

Audiovisual industry and the structural factors of the television crisis

A indústria audiovisual e os fatores estruturais da crise televisiva

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ABSTRACT

This article analyzes the current state of traditional television financing resources, detecting critical situation in its three main sources (advertising, subscriptions and service charges). Next, it discusses the most dynamic part of the television sector: Video on Demand (VoD) and Subscription Video on Demand (SVoD) services, which could generate new resources for audiovisual production. However, the analysis of the catalogues of these services shows a low supply of European movies compared to the United States of America. Thus, as on other occasions, the development of new television services and new business models could be a missed opportunity for the European audiovisual industry.

Keywords: Political economy of communication, television, audiovisual industry, video on demand

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RESUMO

Este artigo analisa o estado atual dos recursos tradicionais de financiamento da televisão, detectando uma situação crítica em suas três fontes principais (publicidade, assinaturas e taxas de serviço). Em seguida, discute a parte mais dinâmica do setor televisivo: os serviços de *Video on Demand* (VoD) e de *Subscription Video on Demand* (SVoD), que poderiam gerar novos recursos para a produção audiovisual. Porém, a análise dos catálogos desses serviços mostra baixa oferta de filmes europeus, em comparação com os dos Estados Unidos. Desse modo, como em outras ocasiões, o desenvolvimento de novos serviços de televisão e de novos modelos de negócio pode ser uma oportunidade perdida para a indústria audiovisual europeia.

Palavras-chave: Economia política da comunicação, televisão, indústria audiovisual, vídeo sob demanda

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INTRODUCTION

Conditions of growth and prospects of the audiovisual industry depend, obviously, on the combination of many factors. Among them, the three main factors are: available resources, consumer behavior and State intervention in regulatory terms. The proposal of this article is to verify the situation and trends facing the economic resources intended for television, because much of the national audiovisual production, as well as the behavior of viewers, depends on the stability of the economic model and its possible mutations.

To go beyond the acknowledgment of the current situation and subsequent trends, I believe it is necessary, first of all, to try to distinguish in the Italian television the phenomena related to conjuncture factors, which are potentially surmountable, from those that depend on structural changes, probably irreversible. Based on this, it is possible to assess the impact of new business models that are advancing in the television market and, in particular, non-linear services as the *Video on Demand* (European Audiovisual Observatory, 2016). Non-linear services offer audiovisual content without the immobility of the schedule program, allowing the viewer (according to various payment forms) to choose from a catalogue of thousands of titles of their choice, ordering and watching via the internet at the preferred moment and device (TV, PC, i-Pad, smartphone etc.).

They currently represent, along with the cell games, the most dynamic part of the audiovisual market, one that can generate growth of resources intended for the production of new television content. Concerning the non-linear television services, we will discuss it after evidencing the difficulty mentioned regarding resources generated by the linear television.

The period between 2010 and 2015 recorded, as it is noticeable, a profound crisis of Italian television activity (crisis that also occurred in many other European countries) and saw the first affirmation of a new mode of supply and access to television content online, raising new questions about the future of Italian and European audiovisual industry. In face of this, a new phase of very intense competition starts, especially among the audiovisual production companies and the *made in USA* products.

IMPACT OF THE 2007-2008 FINANCIAL CRISIS IN THE TELEVISION MARKET IN ITALY

The economic crisis that began in 2007 had a rapid impact on the television market, heavily focused on its main feature, the advertising, and also blocking the growth of other resources. From 2010 to 2015, based on data provided

by Autorità per le Garanzie nelle Comunicazione (Agcom)¹, total advertising investments destined to television have decreased: from 4.283 billion euros in 2010, they came to 3.223 billion in 2015 (24.7% less), the service charge² recorded a contraction of almost 3%, and the resources derived from paid TV subscriptions are getting substantially stagnant (from 3.007 billion euros in 2010 to 2.985 in 2015, 0.7% less). In general, as shown in Table 1, in the period under consideration, the resources earmarked for television activity substantially declined.

¹ Authority to Guarantee Communication, intended for communication regulation authority in Italy, specifically concerning pluralism of information (T.N.).

² In Italian, *canone* – broadcast TV service charge, paid by the Italians annually (T.N.).

Table 1 – 2010–2015 Total resources of television activities in broadcast and pay TV: advertising, service charge and subscriptions (billions of euros)

Year	2010	2015	2015/2010
Broadcast TV	5,619	4,530	-19,4%
Pay TV (*)	3,406	3,324	-2,4%
Total	9,025	7,854	-12,9%

(*) The 0.7% decline of subscriptions is added to 13% decrease of the advertising income

Source: Elaboration on data from Agcom 2016

Together with the economic crisis, however, there was a crisis that altered the traditional television market order, marked by changes in the behavior of viewers: a reduction in the consumption of the main generalist channels managed by Rai and Mediaset and the increase in the market for other minor channels.

Table 2 – 2010-2015 Annual television audience share, on average, per day

Year	2010	2015	2015/2010
Rai	41,3%	37,2%	-4,1%
Mediaset	37,4%	32,4%	-5%
Others	21,4%	30,4%	+9%

Source: Elaboration on data from Agcom 2016

In summary, between 2010 and 2015, all financing sources of television activities were resized and there was a net reduction in the audience of the main generalist channels.

Therefore, in the face of this situation, the two main questions to answer are:

- Will the three business models that prevail today in the television field, respectively based on the funding of the State (derived from the service charge), business (advertising) and domiciliary (subscriptions), be able to recover the lost resources and start a new expansion cycle, which

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- is essential to sustain the regime of rising costs that characterizes the television business in a competitive environment?
- Will the generalist television network, designed to attract large audiences, be able to recover the *lost* viewers after the fragmentation of supply and the new opportunities available to a growing number of people?

WITH WHAT RESOURCES? TOWARDS A STRUCTURAL CRISIS

Advertising, despite the drastic reduction suffered in the period considered, continues to be the main financing source of television activity, followed by the subscriptions and the service charge, although the last two items have increased when compared with the first.

Table 3 – 2010-2015 Resource input of the three main sources of financing for television (%)

Year	2010	2015
Advertising	47,5%	41%
Subscriptions	33,3%	38%
Service charge	19,2%	21%
Total	100%	100%

Source: Elaboration on data from Agcom 2016

The license fee for broadcasting

First, we will analyze the service charge, which represents the third television financing source in order of importance, but it is the first one of the historical point of view, at least in Europe. The perspective that predicts the increase of contribution charge for television activity and, in particular, for the production of content, seems unlikely. In fact, there are no conditions for that to happen, for reasons that are well known and mentioned here, but without going into details (Richeri, 2014). The service charge is a form of financing typical of public television monopoly, when all the Italians *consumed* only Rai programs. This is no longer the case because more than half of television consumption is in other channels, financed in other ways. The second consideration is that the service charge is basically a tax that governments prefer reducing rather than increasing. Also, historically, the service fee has long been justified by the fact that it serves the funding of a service of general interest, intended to satisfy the general *need* of information, culture and entertainment: when a large part

of the population had little or no opportunity to satisfy these needs. However, there has been some time that this situation no longer applies because nowadays the majority of the population has other opportunities to meet their cultural, entertainment, informational needs and aspirations through a variety of free and paid sources, being well off without the public TV services. Under these conditions, it seems unlikely the emergence of a “political will” able to increase income service charge in a way to be able to expand the resources for audiovisual production (also considering the reduction of bad debt, which relates to the legal obligation to pay the service charge).

Advertising

Advertising is the second relevant source of television resources. Also in this regard, growth prospects are not encouraging. After sharp decline, a result of the economic crisis that began in 2007–2008, which had a negative impact on GDP, industrial production and household consumption, in recent years, the seriousness of the situation seems attenuated, but not yet resolved. As it is notable, historically, advertising has never been used by companies with an anti-cyclical function: the recent crisis has shown that companies still consider advertising not as an investment but as a cost to be cut as soon as they feel the first negative signs (Richeri, 2012). As if things would be resolved when the economic cycle were in a new expansion phase. In the situation observed, however, some structural changes have been consolidated and weakened television as a means of advertising. There are three main aspects that support this assertion.

The first aspect is the progressive multiplication of TV channels and the resulting dispersion of viewers, from an increasingly fragmented offer of audiovisual content. Currently, in Italy, more than 30% of viewers prefer the *niche* channels that mostly have less than 1–1.5% of audience each. But in other European countries, where the fragmentation process is more advanced, viewers are dispersed in a larger number of channels with small audiences, reaching averagely 50% of all the audience. The most advanced case in this regard is the United Kingdom, where measurements of the *Broadcasting Audience Research Board* (Barb) evaluate the share of 300 TV channels, among a total of 526 (Ofcom, 2015). In the week from August 29th to September 4th 2016, for example, only two channels had share exceeding 10%, other five channels had share between 6% and 2% and the other more than 300 channels measured daily had, in total, an accumulated share of 51.13%, reaching a share inferior to 1% each.

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Table 4 – Share of the six major TV channels in the United Kingdom (from 8/29/2016 to 9/4/2016)

Channels	Share
BBC 1	20,4%
ITV	12,45%
BBC 2	5,22%
Channel 4	4,98%
Channel 5	3,5%
ITV HD	2,32%
Niche channels	51,13%
Total	100%

Source: Barb (2016)

The fragmentation process of television audiences has a negative impact on advertising investment. The example of the United Kingdom illustrates well what probably happens in other contexts. A considerable part of the TV audience abandoned the big generalist channels and migrated to the multichannel offer, consisting of hundreds of pay niche TV channels (where advertising plays a supporting role), of course, with very low ratings. The advertising slice of these hundreds of specialized channels is greatly reduced and, consequently, it also impacts their income. The values of the main variables – audience, advertising fees and income, investments in TV programming – are relatively inferior to traditional big generalist channels. In this situation, the advertising investment in channels with large audience, although in decline, tends to stagnate or decrease, whereas this investment in the set of channels with smaller audience tends to grow due to low values of advertising rates, which attract new advertisers (Ofcom, 2016).

There are three main negative impacts of audience fragmentation on advertising investments. Firstly, the advertisers, to reach a large number of viewers, should plan their advertising campaign in tens or hundreds of different channels, instead of a limited number of channels, and therefore they will have great organizational and negotiation costs. Furthermore, as it is known, the smaller the audience of a television channel, the harder it becomes to measure it (to keep the statistical deviation within an acceptable margin, when smaller is the audience, the greater must be the sample, but its dimension cannot grow much for financial reasons). If in the coming years the trend of fragmentation continues, it is likely that it will have a negative impact on the amount of resources earmarked for television advertising.

The second aspect relates to the fact that, in recent years, advertisers have focused part of their investments in other media, reducing the ones traditionally

intended for television. The area of greatest success has been the internet, which offers some advantages over television. To name a few: advertising has a lower cost on the internet, messages can be directed to a target audience, the measurement of the number of people affected by the advertising message is more accurate than the measuring of TV audience. The third negative aspect is represented by the new forms of commercial promotion as product placement (merchandising) and branded content, which are funded with budgets destined for advertising, but that normally do not generate resources for television companies (Dagnino, 2016).

Pay TV subscriptions

Currently, the subscriptions of pay TV comprises the second largest source of television financing after advertising, by order of magnitude. Even in this field, signs of slowdown and perhaps of stagnation can be observed. In fact, besides the decrease in the number of subscribers caused by the economic crisis, pay TV shows signs of saturation, both in Italy and in other European countries: on the one hand, the number of new subscribers is shrinking; on the other, the number of withdrawals have been increasing. Probably, this situation will not be resolved in the near future, mainly because the new video on demand service (*Video on Demand* – VoD) is growing in Italy and is concurrent of the pay TV offer.

In fact, the new VoD services, particularly those accessible by subscription, called Subscription Video on Demand (*Subscription Video on Demand* – SVoD), offer an attractive alternative to former pay TV subscribers as well as new subscribers. The competitive strength of SVoD services in relation to pay TV can be highlighted by the example of Netflix, case of greater international success. Netflix offers thousands of audiovisual products (including movies and recent TV series), available upon request at the desired moment, with a very cost-effective subscription in relation to pay TV.

The two groups more linked to the pay TV model are: viewers who do not want to invest time and attention to choose among thousands of movie titles available in a catalogue; and viewers who are interested mostly in live sports broadcasts, exclusively offered by pay TV. Those who decide to subscribe to a pay TV service mainly to have access to a range of cartoons (for children), recent and classic movies, may find better conditions in SVoD services to meet their needs: more titles, more variety, more flexibility with a lower price and also access to a large number of hit series. Netflix also has a personalized offer: to prevent the subscribers from investing too much time and to facilitate their

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choices among the thousands of titles in the catalogue, Netflix provides each subscriber a list of titles that better correspond to their user profile and their consumption habits.

AUDIOVISUAL PRODUCTION AND DEVELOPMENT OF NEW TELEVISION SERVICES

Considerations discussed so far highlight how three traditional economic sources of television activity do not exactly have encouraging future expectations. In fact, considering the recent data and ongoing developments in the television market, income from service charges has little chance of growth, as well as, for other reasons, the ones from advertising and subscriptions of pay TV. In this context, we cannot expect that the production of audiovisual content for television, especially the non-innovative ones, finds the resources needed to expand.

There are new television sectors that are growing both in terms of public and resources; and among these sectors, the most promising are the television services that use the world wide web as a distribution and access infrastructure: the so-called Over the top (OTT) services.

According to a recent survey of the European Audiovisual Observatory (EAO), the main factor of success of Ott video service is the possibility of subscription of video on demand services (SVoD), offered by companies such as Netflix and Amazon. This is not a novelty: “SVoD services existed in the most important markets before the entry of these two SVoD service providers, but their marketing strategies [...] coupled with attractive content, multi-screen availability and ease of use has appealed to European customers” (EAO, 2015: 139).

The strategy of penetration of two U.S. companies was well calculated to strengthen their presence in privileged European countries, and then it spread throughout the rest of the European Union:

Netflix and Amazon also decided to expand first to the countries that presented the most favorable market conditions for digital services, such as broadband penetration in households, high level of equipment in connected device such as smartphones, smart TVs and fairly mature digital economy (e-commerce, offer of digital media) and a tech-savvy population. (Ibid.: 139)

Since the autumn of 2015, Netflix began operating in Italy; therefore, it is worth a reflection especially regarding the contribution of that company, and of those that have a similar business model for the audiovisual production in Italy and the rest of Europe. We take as a reference another article that presents

in detail the Netflix's business model, which appears as the most advanced in comparison with other companies in the sector (Richeri, 2015). The main issue to consider here is how the success of Netflix and similar businesses can benefit, in a non-marginal way, the growth in the European television industry and particularly in the Italian industry.

To answer this question, we used data provided by a study published in 2015 (Ene; Grece, 2015) on the origin of audiovisual products offered in catalogues of 75 VoD services and 17 SVoD services in some countries of the European Union (EU).

Table 5 – Region of origin of movies offered in catalogues of 75 VoD services in the EU in 2015

	Accumulated titles	Single titles
European Union	27%	43%
Other european countries	2%	3%
United States of America	59%	41%
Other non-european countries	12%	13%

Source: EAO (2015) *apud* Ene and Grece, 2015

Titles of the products offered were divided into two broad categories, and then according to region of origin: 167,676 accumulated titles, which represent all titles in catalogues of the 75 VoD services considered (each movie can be counted several times) and the single titles, 28,000, which represent the set of individual titles (the same movie present in most catalogues is counted only once). This means that, on average, each title was present in catalogues of 5.8 VoD services.

Table 5 shows that movies produced in the European Union represent 43% of the titles offered, but only occupy 27% of total supply, whereas the USA have 41%, but are responsible for 59% of the global supply.

In other words, catalogues of VoD services in each country researched offer a percentage of national movies, but that are not exported, since they are not present in VoD catalogues of other European countries. On the other hand, most U.S. movies are simultaneously present in the catalogues of many European countries. Therefore, whereas a European title is distributed only in the country of origin, a U.S. title is respectively explored in various European countries. As a result, from the economic point of view, we see that a U.S. title is potentially more profitable than a European title.

The same survey also examined 16 catalogues of SVoD services, where they identified 17,800 accumulated titles (present in most catalogues) and 8,300 single

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titles. In this case, the U.S. titles have a stronger position than in the previous case, since they represent 60% of accumulated stocks and 51% of individual titles against, respectively, 30% and 38% of the titles produced in the European Union (Ene; Grece, 2015).

Considering the specific case of Netflix, which currently represents the most successful SVoD service, both in the U.S. and in Europe, the situation for audiovisual products in the European Union is even more critical than in previous cases.

In October 2015, in the Netflix catalogues of eight European countries, the average number of movies was 1,151 (Italy was not considered because Netflix had not yet begun to operate at the time of research). In all eight countries considered in the research, from the titles in the catalogue, 6% were national audiovisual products, 21% produced in other European Union countries and 69% were originated in the U.S.A. Details of the three main EU countries considered in this research are in the following table.

Table 6 – Netflix catalogue content in three European countries (October 2015)

	National	EU	USA
Germany	6%	25%	64%
France	15%	26%	53%
United Kingdom	10%	17%	69%

Source: Netflix

Thus, in the three countries analyzed, most of the titles offered by Netflix are from the USA; the titles of European origin are more present in France, where they represent 41% of the total, followed by Germany with 31% and in the United Kingdom, with 27%.

CONCLUSION

After analyzing growth potential of traditional television resources and detecting a critical situation in the three main financing sources – advertising, subscriptions and service charges –, we started to analyze the new non-linear television services, *Video on Demand* (VoD) and *Subscription Video on Demand* (SVoD). In Italy, as in the rest of Europe, these represent the most dynamic part of the television industry, one capable of generating new resources that may be partly intended for the production of audiovisual content.

An analysis of the VoD and SVoD services catalogues, offered in various European countries, shows low offer of European movies in comparison with

those from the United States, which are likely to collect most of the generated resources. As it has happened when the commercial television expanded and as was repeated with pay TV, the development of new TV services and new business models can be a lost opportunity for the Italian audiovisual industry, which would only have secondary benefits.

Therefore, some issues should be discussed to think of initiatives (laws, regulations, restrictions) able to take advantage of the new non-linear television services and bring advantages for the Italian and European audiovisual industry. Among them, at the conclusion of this article, we present two:

- Are there conditions to define a *quota* of European products in catalogues of VoD and SVoD services?
- Are there conditions to force the investment of a significant portion of profits generated by VoD and SVoD services in national and European audiovisual production? 

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