

UK Digital TV: A Case Study

Adolf Grimme Institut
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Screen Digest

Who are we and what do we do?

Screen Digest core coverage areas:

- Cinema
- Video & DVD
- TV - broadcast, cable, satellite & IPTV
- Broadband
- Video Games

Our analysts:

Ben Keen – Chief Analyst

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David Hancock – Senior Analyst

Mark Smith – Senior Analyst

Charlotte Jones – Analyst

Video & DVD

Helen Davis Jayalath – Senior Analyst

Paul Callaghan – Analyst

David Scott – Analyst

Marie Bloomfield – Analyst

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TV – broadcast, cable, satellite & IPTV

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Nick Gibson – Analyst

Screen Digest online services

Continuously updated and comprehensive data-sets and forecasts of the key media markets. Up-to-the-minute market data and forecasts.

- Cinema Intelligence – 56 countries
- Video & DVD Intelligence – 45 countries
- TV Intelligence – 37 countries
- Broadband Intelligence – 27 countries
- Video Games Intelligence – 18 countries

Industry reports

Screen Digest publishes a regular flow of major reports on the entertainment media. Reports usually include market forecasts, trend analysis, results from surveys and interviews with key players in the market. Current and future reports include:

- European Digital Pay TV Platforms: Market Assessment and Forecast
- TV Commerce and T-Shopping in Europe
- Online Gaming Markets to 2007
- Global HDTV Outlook
- Wireless Gaming – Global Operator Strategies
- European Broadband Cable 2005
- Broadband Entertainment Content: European Operator Strategies and Market Forecasts to 2007
- Interactive Leisure Software: Global Market Assessment and Forecast

Consultancy

Screen Digest has been engaged by many leading entertainment media and financial groups for single client consulting projects. Consultancy services offered across our core areas include:

- Market research and forecasting
- Corporate strategy
- New technology impact assessment
- Due diligence
- Expert witness assignments
- New market pre-entry studies
- Competitive intelligence

The story of British TV: national broadcasters

- 1936 – BBC1
- 1955 – ITV
- 1964 – BBC2
- 1982 – Channel 4
- 1992 – BBC Parliament
- 1997 – Channel 5
- 1998 – BBC3, BBC News24, and ITV2
- 2002 – BBC4, Cbeebies, and CBBC
- 2004 – ITV3



The story of British TV: analogue to digital

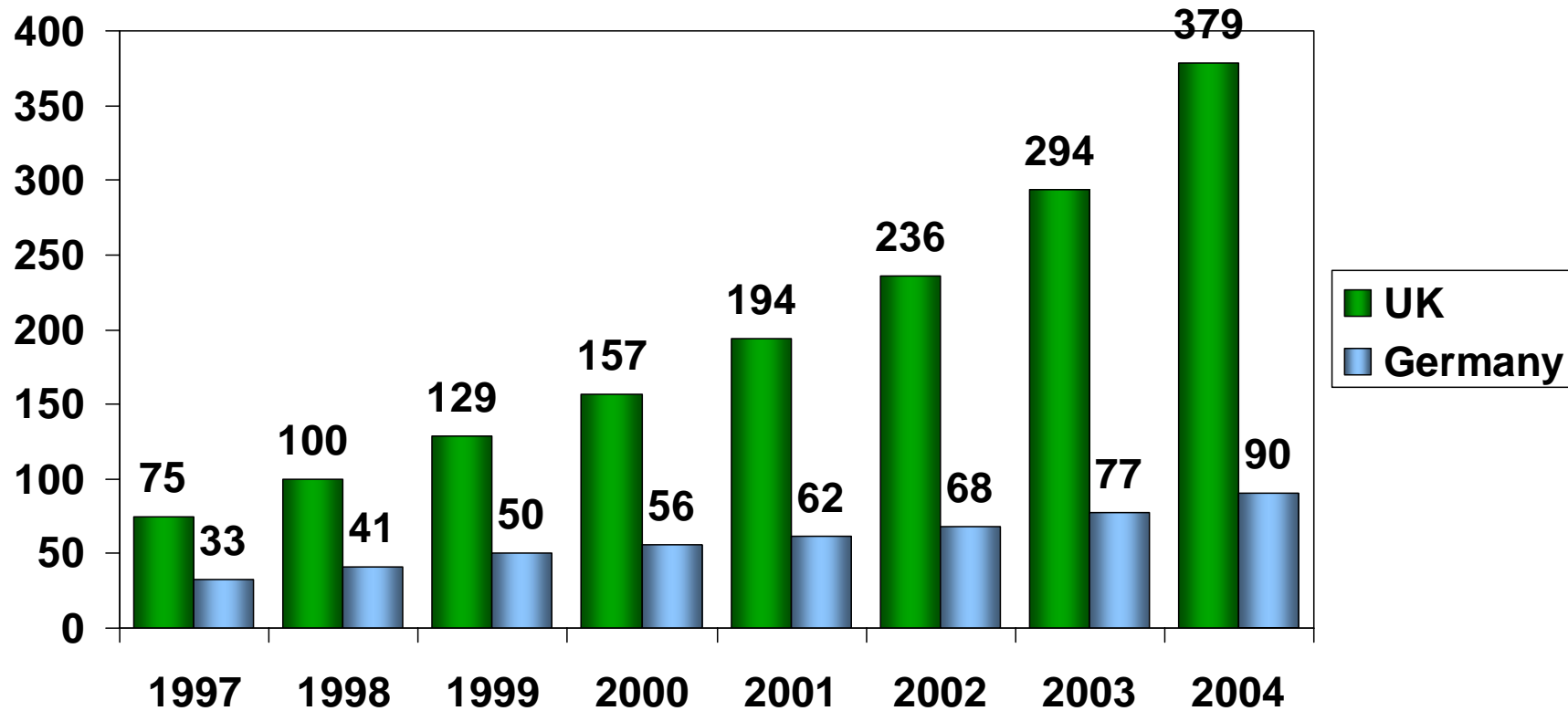
- Up to 1988 there were just 4 terrestrial channels
- 1989 – Sky TV launched 4 channels on DTH satellite
- By 1994 there were 4 terrestrial channels + 44 (analogue) channels on cable/satellite
- 1997 – C5 makes 5 terrestrial channels + 86 (analogue) channels on cable/satellite
- 1998 – the year that ‘digital’ began to change everything

The digital TV story – key platform milestones in the last 7 years

- 1998 – Sky Digital launched (2 years after digital DTH launched in Germany by Kirch)
- 1998 – digital terrestrial channels launched by national broadcasters BBC, ITV, C4 and C5 (4 years ahead of first DTT in Germany)
- 1998 – digital terrestrial pay TV service ONdigital launched
- 1999 – digital cable services launched by NTL and Telewest (1 year before Primacom in Germany)
- 1999 – Homechoice video-on-demand service launched by Video Networks
- 2002 – ITV Digital (formerly ONdigital) service closed
- 2002 – Freeview free-to-air digital terrestrial service launched by BBC, Crown Castle and BSkyB

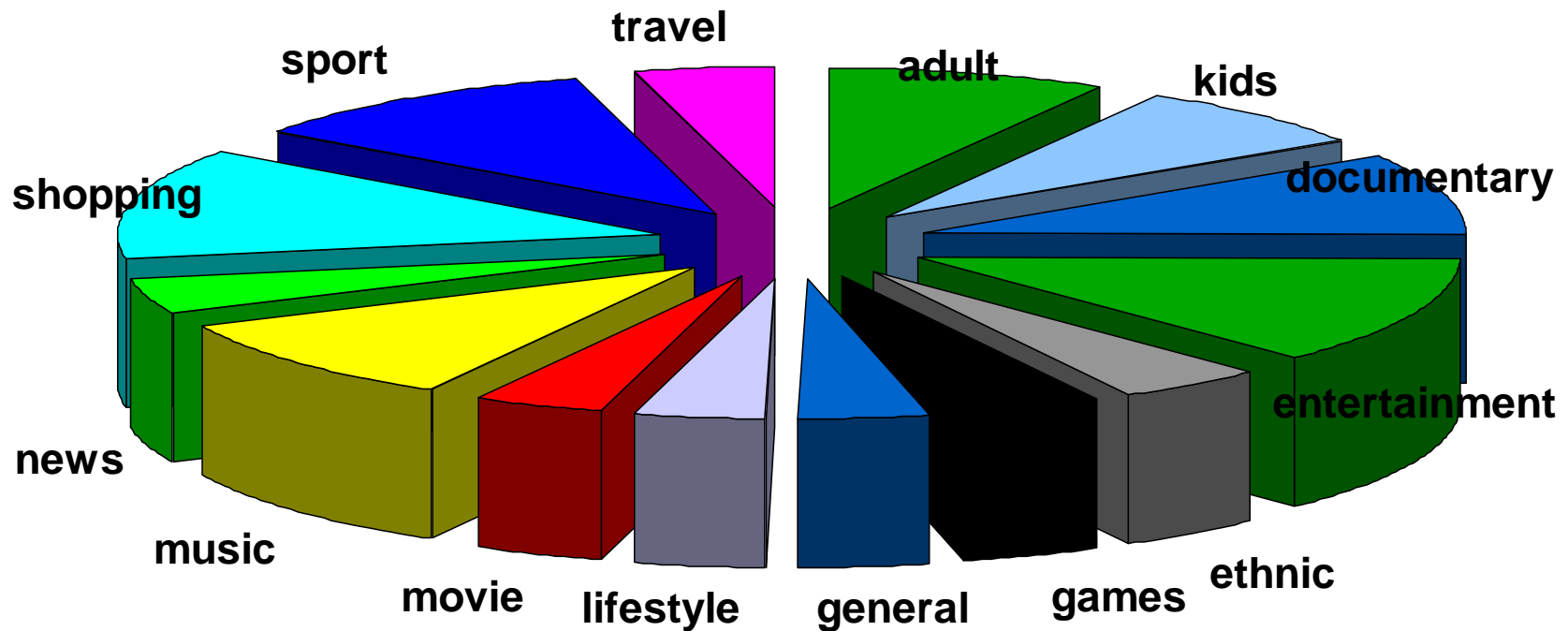
Digital has resulted in an explosion of channels in the UK

Cumulated number of channels



TV shopping and entertainment channels dominate, followed by sport, music, documentary and adult

of channels by genre

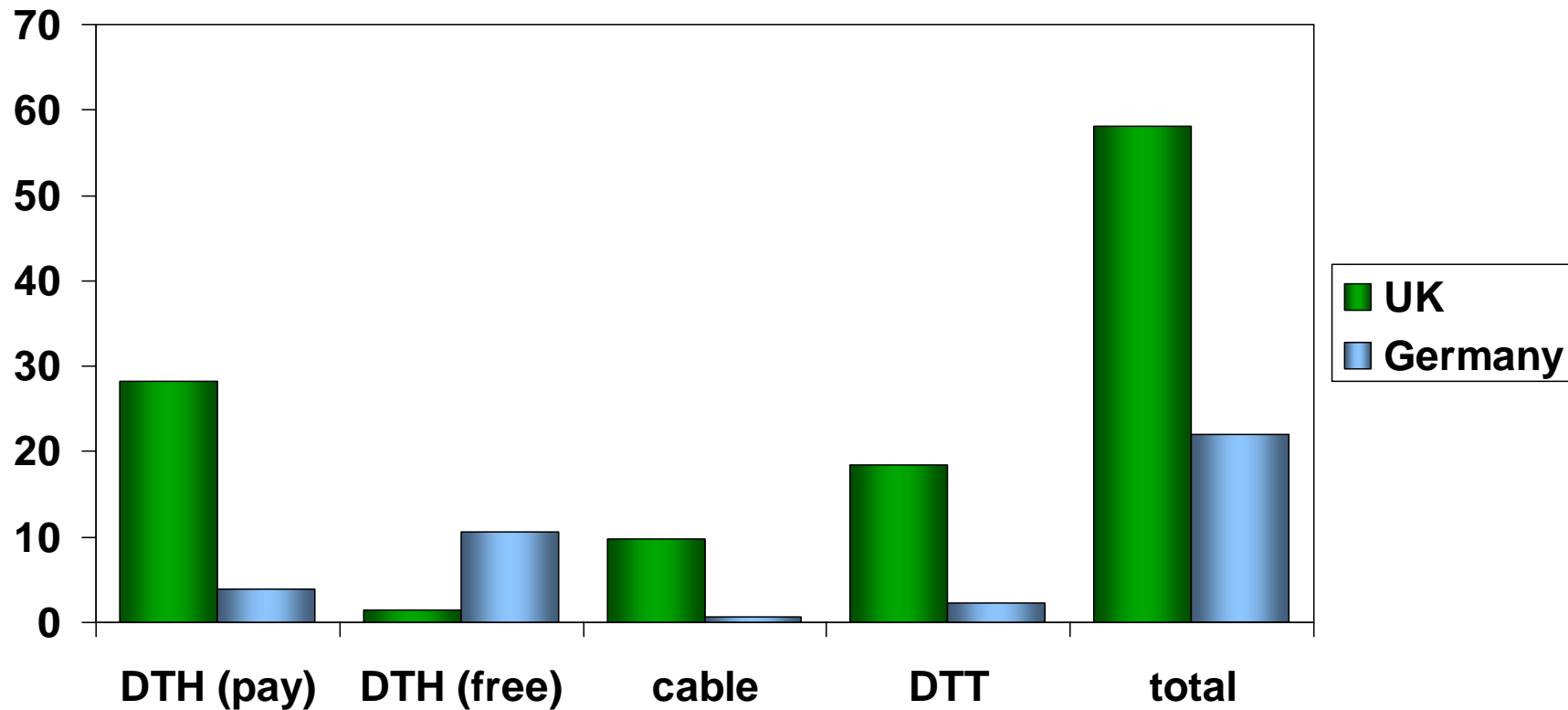


The UK has become a digital TV leader

- Largest digital TV market in Europe
- Most successful digital DTH operator
 - Sky Digital
- Most advanced digital cable infrastructure
 - NTL & Telewest
- Most successful free-to-air DTT platform
 - Freeview
- Pioneering home of DSL TV
 - Homechoice & KIT

Total digital TV penetration in the UK now at about 60% compared to about 24% in Germany

2004 penetration of digital platforms (%)

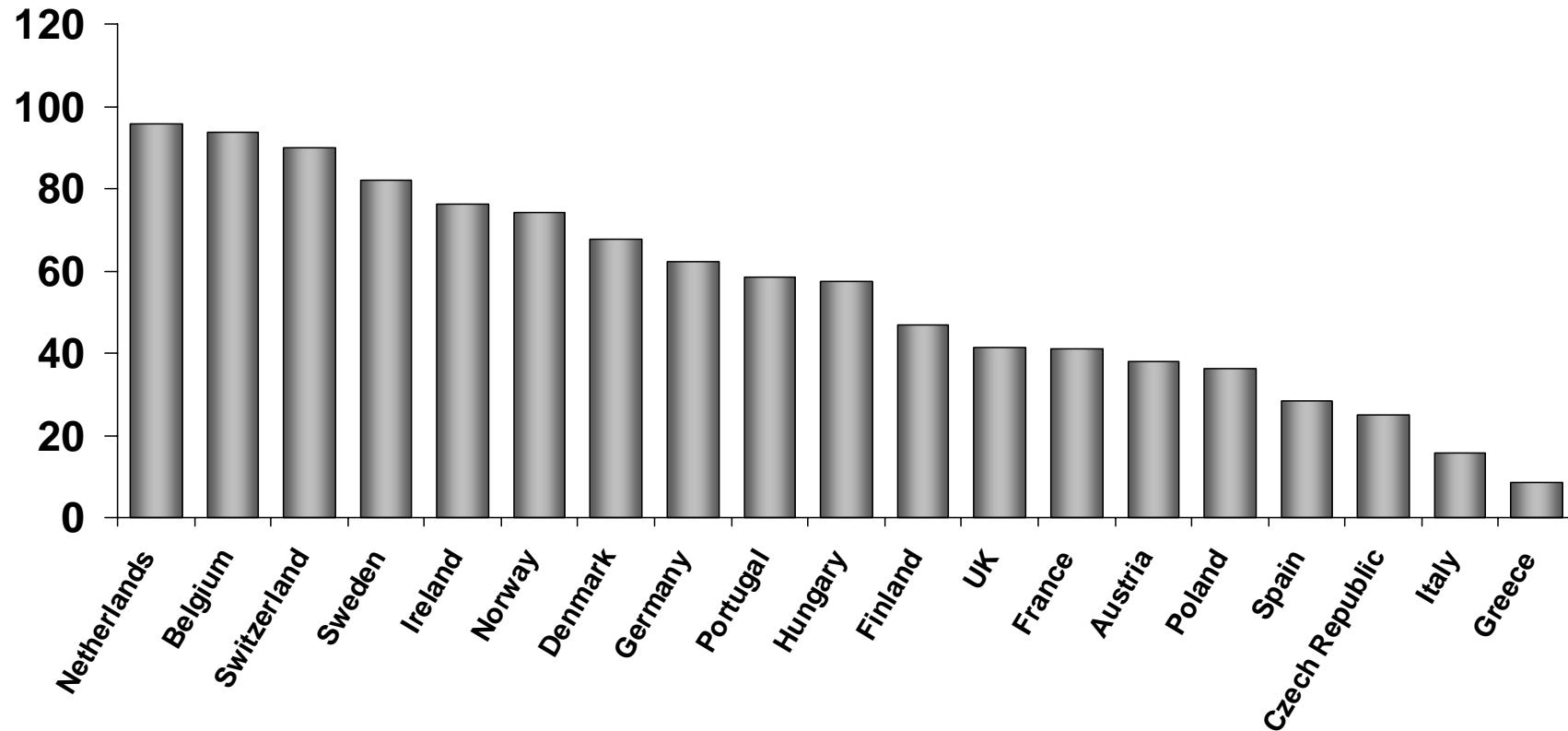


Two models for multi-channel TV in Europe:

	<i>Premium Pay TV model</i>	<i>Utility TV model</i>
Territories	UK, France, Spain, Portugal, Ireland	Germany, Austria, Switzerland, Benelux, Scandinavia
Penetration driven by	Premium channels	Free-to-air channels
Penetration	Under 50%	Over 80%
Cable subscription	Expensive	Cheap
Cable regulation	Light	Heavy
National free-to-air channels	Few	Many
Digitisation	Growing fast	Low, progressing slowly
Dominant business model	Subscriptions	Advertising
Channels business model	Share operator subscriber revenues	Pay for carriage on systems

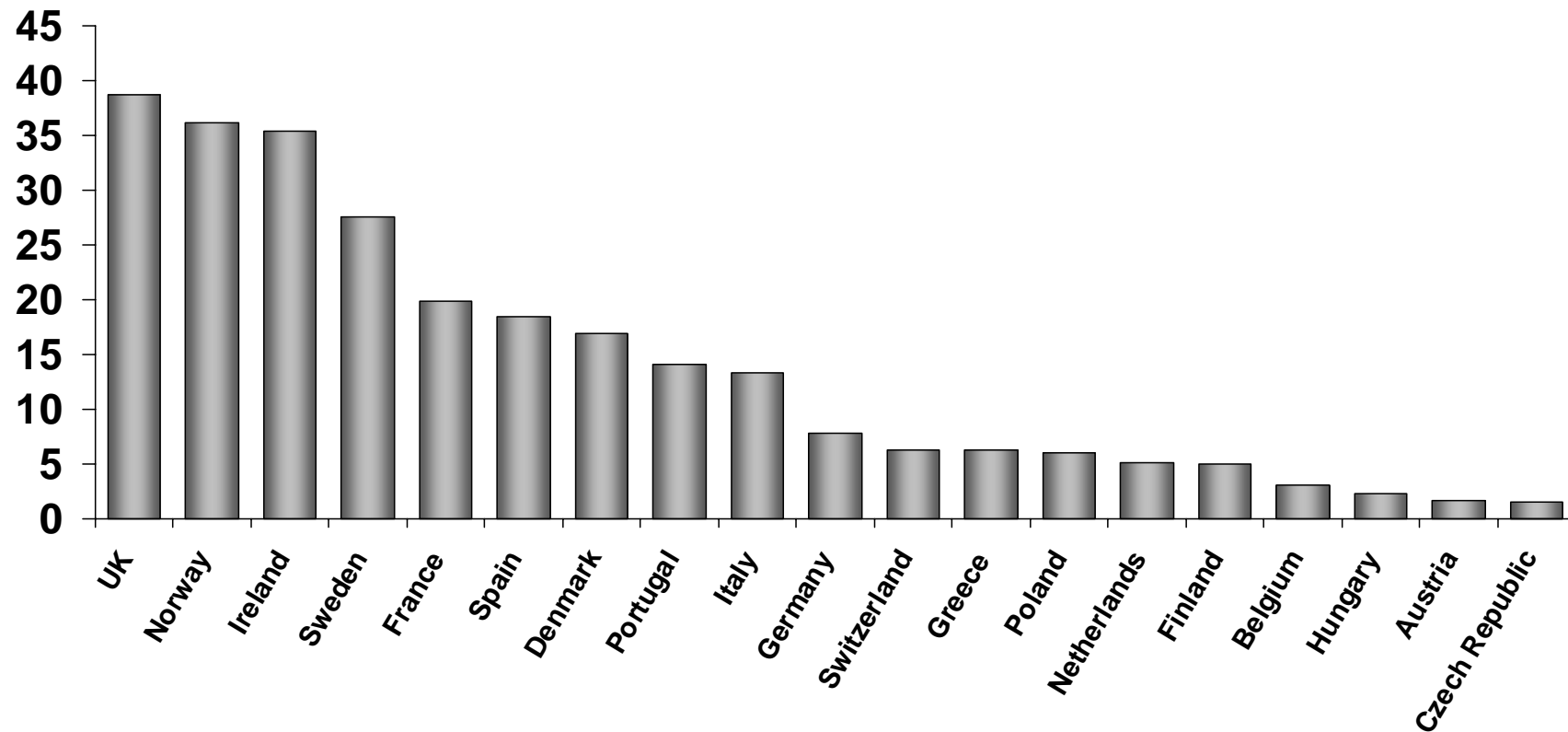
The 'Utility' model countries tend to have higher overall multichannel penetration

Ranking by multichannel TV penetration (%) - 2003 data



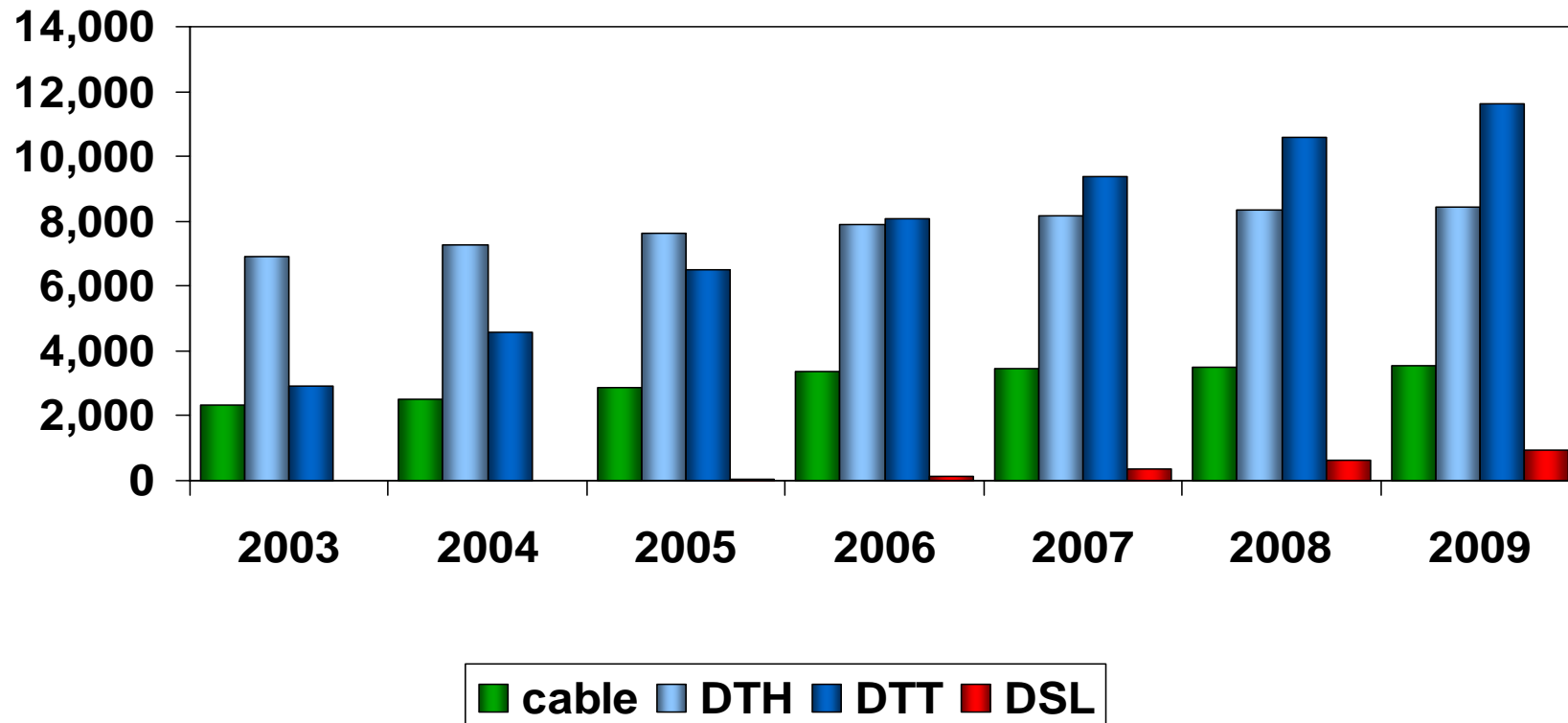
But lower digital pay TV penetration

Ranking by digital pay TV penetration (%) - 2003 data



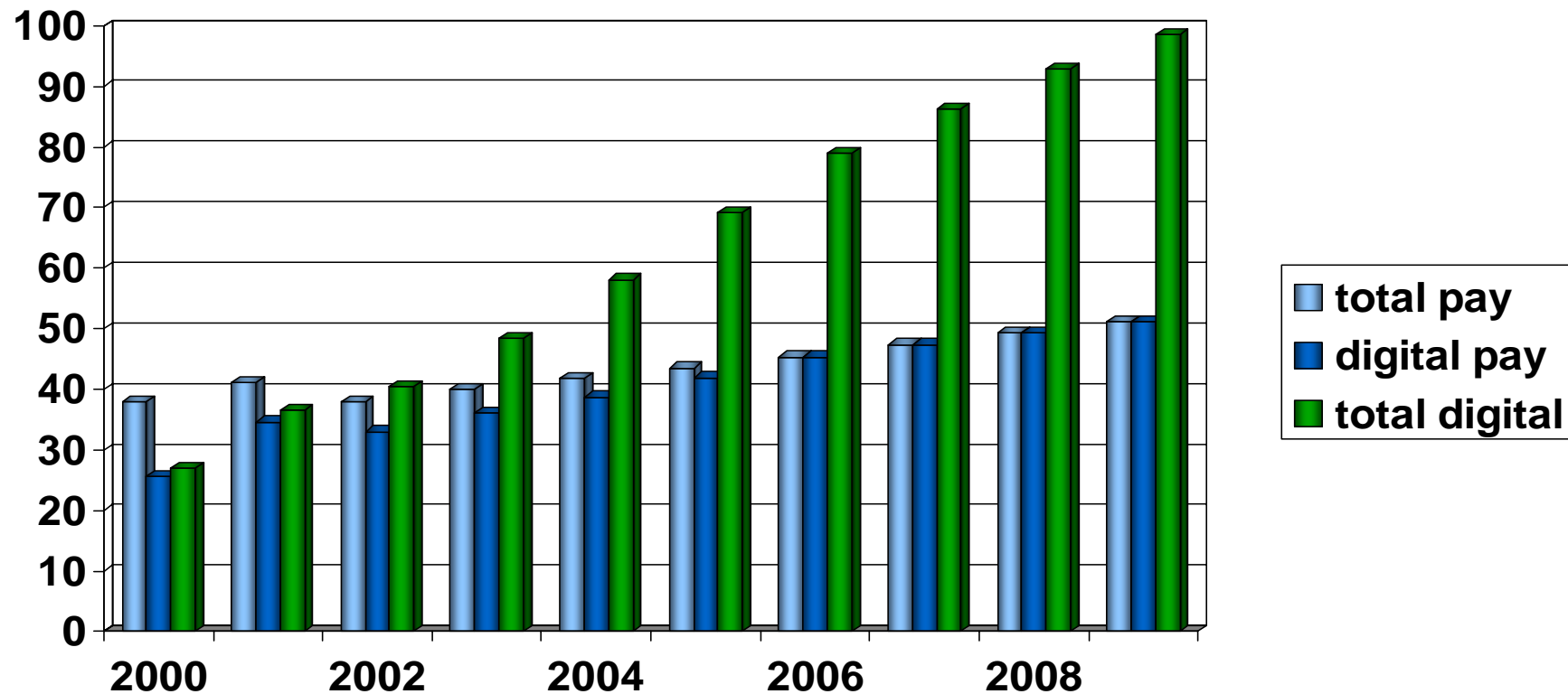
UK: Sky Digital has led the way but likely to be overtaken next year by Freeview as far as eyeballs are concerned

Total UK digital TV households by platform (000s)



Overall, pay TV penetration now at 42% - forecast to reach 51% by 2009

Pay TV and digital TV penetration (%)



Sky Digital

- Largest digital DTH operator in Europe
- Launched digital TV in 1998, free set-top box strategy in 1999
- Over 7m digital subscribers in the UK
- c. 400 digital TV channels, 85 PPV/NVoD channels
- c. £3.5bn/€5bn turnover annually
- High ARPU – £386/€557 annually in 2004
- Dominant provider of premium content in the UK

Sky strategy based on dominance of premium content market

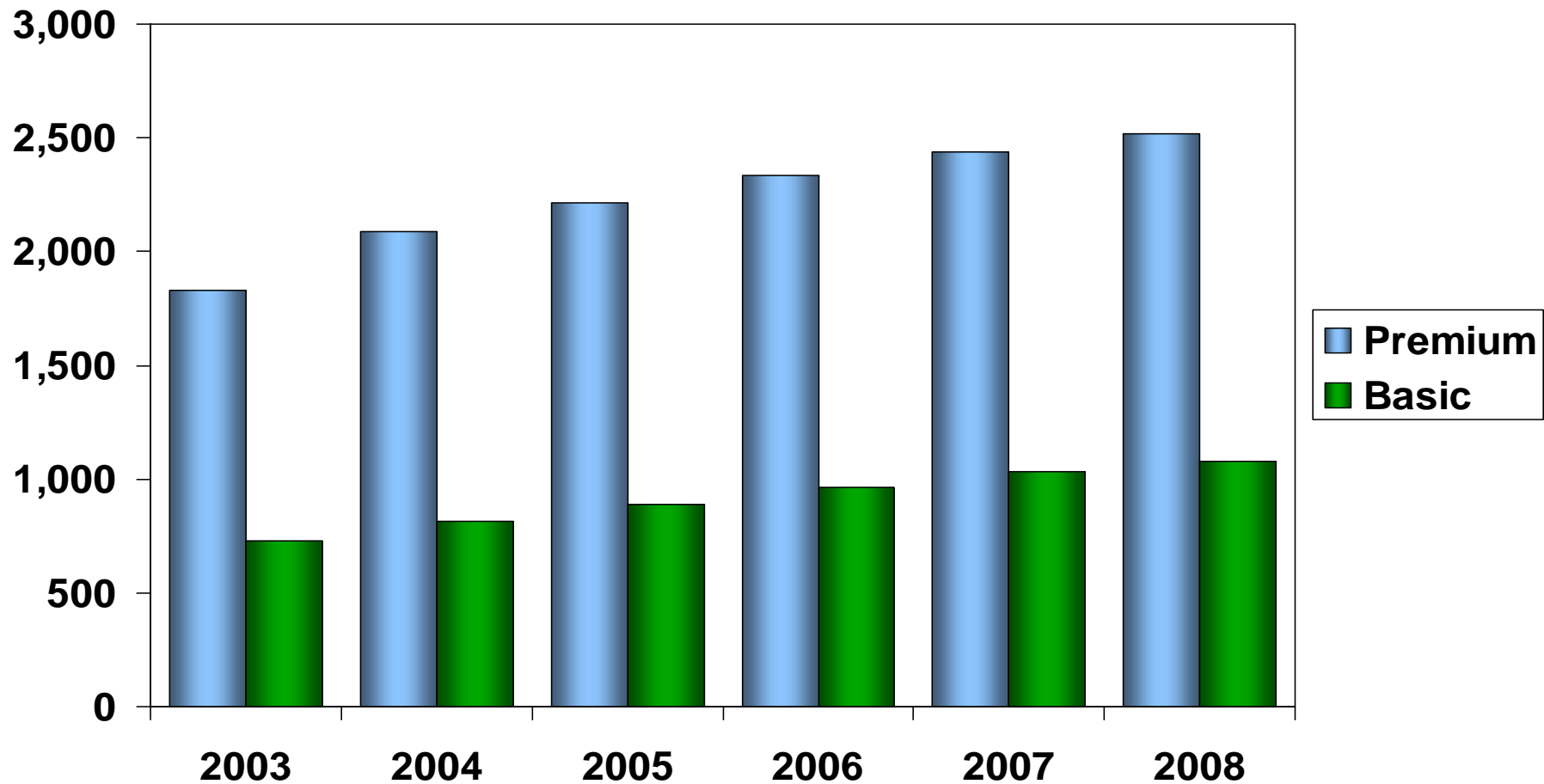
- Sports
 - >£2bn/€2.9bn spent on UK and European football rights
 - Coverage of most major sports events
 - Sky Sports 1-3, Sky Sports Xtra, Premiership Plus
- Movies
 - Deals with all major studios for first run and library titles
 - Sky Movies 1-9, Sky Cinema 1-2
 - 62 Sky Box Office PPV/NVoD channels
- Carriage deals with cable operators and IPTV

Sky also provides range of premium entertainment and news channels, as well as 3rd party channels

- News: Sky News, Sky Sports News
- Entertainment: Sky One, Sky One Mix, Sky Travel, Sky Travel Extra
- Music: Flaunt, The Amp, Scuzz
- Gambling: Sky Vegas Live

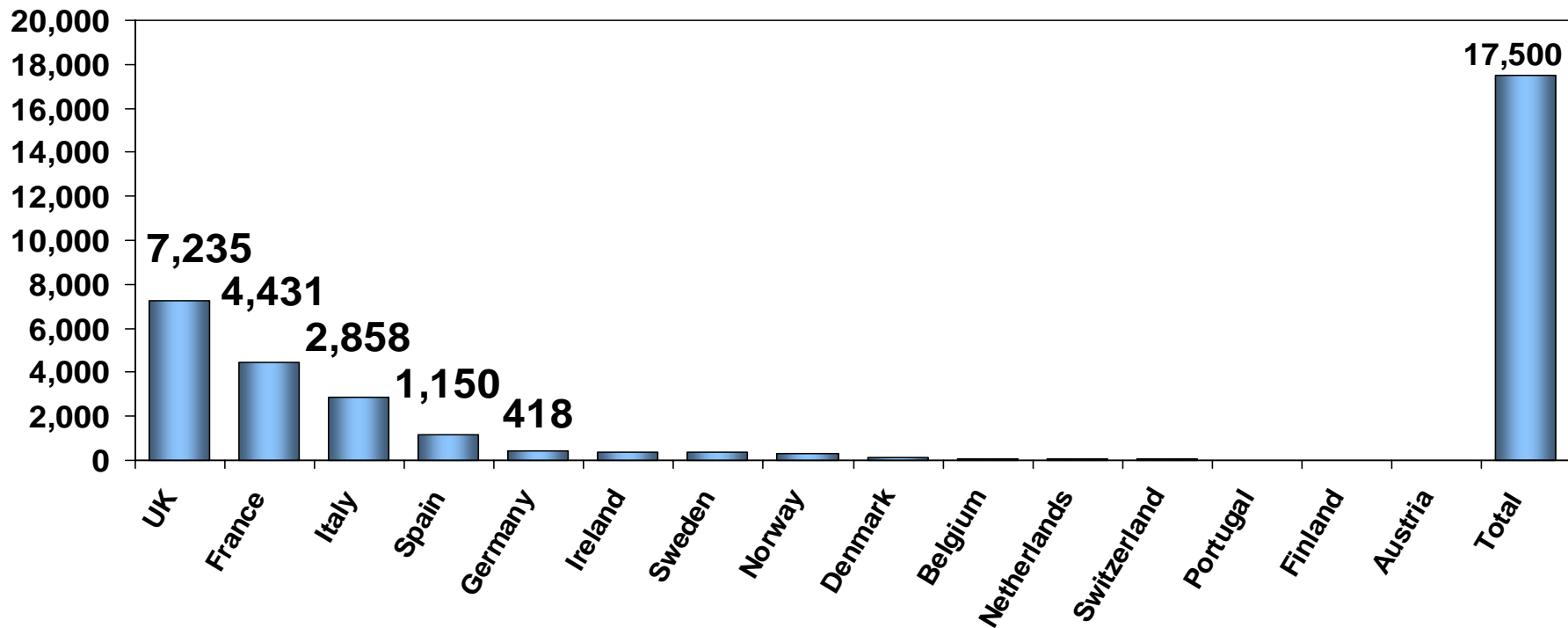
- BBC, Disney, Time Warner, Flextech, MTV, ITV, C4 etc.

Sky Digital basic/premium revenue (£bn)



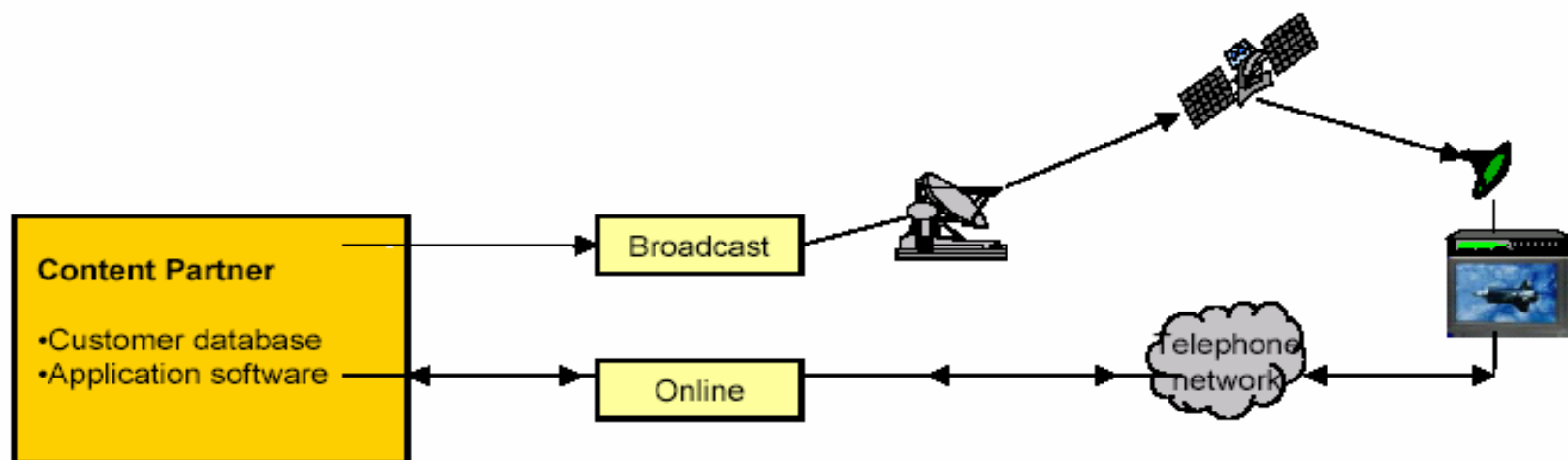
Sky responsible for high number of 2-way digital TV households in UK

European two-way connected homes (000s)
(October 2003)



Satellite return path

Sky Digital infrastructure



Source: BSkyB

Return path enables effective PPV/NVoD

- Movies
 - Sky Box Office generated £69m (€100m) in 2004
- Sports
 - Sports PPV generated £34m (€49m) in 2004

Sky strategy evolving in 2002-2005 - customer acquisition + customer retention

- Interactive TV
- Sky+

- ✓ Boost net additions, keep churn below 10%

Interactive TV (iTV)

- Sky Interactive formed in 2001
- Operates Sky Active 'walled garden'
- Generated £131m (€189m) interactive revenue in 2004
- Offers more iTV channels than any other European operator – 80 per cent of all iTV services available in the UK
- Sky Interactive ARPU close to £20 (€29) a year

An iTV killer application has yet to be found

- Very few iTV services have proven business models
- Best examples are:
 - **Advertising**
 - **Shopping (T-commerce)**
 - **Games**
 - **Betting**

Interactive TV: 2 main types of application

- Stand-alone services
- Enhanced TV services

Standalone services

- Specific applications accessed via “walled garden”
- E.g. on Sky Digital:
 - Shopping
 - QVC (20% of all sales in 2003)
 - Games: (more than 50% of viewers play regularly)
 - PlayJam
 - Sky Gamestar
 - Gambling
 - The Betting Zone
 - Fancy a Flutter
 - Avago

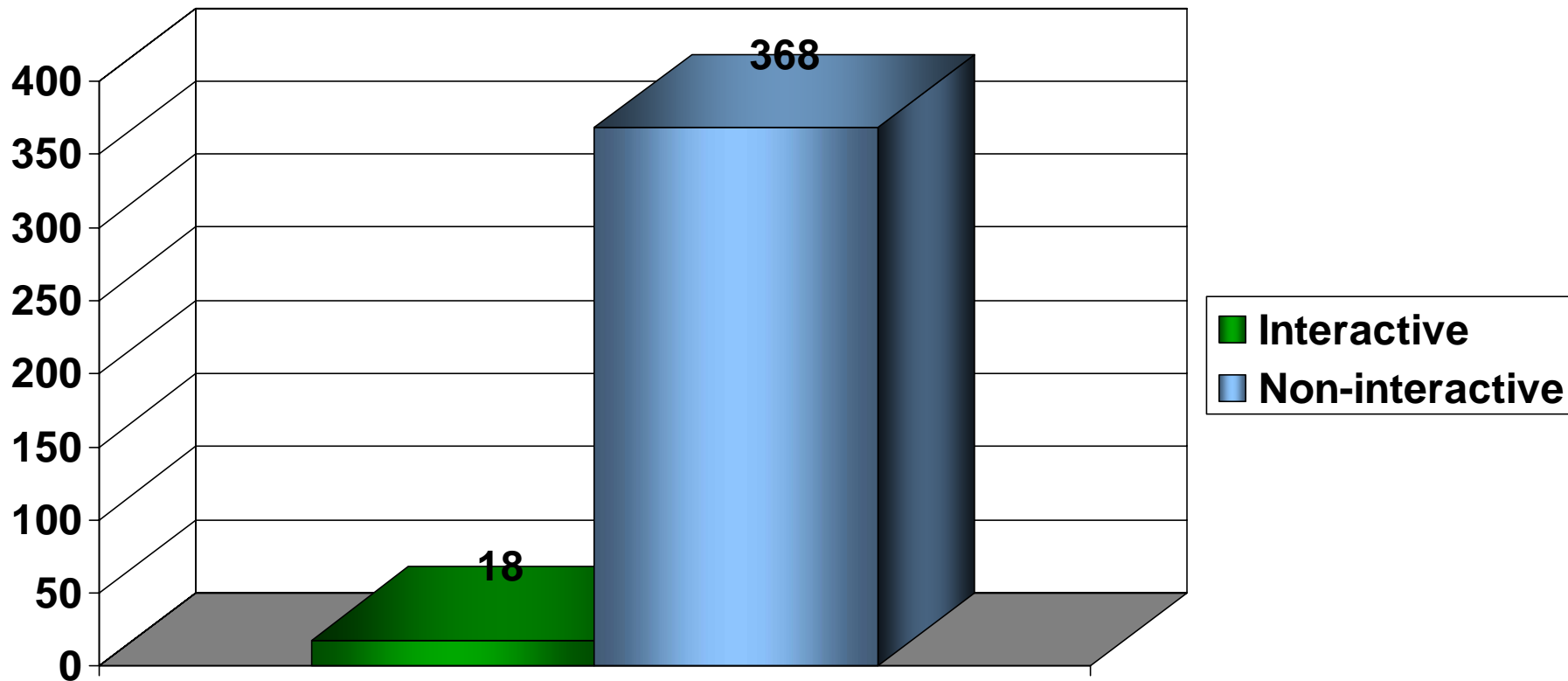


Enhanced TV: the 'red button'

- TV content becomes a launch-pad for iTV applications
 - Improve 'stickiness' (channel loyalty)
 - Content creates revenue opportunities (votes, SMS, advertising links, spin-off games, etc)

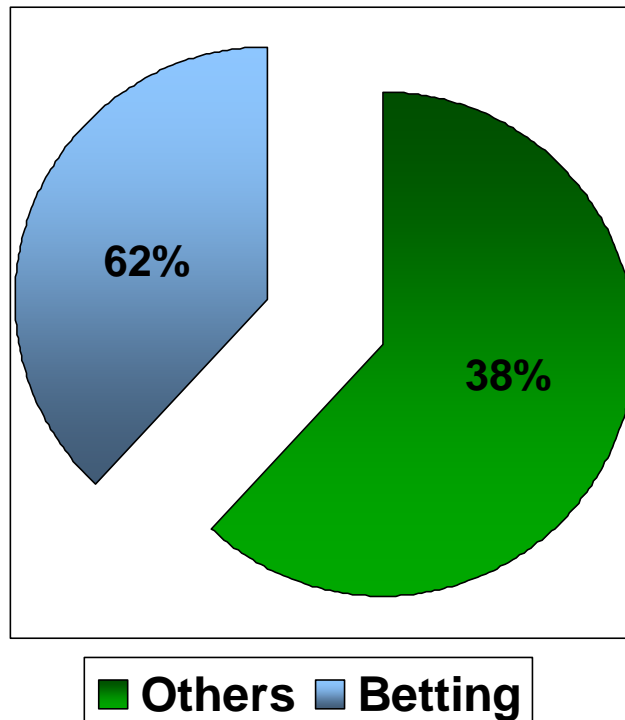
Sky Interactive spending still 20X smaller than non-iTV spending

Annual ARPU (£)



iTV gambling accounts for more than half Sky's total iTV revenues

BSkyB iTV revenues - end 2003



Sky+: premium 'on-demand' TV



Sky+: premium 'on-demand' TV

- Launched September 2001
- PVR STB, £89/€122 (was £199) + £10/€14 per month (waived if taken with premium subscription)
- Marketed as evolution of TV ('Create your own channel')
- 250k subscribers by end 2003, 640k by end 2004, on course for 1m early 2006
- Promoting 'Virtual VoD' – subscribers can record several NVoD movies onto Sky+ but only charged upon viewing
- Capacity of STBs now doubled from 20 to 40hrs
- High definition version of Sky+ coming in 2006

Digital cable has troubled history

- Two major cable TV operators: NTL, Telewest
- Largest digital cable TV market outside the US
- Late to launch digital TV (1999)
- Suffered financial setbacks in 2001
- Scaled back plans for digital TV and VoD as a result of bankruptcy proceedings and debt restructuring
- ‘Triple play’ strategy means competing in three markets dominated by two operators, Sky and BT

Cable TV status

- 3.3m cable pay-TV subs, 2.5m are digital
- Total subscriber count down since 2001 (3.6m)
- Total platform market share on the decline
- Over 50% of UK homes are not passed by cable
- Digital cable subs only 21% penetration of homes passed

Cable TV status

- Merger of NTL and Telewest now imminent
- Total cable TV revenues much lower than Sky - £880m in 2004 (cf £2.7bn – Sky) – and down since 2001
- High churn rate of 20%, but improving TV ARPU
- Neither in premium content market, choosing to carry Sky channels (complaints of Sky market abuse dismissed by OFT)
- Little incentive to push premium packages
- Video-on-demand finally launched by NTL and Telewest earlier this year after many years of false starts
- Also rolling out PVRs to match and better Sky Plus strategy

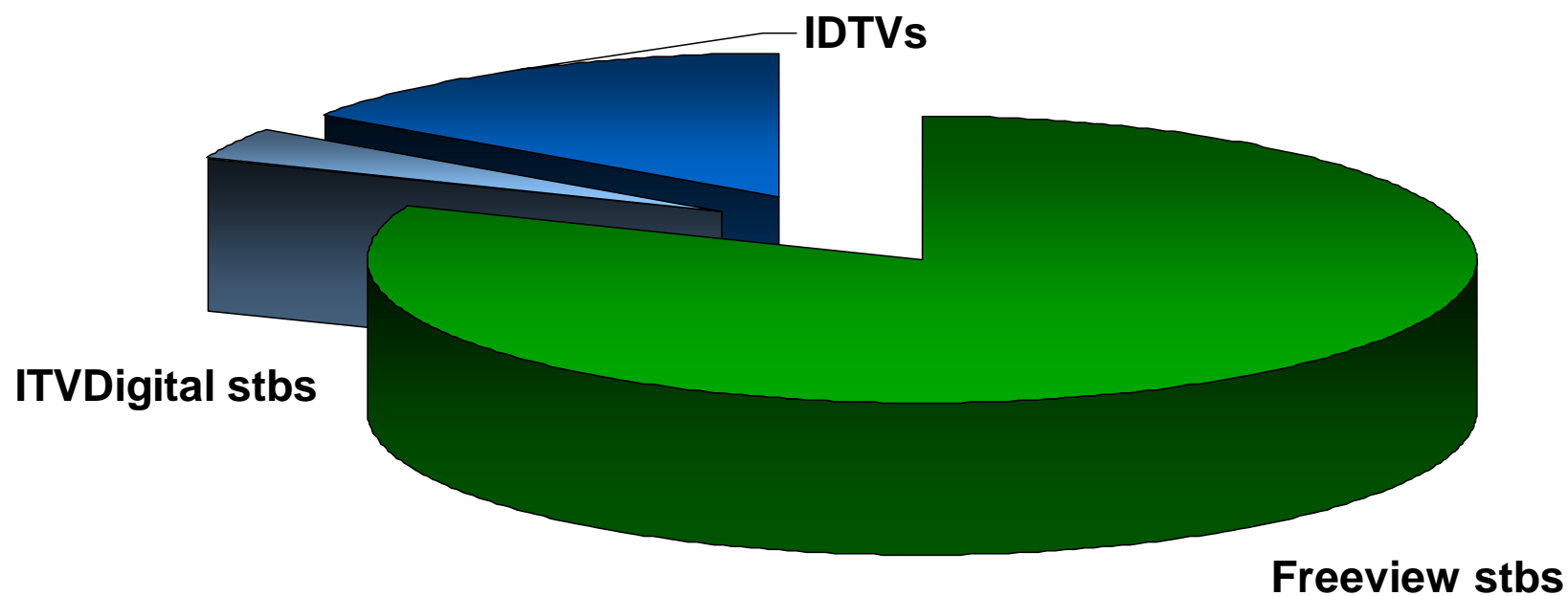
Freeview

Freeview^{*}


- Grew out of ITV Digital ashes
- Retail proposition (£35 upwards)
- Backed by BBC, Crown Castle and Sky
- 30 digital TV channels, 8 digital radio channels (all independently operated)
- No return path
- Eating into basic cable market rather than premium market
- Partially driven by analogue switch-off (2008-2012)
- New business models: Top Up TV

Now 7.9m DTT receivers in the market

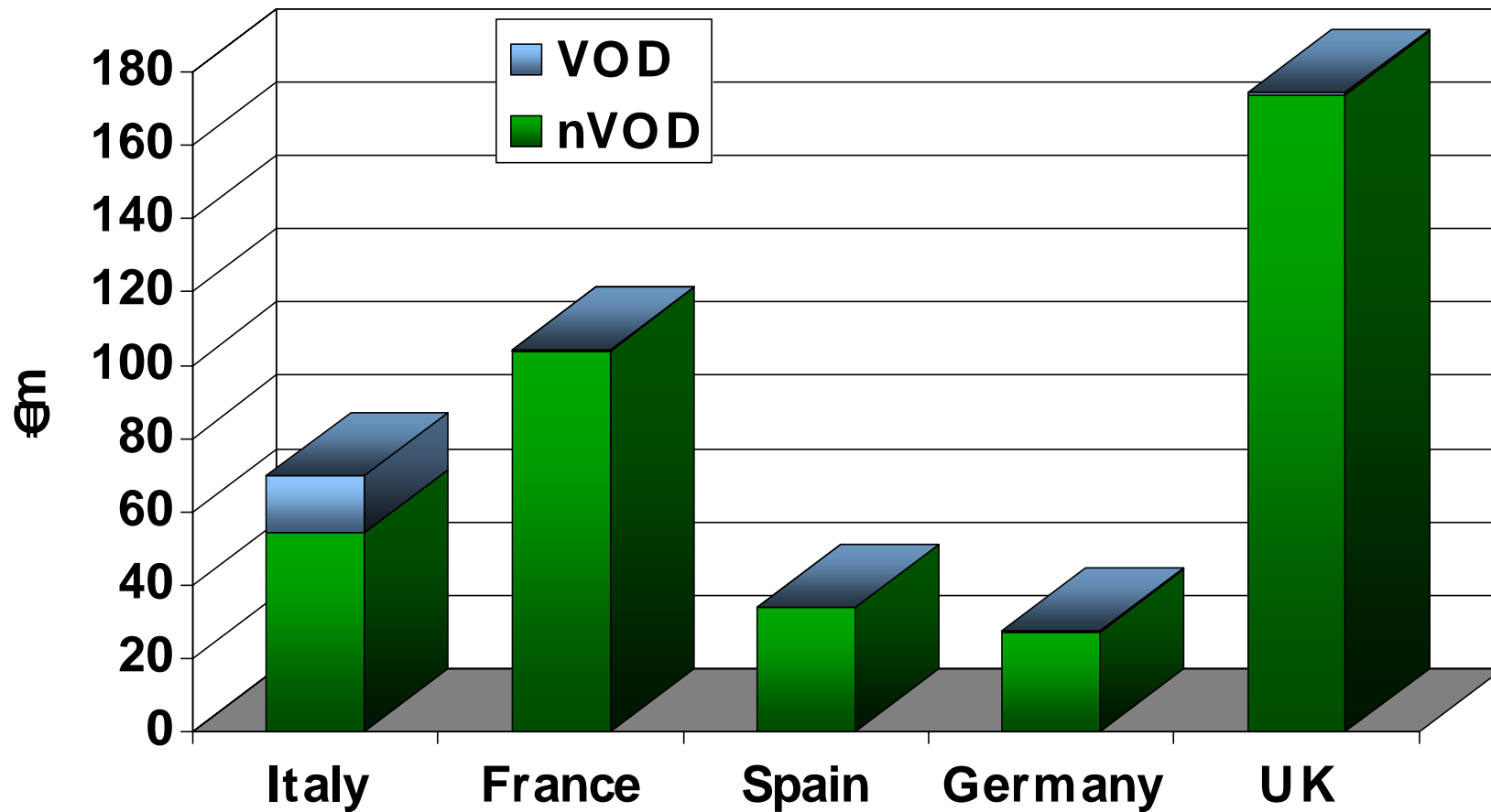
Cumulated DTT receivers Q2 2005



UK: Europe's most active VOD market

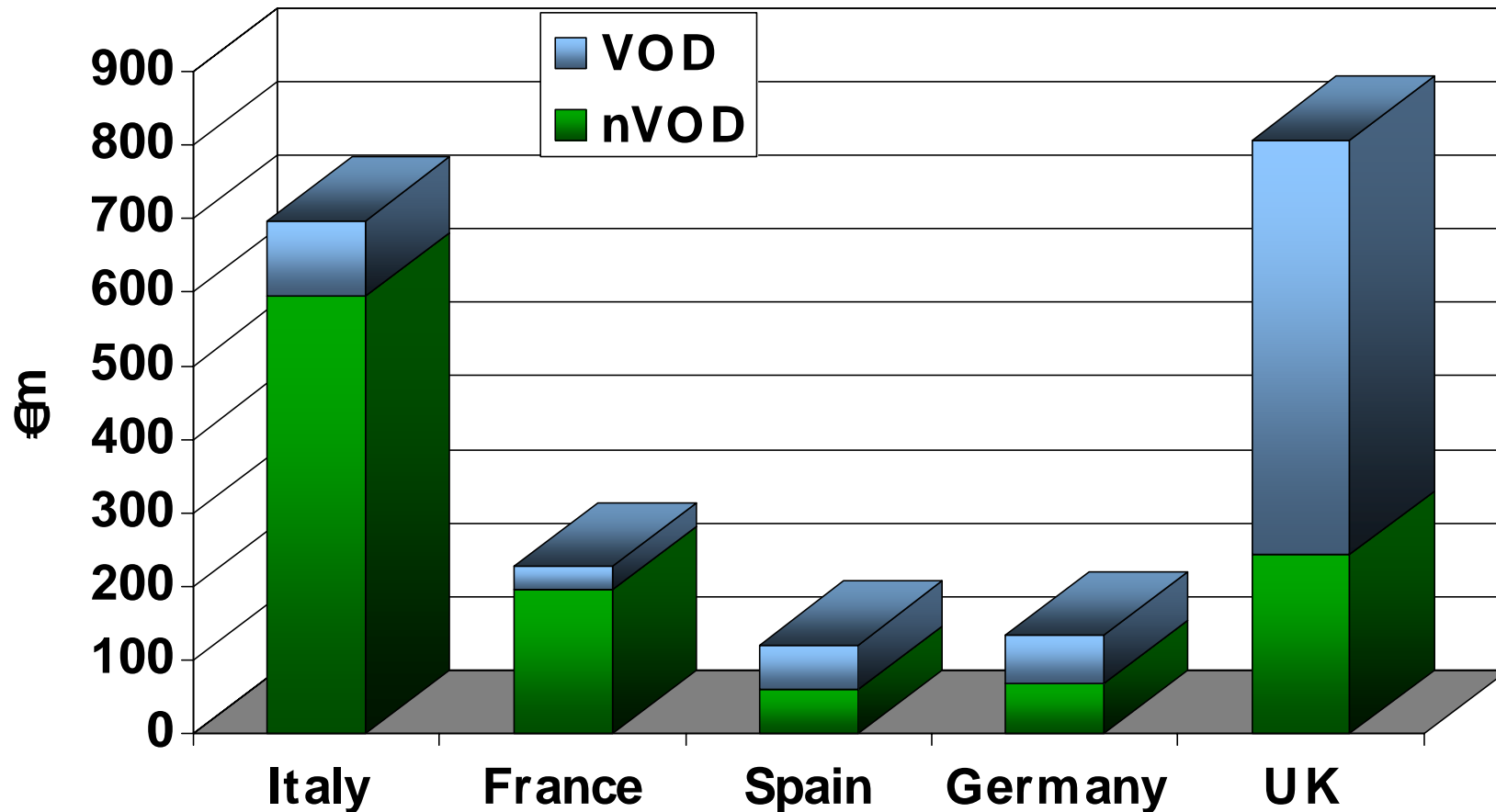
Homechoice	VOD, Pay TV	Active (2000)
Kingston	VOD, Pay TV	Active (1999)
Telewest/NTL	VOD, Pay TV	Active (Jan 2005)
BT Freeview Plus	VOD/Freeview hybrid	Planned mid-2006
BSkyB	Internet  hybrid?	Planned end 2005

Revenues: nVOD/VOD mix 2004



Sky dominates in Europe

Revenues: nVOD/VOD mix 2009



DTT nVOD drives strong Italian growth

Final thoughts

- The digital TV market is becoming increasingly competitive
- Revenues and margins are being squeezed in the core business models
- Interactivity enables some promising new revenue models, but don't get carried away by the hype!
- On-demand TV is - finally - coming of age
- PVR technology will become increasingly mainstream and an important means of generating new revenue streams
- HDTV will emerge as a key differentiator of premium services before becoming mainstream

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