer can be manipulated, viewed or stored. The key issue in communications development is the type of hardware that will eventually dominate the household, allowing this very personal control over content.

The Internet already provides access to a plethora of content, devoid of any limitations such as time or place. However, consumer choice in content is not unfettered. Technical issues such as bandwidth and affordable computer hardware still constrain most consumers.

[1] Price Waterhouse, EMC Technology Forecast: 1997; 'The Status of Convergence', p.25

Digital television will be one platform that will eventually give consumers a significant amount of personal choice in content received in the home. Customised programming, video-on-demand, advertising response (direct marketing) and pay-per-view will all lead to an environment of 'thematic channels' that fragment audiences even further.

The gatekeepers to this evolution are the telephone companies, owners of the infrastructure that will facilitate this interactivity and delivery of content. Controlling the information 'highways' and 'by-ways' will be their agenda, accepting a few cents in every transaction that takes place on their network. The bundling of telephony, Internet and television through one network will maximise this transaction activity leading to almost pure profit reaching the bottom line once the sunk costs of network development have been recouped.

The common thread running through these developments is personal, interactive communications. How a consumer selects content will depend on the interface that dominates the household. Will the interface be the home PC, the television or a hybrid of the two? Yet given that digital content can be manipulated in any number of ways, it is almost certain that a range of other interfaces will emerge to assist in this 'information overload'.

Personal video recorders (PVRs) are now being realised as a way to filter content delivered to the household from the thousands of information sources available via the Internet and cable television. Guided by a program profile developed by each member of the household, the PVR will read the digital 'tag' or 'watermark' on every program coming into the home via its cable connection. If the 'tag' matches one of the program preferences set by a household member then that program is recorded and stored in their personal folder on the PVR disk. The PVR will also identify and remove commercials from the recordings as well as redirect phone calls to another number.

Importantly, these PVRs do not have to be located in the home. It could simply be another service offered by the cable company or telco, where the program preferences of each subscriber are stored in a central database.

This is probably the most effective way to illustrate the future of digital content - technology neutral and totally malleable by the consumer.

3.0 Economies of Broadcasting – Loosing another Slice of the Advertising Pie

The euphoria surrounding Internet investments has sometimes, though not always, been grounded by critical evaluation of business models and their subsequent timing in providing a sound revenue stream.

The one revenue stream currently dominating Internet development is advertising and sponsorship. While revenues originating from this source are not nearly enough to cover the capital investment and ongoing costs, advertising is seen as an interim measure until a more viable revenue model can be implemented. One alternative option moving quickly to centre stage are e-commerce systems capable of handling micropayments from thousands of subscribers.

In 1998, worldwide online adspend totaled $US1.5 billion. Of this, the North American market accounted for 87 per cent, the remainder split between Europe (7%), Asia/Oceania (5%) and Latin America (1%).[2]

To put this into perspective, the following table outlines adspend on a US per capita basis as it currently stands and then projected to 2003:

$US	1998	1999	2000	2001	2002	2003
Online	$25	$39	$57	$60	$84	$104
Newspaper	$303	$315	$328	$341	$355	$370
Television	$229	$243	$257	$272	$287	$304
Magazine	$74	$78	$82	$86	$90	$94
Radio	$69	$73	$77	$80	$85	$89

The exponential growth of Internet advertising relative to other mediums is a salient reminder of the finite nature of the advertising/marketing dollar and those communication mediums most effected by the Internet and its accountability in delivering a measurable ROI.

While measuring a return on investment may seem near impossible from the point of view of advertising with mass media, it will be the Internet's capacity to deliver this precise measure of accountability that will support its continued involvement in marketing and advertising campaigns.

In other words, as a direct marketing medium with a high level of accountability, the Internet will only accelerate the process of fragmenting advertising expenditure.

Yet for terrestrial broadcasters, their share of the advertising pie has not even begun to feel the full impact of new media. Internet only tinkers with the edges; cable television has the most the gain from the accumulated losses shared by free-to-air broadcasters.

In 1998, cable networks in the US for the first time reduced the audience share of the four main terrestrial broadcasters (CBS, NBC, ABC, Fox) to below 50 per cent. A year earlier, the cable industry celebrated total advertising revenues of $US8 billion – up from $US4 billion in 1993.

Ratings for the top five shows shown by terrestrial broadcasters in 1996 – 1997 and 1986 - 1987

	1996 – 1997 season		1986 – 1987 season	
1.	E.R.	21.2	The Cosby Show	34.9
2.	Seinfield	20.5	Family Ties	33.4
3.	Suddenly Susan	17.0	Cheers	27.5
4.	Friends	16.8	Murder, She Wrote	25.4
5.	Naked Truth	16.8	Night Court	25.0

The decline in advertising growth and audience share by terrestrial broadcasters has occurred concurrently with a steady growth in the average number of television stations available to each American household.

In 1991, when the main four commercial networks held a combined 62 per cent audience share, there was an average of 35 stations per household. By 1997, the average number of stations available rose to 49 while audience share for the main four broadcasters slipped to 51 per cent.[3]

For the Australian television marketplace the consequences are predictable.

The three Australian pay TV operators, Foxtel, Optus Vision and Austar, currently serve approximately 950,000 households, delivering 58 unique channels, with at least 37 supported through advertising. And while cable rollout might have ceased for the immediate term, a recent agreement between Foxtel and Optus to use the Optus B-1 satellite will only accelerate access to many of these channels across most of the country.

In terms of forecasting pay TV growth, it is estimated that there will be approximately 1.5 million households subscribing by the end of 1999. In subsequent years, subscriber numbers will rise to 2.07 million in 2001 and then to 2.6 million by 2004.[4]

[2] Forrester Research, Inc.
[3] Nielsen Media Research (US)

The diffusion of media technologies, as experienced in the past, cannot help but erode the share of advertising expenditure held by incumbent media.

In 1960, for example, newspapers attracted $108 million in adspend, compared with $27.6 million for television; $21.2 million for radio; $22 million for outdoor and $8 million for cinema.

By 1970, the share held by newspapers rose to $166.3 million, compared with $94.5 million for television; $44.2 million for radio; $36.6 million for outdoor and $9.9 million for cinema.

By 1981, the share held by newspapers rose to $880 million, compared with $677.9 million for television; $177.6 million for radio; $142 million for outdoor and $29.5 million for cinema.

And by 1996, the share held by newspapers rose to $2.54 billion, compared with $2.09 billion for television; $524 million for radio; $248 million for outdoor and $41.3 million for cinema.

Source: Commercial Economic Advisory Service of Australia

Between 1960 and 1996, newspaper's share of total advertising fell from 57.8 per cent to 46.7 per cent compared with television's share rising from 14.8 per cent to 38.4 per cent. Over that same period, radio's share of total advertising fell from 11.3 per cent to 9.6 per cent.

Against this background, Australian Internet advertising will rise from $US10 million in 1998 to:

1999	$US20 million
2000	$US40 million
2001	$US75 million
2002	$US130 million
2003	$US195 million

Source: Forrester Research Inc.

[4] James Spowers, James Capel Australia, Pay TV Review

4.0 Principles of Regulation

Victrix Media holds a similar view to the CPA in that “legislation should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the legislation can only be achieved by restricting competition.”

The obvious intention of this principle is to ensure owners of media do not have undue influence in setting a particular personal agenda and disguising that agenda as one with genuine community interest. Alternatively, the intention of the legislation would also be to minimise the chance of selected information being made public without having an alternative avenue available for recourse.

The essence of this regulatory principle is about the dangers of concentrated ownership, particularly as they relate to the scarcity of spectrum associated with free-to-air broadcasters and the regulatory freedom to reach up to 75 per cent of the population.

The regulatory principle of applying certain controls on broadcasting services as determined by the degree of influence they exert on shaping community views could be criticised as being dangerously subjective and hopelessly outdated. But this is from the point of view of someone who has access to numerous modes of communications and who is educated enough to critically evaluate the information available.

In short, there are those in the community who are ‘information rich’ and see little value in legislation which stops ownership of one media platform extending its control into an alternative media. The information rich are the first to access technologies which circumvent the influence of the mass media, while the information poor do not. Predictably, the division between these two groups is along socio-economic lines, with less wealthy households having fewer media choices.

Access to pay TV and the Internet is dominated by households located in metropolitan areas with incomes of more than $66,000 per annum. Pay TV penetration, for example, stands at around 14 per cent of all households, while Internet is slightly higher at 18 per cent. For a more detailed profile of Australian Internet users, consider the following points:

> 54% of households with Internet access consisted of a married couples and children;
>
> 9% of single people were connected to the Internet;
>
> 36% of households with combined income greater than $66,000 have Internet access;
>
> 26% of households with incomes of between $44,001 and $66,000 have Internet access;
>
> 10% of households with incomes of less than $27,000 have Internet access;

Source: Australian Bureau of Statistics (1999)

For pay TV users, the profile is remarkably similar.

> 25% of households with an income between $60,000 and $100,000 subscribe to pay TV;
>
> 38% of households with an income greater than $100,000 subscribe to pay TV;
>
> 20% of households with a PC and/or laptop subscribe to pay TV;
>
> 34% of households with Internet access subscribe to pay TV.

Source: AC Nielsen Pay TV Establishment Surveys 1998

Any regulatory control over broadcasting services (i.e. mass media in general) is admittedly an anachronism for part of society but arguably a necessary restriction for the majority who still rely on these services as their only means of information and entertainment.

Victrix Media makes the following recommendation: That any liberalisation of broadcasting legislation be on the proviso that the diffusion of communications such as the Internet and pay TV reach a certain level of household penetration. Leading up to this point, some degree of access to the digital spectrum would be allowed to datacasters as a way of encouraging program diversity at a 'mass media' level.

The intention would be for the legislation to encourage growth by offering commercial operators an incentive to encourage household take-up of these technologies rather than simply being satisfied with maintaining the status quo with little recognition of the technological changes currently underway.

In short, new media is not yet mature enough to counterbalance the influence of mass media on community views and that any legislative change first take into consideration the real consumption levels of new media, both in terms of household penetration and those demographics which dominate the markets for new media.

5.0 Ownership & Control

Standing back from the euphoria which surrounds so much commentary about new media and the phenomenon of convergence, the previous section highlighted the fact that new media is far from pervasive and is still very much contained within selected demographics. The high growth rates shown by Internet and pay TV take-up is not unusual for a technology starting from such a low base.

Victrix Media believes that what limitations there are to media ownership in the current legislative regime remain in place, with an eventual phasing out once penetration levels of new media have reached certain prescribed levels. Victrix Media does not subscribe to the view that current ownership restrictions be extended in any way to media platforms beyond metropolitan newspapers and television broadcasters.

The adoption of new communications is obviously dependent on the content available, which either complements content available elsewhere or is of an exclusive nature, encouraging take-up at an even faster rate.

The key to encouraging diffusion of consumer communications is to build up a critical mass of available content. Governments are encouraged to put as many services online as possible in an effort to encourage more people to use the Internet. This starts the process of the 'virtuous circle' where a growing number of people online encourage more commercial operators to adopt the medium which in turn attracts even more people to use online services.

Content generators like incumbent media groups such as publishers and broadcasters must be given unfettered access to new media platforms, unhindered by ownership limitations which might discourage the full 'translation' of current content as well as the development of original material for the new platforms. Content which has strong branding 'offline', like magazines and metropolitan newspapers, generate enormous interest because of their relevancy to local communities.

5.1 Foreign Ownership

The negative connotations associated with the phrase ‘foreign ownership’ has gone a considerable way to igniting heated passions about international investment in Australia’s media industry instead of encouraging rational debate on the merits of utilising international expertise and equity more widely within our media and communications industries.

Victrix Media believes current limits to foreign ownership (equity) work like an archaic and ill-fitting cog in a media machine progressively moving faster to meet the insatiable demand for content.

Foreign ownership laws hinder the machine from reaching full capacity, where resources could be utilised to their absolute potential.

Opponents to a foreign ‘influence’ in local media groups often cite the potential for foreign programming to be dumped on domestic audiences or for international players to use their media properties to set the local agenda from smoked filled rooms in London, Bonn or Los Angeles.

There are two answers to these concerns and neither relies on ownership restrictions. The first is that as commercial assets, media organisations are influenced by market sentiment and consumer demand, regardless of ownership. In other words, a foreign owner if they care about receiving a return on their investment, will manage that asset in a way that is responsive to the needs of local audiences. News Corporation’s Asian satellite broadcaster, Star TV, for example, learnt the hard way when it realised that programming from one market could not simply be repackaged and then used across the entire region in one transmission; indigenous tastes and preferences will always hinder the globalisation of broadcast software (programming). Besides, how would a media conglomerate like Germany’s Bertelsmann get way with German programming on Australian television at prime time!

The second answer to foreign ownership concerns is simply to legislate for a minimum level of Australian content. Currently a 10 per cent rule applies to pay TV operators and their production of Australian drama. A similar measure might also be possible with terrestrial broadcasters.

The consequences of refusing our local media industry access to foreign equity and technology will be long lasting.

Should local industry lack the resources to develop content and distribution channels which are in-line with other industrialised countries, then a number of negative consequences will emerge:

1] We loose the ‘critical mass’ in content needed to encourage households to adopt new technologies, and

2] When new distribution technologies are eventually introduced to the local market place, behind other international markets, we will need to import content and expertise to fill the void left by the lack of local production.

Overall, it is important to never loose sight of the influence of consumer sovereignty when the issue of foreign influence is raised. Whether the media asset is a newspaper or television station, neither will survive commercially if content does not reflect local issues or personalities.

6.0 Digital Conversion

Under current legislative amendments, free-to-air broadcasters will be restricted from using their digital spectrum to broadcast multiple channels. Instead, broadcasters will use this capacity to provide services in a high-definition format. Victrix Media believes commercial television operators should instead be given the opportunity to freely choose which spectrum arrangement best suits their own position in the marketplace.

In short, free-to-air broadcasters must decide for themselves whether a multi-channel format is commercially viable given the current channel capacity of cable and satellite distribution systems. Free-to-air broadcasters also have to evaluate whether a multi-channel format can be supported with advertising and sponsorship. Given that no subscription services are allowed, will a splintering of advertising revenue between six or seven channels support quality programming or will viewers have the pleasure of viewing 12 game shows in succession followed by re-runs of The Brady Bunch?

In such an environment where programming choice is almost at saturation point already, free-to-air broadcasters will more than likely come to the conclusion themselves that high-definition television is a very effective way of differentiating their service from existing multi-channel platforms. It might even be a way of stemming the audience flow away from terrestrial television. The broadcasters, however, must arrive at this conclusion themselves.

In terms of restricting the new digital spectrum to incumbent media groups until 2006, Victrix Media believes this is too long a period to withhold competitive pressures on free-to-air broadcasters. Content being developed online now could receive far larger audiences via terrestrial broadcasting, and in the process, capture another potential revenue stream for media groups to use as a way of financing more local content.

7.0 Conclusion

The isoquantic shift spoken about at the beginning of this paper is certainly underway within our media and communications industries. This so-called shift is about providing individuals with more services and more content in a convenient and personalised manner. It is about taking the role of program producer away from the broadcaster and content developer and giving it to the household to manage. But again we ask, is this a role deemed necessary by commercial technocrats who see the opportunity to sell expensive software packages for the household 'webvision' set, or a choice consumers have long wanted?

But importantly, this is about a revolution in progress. It has not yet overwhelmed the lives of everyone in our community, only those who seem a little frustrated that the 'revolution' seems to be slowing down to let the rest of us catch up. There is no critical mass in any local Internet audience, except perhaps in the United States. Even the multi-channel environment associated with subscription television is restricted to a fraction of the community.

Nevertheless, the effects of this revolution are being felt. Both the time and advertising dollars spent with media are increasingly fragmenting because of a combination of emerging new media and changing lifestyles. This inevitably reduces the reach of mass media in some socio-economic segments, but not all.

This is why Victrix Media advises caution in the liberalisation of existing broadcasting legislation. Certainly a time will come when the concentration of ownership is not an issue, but that time is not yet. To hasten that inevitability, Victrix Media stands by its recommendations that restrictions to foreign ownership be lifted completely and that the digital spectrum be opened up to third parties sooner rather than later.

Written By:

Andrew Reid
Director
Victrix Media
A.C.N. 086 024 277
http://www.victrixmedia.com.au
reidvm@victrixmedia.com.au