



Governance Unit

# **PSB Freesat: BBC Governance Unit review of market implications**

**November 2006**

## Contents page

Section 1	Purpose of the report .....	3
Section 2	The proposition .....	3
Section 3	Key findings .....	4
Section 4	Methodology .....	5
Section 5	Definition of relevant markets.....	6
Section 6	Counterfactual.....	11
Section 7	Assessment of the impact of the proposal .....	11
Section 8	Conclusions .....	15

## Section 1 Purpose of the report

1. This paper provides a desk based review of the potential market implications of the 'PSB Freesat' proposal. This review is **not** intended to provide a definitive view of the potential market impact. The review has been prepared by the BBC Governance Unit solely to inform the BBC Governors' wider thinking in relation to the proposal.
2. The review has been based on analysis conducted by BBC management as part of their submission to Governors and published sources of information.
3. Under the current Charter and Agreement the Secretary of State's permission is required before the launch of a joint venture – hence the application from the BBC Governors in this case given the intention to launch PSB Freesat as a joint venture with other PSBs.
4. Governors have also considered the new Charter and Agreement due to come into force on 1 January 2007 when approaching this issue. As a 'non-service'<sup>1</sup> the PSB Freesat proposal need not be subject to a formal Public Value Test. Nor does the analysis contained in this note rely on the Ofcom methodology for the conduct of the MIA process, although it has regard to those principles. Therefore, this note does **not** therefore represent a Market Impact Assessment (MIA), as required under the Public Value Test framework.

## Section 2 The proposition

5. The BBC intends to deliver a universally available free satellite offering, referred to hereafter as "PSB Freesat" or "the proposition". Permission is sought from the Government in order to do this as a joint venture with other public service broadcasters.
6. The proposition would be expected to offer Standard Definition (SD) services. However as a satellite service it would be possible for HD services to also be carried on the platform. Commercial PSBs would be able to do so subject to the normal licensing requirements of Ofcom. For the BBC to offer a HD channel would require it to be considered under the new Public Value Test Framework established by the new BBC Charter and Agreement that comes into force on 1 January 2007.
7. Therefore, it is important to note that the Secretary of State's approval is only sought in relation to the joint venture. This assessment by the Governance Unit is limited to the establishment of the platform and the operation upon that platform by the BBC of its existing (SD) services. This assessment does not consider those issues related to any future assessment applied by the BBC Trust to the launch of any HD services by the BBC.
8. It is intended that PSB Freesat would be responsible for the collation and transmission of system management and schedule data, the development and maintenance of open

---

<sup>1</sup> Clause 22 of the new BBC Agreement provides a description of non-service activities as applied under the new Charter and Agreement.

technical standards for broadcasters and receiver manufacturers and the marketing of the proposition. PSB Freesat would not manufacture or supply equipment

9. Manufacturers will offer consumers a range of set top boxes (STBs). It is proposed that these would range from basic to high specification functionality, and would be available as either Standard Definition (SD) or High Definition (HD) ready (i.e. capable of receiving and playing HD output). It is also expected that the Proposition will have Personal Video Recording ("PVR") functionality.
10. PSB Freesat is expected to be available to between 96 and 99% of households in the UK. BBC management hopes it will initially carry all channels broadcast 'in the clear' (which currently includes all ITV and BBC digital radio and free-to-view digital TV services) and an electronic programme guide. PSB Freesat would also allow broadcasters to provide richer interactive services than are currently available through Freeview as it will not suffer the same bandwidth constraints.
11. PSB Freesat is to be available subscription free, following a one-off purchase and installation of the necessary equipment. This one-off cost is expected to be in the region of £[ ], plus installation of between £[ ] depending on receiver options.
12. The BBC intends to provide the Proposition either on its own<sup>2</sup> or through a joint venture ("JV") with other public service broadcasters. The primary role of the JV would be to facilitate the development of a supply chain (e.g. manufacturing, installation, retail), manage the Electronic Programming Guide (the "EPG"), issue technical specifications and develop/promote the PSB Freesat brand. The JV would not fund STB manufacture, nor would it be involved in the supply chain, installation or post-sales – this will be left to the market.

### **Section 3**                      Key findings

- The roll-out of PSB Freesat may encourage some consumers to switch from their existing digital providers (or in the case of analogue households, choose PSB Freesat over an alternative digital offering).
- Given the similarity of offerings, the proposal is most likely to impose a competitive constraint on Freesat from Sky.
- The proposal may also have some effect on subscription services. It is possible that the effect may be concentrated at the level of 'basic' subscription services, which in the consumers' view may be comparable to the PSB Freesat proposition. However, the overall effect on subscription providers may be mitigated on the basis that the purchase by an end-user of a satellite system would allow an easier upgrade to subscription satellite services.
- Even in the event PSB Freesat were able to achieve the highest possible expected level of take-up, such take-up is likely to represent less than 9% of the total number

---

<sup>2</sup> Under the present Charter and Agreement this would not require the Secretary of State's consent

of households by 2012 and more realistically 4% of households<sup>3</sup>. Therefore, whilst PSB Freesat may exercise a competitive restraint on competing services, it is highly unlikely to deter significant levels of investment or result in market exit. On the contrary, it is conceivable that PSB Freesat may lead to positive effects for other operators, in the event such operators were to seek to provide pay packages as an add-on to PSB Freesat.

- For consumers, competition may also be further strengthened by the introduction of PSB Freesat, as it provides an alternative supplier of digital TV retail offering to almost all households in the UK. A proportion of these households can currently opt for one provider only. The impact of competition will be particularly strong in those areas outside of the current Freeview footprint.
- The principal effect of approval is therefore likely to be in areas in which Freeview is currently unavailable or less available, which includes the Borders area due to switchover in 2008. It should be noted that Digital UK marketing is encouraging consumers to switch now.
- PSB Freesat might lead to a change in pricing strategy by existing suppliers. For example, Sky might respond to its launch by lowering the price of its free satellite package. The Switchover Select Committee recently noted that<sup>4</sup>, “The BBC/ITV Freesat platform would also provide competition and potentially, lower prices...”

## Section 4 Methodology

13. In assessing the potential implications for the market, the following methodology was adopted:

- Definition of relevant markets
- Assessment of possible counterfactual scenarios
- Assessment of ‘static’ impact of the proposal on:
  - Participants in the market
  - Consumers
- Assessment of ‘dynamic’ impact of the proposal on:
  - Participants in the market
  - Consumers
- Conclusions and assessment of overall effects

---

<sup>3</sup> It is open to debate whether or not PSB Freesat’s other customers (e.g. existing analogue households, pay refuseniks) would have eventually chosen an existing offering without some form of government intervention.

<sup>4</sup> “Report by the Switchover Select Committee”, 30 March 2006

---

## Section 5

## Definition of relevant markets

14. As a first step it is necessary to identify those markets which will be affected by the proposal. For simplicity, we have categorised these 'markets' as either:
- Relevant economic markets i.e. the products that will, in some way, compete with the proposition; or
  - Other economic activities i.e. the related economic activities that may be impacted by the proposition.
15. It is necessary to consider related economic activities because the proposal may create externalities in markets beyond those which the proposal itself directly competes. For example, additional demand could be created in upstream markets, stimulating increased production which would not have occurred had the proposal not been introduced. Conversely the proposal could have a negative effect on such markets.
16. A definition of the relevant market(s) must take into account inter alia, the nature of the proposition and the characteristics of demand and supply. In simple terms, market definition is based on an assessment of the following competitive constraints<sup>5</sup>:
- Demand-side substitution i.e. would consumers substitute other market offerings for PSB Freesat (and vice versa)?
  - Supply side substitution i.e. is it possible for suppliers to switch relatively easily to the provision of a new digital TV retail offering (and vice versa)?
17. For simplicity this paper outlines what the GU believes are the most credible, alternative market definitions from which to assess the impact of the proposition. It is important to note that this assessment does not purport to provide a definition of the relevant economic market for the purposes of EC and/or UK competition law.

### Demand side considerations

18. From a demand-side perspective, the proposal has been considered in relation to differences in product characteristics (e.g. channel line-up, price) with other potentially substitutable products.
19. PSB Freesat offers a means by which consumers (i.e. viewers) can access a variety of digital TV channels. It therefore makes sense to focus the assessment on potential competitive constraints that PSB Freesat could impose on other providers of digital TV retail offerings. The table overleaf describes the key characteristics of the current market offerings.

---

<sup>5</sup> These principles are similar to those applied in the Hypothetical Monopolist Test, whereby a product is considered to constitute a separate market if a hypothetical monopoly supplier could increase prices by 5-10% above the competitive level (or lower the quality of a service by a comparable proportion) without switching by customers to alternative products or entry/expansion by other suppliers such that the price increase (or quality reduction) would become unprofitable.

20. As part of this we also need to consider the likely uptake of any PSB Freesat Service. As part of this assessment the GU looked at research commissioned by BBC management<sup>6</sup>. This suggested that highest possible take up of the proposal by 2012 will be approximately 2.5 million households<sup>7</sup>. There is good reason to believe that this may be an over-estimate of the potential impact of the proposition in the short term.
21. First, this forecast is based on the provision of both SD and HD+SD - enabled versions of the receiver, which is expected to increase the take up of the Proposition. Assessed on a SD only basis, the estimate in this work fell to nearer 0.5m. It should therefore be noted that under the BBC management's model HD is a significant factor in driving demand, however were BBC management to wish to launch a BBC HD service this would need to be considered separately under the Public Value Test framework
22. Second, the forecast was highly susceptible to the competitive response of Sky to the A more conservative scenario forecasts that the SD+HD Proposition may attract 1.1 million customers over the same period. Given the potential range, the most cautious approach in terms of potential impact on competitors has been adopted throughout the review and all potential impacts on the market are considered in terms of the upper 2.5 million range. Any actual impact may therefore well be significantly more limited than that suggested by management's analysis.
23. As part of the desk based review we have not undertaken a detailed analysis of the research commissioned and presented by BBC management. For the purposes of this basic assessment, the GU's consideration was limited to consideration of what a reasonable figure for impact might be based on a SD services from the BBC (0.5m). We also sought to test a cautious proxy "upper figure" (in the absence of any better estimate we used 2.5m whilst recognising the latter is based on BBC HD services being in the mix which would require separate approval from the Trust and therefore be fully considered in detail under the Public Value Test framework).

---

<sup>6</sup> The research was conducted by BMRB and Scientific Generics

<sup>7</sup> This analysis is based on the number of households and not the number of STBs purchased per household. The analysis also assumes that the majority of households will select a single provider for all their digital TV usage and will not rely on multiple providers in the same household

---

**Table 1: Key characteristics of existing digital TV retail offerings**

<b>Offering</b>	<b>Delivery method</b>	<b>HD element</b>	<b>Payment mechanism</b>	<b>Channel portfolio</b>	<b>UK coverage</b>	<b>Current forecast household take-up</b>
PSB Freesat (proposed)	Digital satellite	Yes – although separate permission required for BBC HD services	One-off, upfront payment for range of receiver options (£[ ]), plus installation (£[ ])	Intended to include BBC, ITV, C4 and C5 free digital channels with up to 200 other channels.	96-99%	Estimated take-up of max. 2.5m by 2012 (assuming HD) 0.5m SD
Freeview	Digital terrestrial	Unlikely prior to 2012	One-off, upfront payment for range of receiver options (£30-200)	30+ channels, including all BBC, ITV, C4 and C5 free digital channels.	75%	6.5m
Freesat from Sky	Digital satellite	No – only via subscription	One-off, upfront payment for standard receiver (£150 including installation)	160+ channels including all BBC, ITV, C4 and C5 free digital channels.	99%	0.6m (incl. other non-pay options)
Sky Pay packages	Digital satellite	Yes	Various subscription packages (£15-42.50 per month)	Various packages on top of Freesat from Sky	99%	All Sky 7.7m
Top Up TV	Digital terrestrial	Not expected before 2012	Single subscription package	11 channels	Close to Freeview but limited STB compatibility	Less than 0.1m
NTL/Telewest	Analogue / Digital cable	Yes, but only an on-demand service at present	Various subscription packages (£15.50 to £29.50 per month)	Various channel, internet and telephony packages	50%	3.3m
Homechoice	ADSL	Plans unknown	Various subscription packages	Various channel, internet and telephony packages	Parts of London only	Less than 0.1m

Sources: BBC management estimates and assessment, as at June 2006  
[www.ofcom.org.uk/research/tv/reports/dtv/dtu\\_2005\\_q4/](http://www.ofcom.org.uk/research/tv/reports/dtv/dtu_2005_q4/)  
[www.ofcom.org.uk/consult/condocs/promotion/](http://www.ofcom.org.uk/consult/condocs/promotion/)

24. The Table indicates that the two closest offerings to PSB Freesat are Freesat from Sky and also Freeview. This is based on inter alia the following factors:

- Content - the channel line up on PSB Freesat is likely to be similar to Freesat from Sky and Freeview.
- Pricing - all require a one-off payment and no subscription thereafter
- Coverage - all three are available to the majority of UK households.

25. Subscription digital providers (e.g. Sky, NTL/Telewest and so on) also carry similar 'core' channels. However, they also offer a wide range of additional 'premium' channels. Previous decisions by the European Commission have suggested that there are separate markets for pay and free to air TV. Moreover, the offering of different combinations of channels at different prices could also imply that consumers have significantly different preferences. It is uncertain to what extent there is a chain of substitution between subscription and non- subscription services.

26. In addition to the carriage of channels, some suppliers also offer other services such as internet access and telephony.

27. Another consideration is the functionality of the proposal and in particular the availability of HD. PSB Freesat STBs are likely to be available in both a SD and HD-ready format from launch. However, currently, HD is only available from subscription providers and no PSB offers HD. For the BBC to do so would require separate approval under the Public Value Test framework.

28. Therefore in the short term there is likely to be no direct competitive effect on either providers of platforms offering HD services or platforms that do not.

29. In theory, at the margin, PSB Freesat could place a competitive constraint on those providers who do not offer HD ready output, such as Freeview, as consumers choose to purchase the product with greater future functionality. It may also place a constraint on subscription HD providers if consumers opt for HD-ready PSB Freesat boxes, on the assumption they may receive free HD services in the future, although the range of content available on such channels, such as premium movies and sports HD output may not necessarily be available through a PSB Freesat receiver.

30. A proper consideration of the scope of the relevant market should also take into account the competitive constraints that may arise from future offerings. However, it is very difficult to define relevant markets in sectors where technology is fast-changing and future consumer behaviour is highly unpredictable. It is evident that one source of potential competition could be the major telcos/ISPs (or, indeed, any company that obtains access to the broadband network). These digital offerings are currently in their infancy and it is not clear how they will develop<sup>8</sup>. At present, it is reasonable to assume that these products may not form part of the relevant market<sup>9</sup>.

---

<sup>8</sup> For example, will these providers offer an entire channel or groups of channels, or will the content be limited to on-demand programmes? What business model will succeed – one-off, advertising, subscription, pay-per-view? Will a significant number of consumers consider these products to be credible substitutes for existing products or will they be complementary?

<sup>9</sup> It cannot be ruled out that in the medium term these emerging products will form part of the relevant market.

### Supply side considerations

31. The potential for supply-side substitution would appear to be limited to the provision of a new, digital TV retail offering either via satellite<sup>10</sup> or, more likely, via the national broadband network infrastructure. There are a number of companies beginning to roll-out products which will utilise these distribution mechanisms. For example, BT recently announced that it intends to rollout digital TV via its broadband network during 2006.

### Geographic considerations

32. The geographic scope of the relevant market is assumed to be UK-wide. This is because:

- The coverage of PSB Freesat will be UK-wide
- Suppliers typically offer uniform prices to consumers no matter how fierce the degree of local competition.

### Other Economic Activities

33. It is also necessary to identify which other economic activities may be affected in order to assess the overall impact of PSB Freesat. This is a complex task since a wide range of economic activities may be affected by the launch of PSB Freesat. For simplicity, we have identified three broad categories of economic activity that may be affected by the launch of PSB Freesat:

- Digital take-up – will the roll-out of PSB Freesat contribute to digital take-up providing associated economic benefits?
- Channels & Distribution – will individual TV channels benefit or suffer following the introduction of PSB Freesat? What impact will PSB Freesat have with respect to the relative attractiveness of different distribution platforms (e.g. satellite v. cable)?
- Suppliers – how will companies along the supply chain (e.g. STB manufacturers, installers, retailers) be affected by the proposition?

### Preliminary Conclusions on market definition

34. The relevant market in which PSB Freesat is expected to compete may be defined as the provision of digital TV retail offerings in the UK. It is possible that the economic market may be further delineated. In our view the narrowest possible market could be defined as including free satellite offerings (e.g. Freesat from Sky) only. However, there may be a chain of substitution with certain subscription packages – although such substitution may be limited to the most basic and least expensive of such packages.

35. In the medium term, other suppliers (e.g. BT, Google) may also emerge as credible competitors

---

<sup>10</sup> A new satellite offering could utilise spare capacity in the existing transmission network but would require considerable technical and logistical expertise in order to provide the necessary support.

36. Wider economic markets include upstream suppliers and individual channels.

## **Section 6** Counterfactual

37. This section considers how the relevant market may develop without PSB Freesat<sup>11</sup>. In the absence of the proposal, the take-up of digital TV is expected to continue to grow towards Digital Switchover, although the market alone may not be able to deliver universal uptake.

38. The BBC is unaware of any other existing or potential supplier seeking to launch a non-subscription/ non-pay-per-view digital TV retail offering in the near future. The most likely business models are ones involving some form of subscription and/or pay-per-view element. In particular no other satellite provider is expected to enter the sector, given barriers to entry and long standing lack of competitive entry in that sector.

39. Barriers to entry are expected mainly to consist of a large installed subscriber base of satellite dishes and limited satellite capacity able to service that installed base.

40. The degree of consumer choice for pay offerings is expected to increase in the future however, in particular as broadband and HD take-up increases and the major multimedia firms expand their product offerings.

## **Section 7** Assessment of the impact of the proposal

41. The purpose of this section is to provide a high-level assessment of the potential market impact of PSB Freesat. It is divided into four parts:

- Assessment of 'static' impact of the proposal on:
  - Participants in the market
  - Consumers
- Assessment of 'dynamic' impact of the proposal on:
  - Participants in the market
  - Consumers

### 'Static' impact of the proposal on participants in the market

42. Static impacts refer to those shorter terms effects which occur from the entry of a new service into the market. It is likely that the roll-out of PSB Freesat, will encourage some consumers to switch away from their existing providers (or in the case of analogue households, choose PSB Freesat over an alternative digital offering).

43. The BBC management's research suggests that in their highest uptake scenario, approximately 1.5 million households of the 2.5 million total number of PSB Freesat customers may be 'conversions' from another digital TV retail offering.

---

<sup>11</sup> For simplicity, we have not attempted to predict how the other related economic activities identified in Section 5 may develop without the proposition

44. On this basis, the Proposition may impose a competitive constraint on Freeview and Freesat from Sky. There is little available evidence on the degree of actual switching between different digital TV retail offerings, whether between subscription and non-subscription or between different gradations of subscription (basic, premium).
45. Table 2 provides an indication of the current scale of customer churn within the different forms of digital TV retail offerings. It is unclear to what extent customers are switching to another product or simply cancelling their subscriptions. However, the overall numbers appear to be quite high which may suggest that consumers are willing to change providers should they be incentivised to do so.

Table 2 - Estimated churn rates for selected digital TV retail offerings

Service	Estimated Churn Rate for Q1 2006	Equivalent Number of Subscribers
Sky Pay	11%	Approx 0.9m
NTL / Telewest	16%	Approx 0.5m

Source: [http://www.ofcom.org.uk/research/tv/reports/dtv/dtu\\_2006\\_q1/dtu\\_2006\\_q1.pdf](http://www.ofcom.org.uk/research/tv/reports/dtv/dtu_2006_q1/dtu_2006_q1.pdf)

46. The proposal may also have some effect on subscription services, potentially more centred on existing 'basic' subscription users where the similarities between the proposal and existing services is arguably closest. However, this effect may be mitigated overall by the potential for increasing demand for subscription services through the expansion of the market. For example, some of the relevant households may upgrade or swap from the Proposition to competing premium offerings once the benefits of digital TV are fully appreciated. The purchase of a satellite system would allow an easier upgrade to subscription satellite services, although this effect is obviously likely to be smaller for cable providers.
47. Even in the event the Proposition were able to achieve the highest possible expected level of take-up, such take-up is likely to represent less than 9% of the total number of households by 2012 and a more realistic estimate is likely to be 4% of households. Therefore, whilst the Proposition may exercise a competitive constraint on competitors, it is highly unlikely to deter significant levels of investment or result in market exit.
48. There may also be positive effects for other operators (e.g. Top-Up TV, BSkyB) if they seek to provide pay packages as an add-on to PSB Freesat, or households may choose to switch to an alternative 'subscription-based' offering. The success of Top-Up TV as an add-on to Freeview provides some evidence to support this argument. Top-Up TV expected to have around a quarter of million subscribers by the end of 2005<sup>12</sup>, even though it is only compatible with the STBs in around one quarter of Freeview homes.

<sup>12</sup> <http://www.digitalspy.co.uk/article/ds19134.html>

### 'Static' impact of the proposal on consumers

49. The relevant market – whether non-subscription only or all digital TV retail services - is currently highly concentrated. In some regions of the UK there is only one supplier (Sky). There are very few households that have access to more than three different suppliers.
50. The introduction of PSB Freesat will add another choice of digital TV retail offering to almost all households in the UK, thereby strengthening competition. This effect will be particularly strong in those areas outside of the current Freeview footprint and for consumers that do not consider any other retail package (pay or free) to be a worthwhile option.
51. Although formally outside the scope of this assessment it is also worth noting that the HD version of PSB Freesat will provide consumers with an alternative to the existing HD TV services (which are likely to be limited to Sky HD and the on-demand service of NTL/Telewest in the short term). Sky's HD offering is currently subscription-based although any consumer with an HD STB will be able to pick up the BBC's HD trial service<sup>13</sup>. The degree of competition between PSB Freesat and other digital TV retail offerings may be affected by how quickly broadcasters launch HD versions of their channels and whether they choose to make these channels subscription-free or to form part of, say, Sky's pay service.
52. PSB Freesat might lead to a change in pricing strategy by existing suppliers. For example, Sky might respond to its launch by lowering the price of its free satellite package. The Switchover Select Committee recently noted that<sup>14</sup>, "The BBC/ITV Freesat platform would also provide competition and potentially, lower prices..."
53. There could also be secondary effects on the pricing of Sky's (and other companies') pay services if existing customers seek to downgrade their packages.

### 'Dynamic' impact of the proposal on participants in the market

54. It is difficult to predict whether or not PSB Freesat will deter any investment by potential new entrants. On one reading, the decreasing size of the most lucrative elements of the market (i.e. those households most willing to pay for premium services), the reputation and first-mover advantages of Sky and the recent announcements by multimedia giants such as BT and Google to enter the market, suggest that opportunities for launching a new digital TV retail offering (especially a 'free' one) are increasingly limited.
55. The adverse effects of the proposal on new investment or entry may therefore be expected to be limited. In addition the proposal could potentially support the roll-out of small scale pay services as an add-on to the PSB Freesat service, as although PSB Freesat itself will not be a subscription service, there may be opportunities for third parties to develop a pay offering that is compatible with its STBs.

---

<sup>13</sup> Whilst the trial has permission to continue. Launch of a full service by the BBC would have to be considered under the Public Value Test framework

<sup>14</sup> "Report by the Switchover Select Committee", 30 March 2006

### 'Dynamic impact of the proposal on consumers

56. The introduction of PSB Freesat may encourage other suppliers to strengthen their competitive offerings. This would benefit consumers by encouraging the development of new product offerings such as greater interactivity and HD.

57. The broadcasting sector is currently undergoing a period of rapid change. It is impossible to predict with any certainty how far-reaching these developments will be. The large multimedia firms such as Google, BSkyB and Microsoft are devoting vast resources into developing new ways of accessing audiovisual content. The roll-out of PSB Freesat will not halt this process nor is it likely to have a material impact on whether the initiatives succeed or fail.

### What is the potential impact of the proposition on other economic activities?

58. For simplicity, we identified three main categories of economic activity that may be affected by the launch of PSB Freesat i.e. digital take-up, channels & distribution and input suppliers.

#### *What is the potential impact on digital take-up?*

59. The rollout of Freeview led to an acceleration in digital TV conversion across the UK. Freeview's success has shown the appeal to consumers of a simple subscription-free proposition – penetrating population segments that have traditionally been more resistant to multi-channel TV. PSB Freesat is intended address areas outside of the Freeview footprint as well in households that have so far resisted digital conversion.

60. It is expected that PSB Freesat will provide a contribution towards the growth of Digital Britain albeit on a smaller scale than Freeview. Recent research undertaken for the BBC suggested that the roll-out of PSB Freesat could, in the best case scenario, lead to around a million households converting to digital (by 2012) that may not have otherwise done so without some form of public initiative.

61. Indeed, Ofcom recently noted that the PSB Freesat solution could<sup>15</sup>, *“help drive conversion of second and third TV sets in existing Sky DTH homes, providing access to free to air digital satellite channels without the need for an incremental Sky subscription”*.

62. The advantages of a fully Digital Britain have been widely reported, although the precise scale of the benefits is subject to debate. The Government has estimated that the benefits may be in the region of £1-2 billion, although industry observers have argued that the actual figure could be much lower.

#### *What is the potential impact on channels & distribution?*

63. There is unlikely to be a significant impact on the overall spread of advertising/sponsorship revenues between channels given that the majority of channels on PSB Freesat also play-out on the other main digital TV retail offerings (non-subscription and subscription). Those channels that may not appear initially as they are not currently 'in the clear' (such as Channel 4 and Five) are not expected to

---

<sup>15</sup> The Communications Market: Digital Progress Report, Digital TV Q4 2005, page 24.

face any significant loss as they will still be available on analogue until Digital Switchover.

64. In theory, PSB Freesat will provide channel owners with a greater incentive to choose the satellite distribution platform as opposed to, say, cable. However, the choice of one platform over another is only usually applicable to the smaller and/or start-up channels since most of the larger and/or more established channels seek distribution on all platforms. It therefore seems unlikely that PSB Freesat will have an appreciable effect on competition between different platforms.

*What is the potential impact on input suppliers?*

65. PSB Freesat will require the services of a wide range of input suppliers such as hardware manufacturers (e.g. STBs) and logistics providers (e.g. call centres). These companies will all benefit from the roll-out of PSB Freesat. However, the fairly low predicted uptake for PSB Freesat will limit the commercial opportunities and as such the benefits may accrue to just a few providers in each sector.

## **Section 8**                      **Conclusions**

- The roll-out of PSB Freesat may encourage some consumers to switch from their existing digital providers (or in the case of analogue households, choose PSB Freesat over an alternative digital offering).
- Given the similarity of offerings, the proposal is most likely to impose a competitive constraint on Freesat from Sky.
- The proposal may also have some effect on subscription services. It is possible that the effect may be concentrated at the level of 'basic' subscription services, which in the consumers' view may be comparable to the PSB Freesat proposition. However, the overall effect on subscription providers may be mitigated on the basis that the purchase by an end-user of a satellite system would allow an easier upgrade to subscription satellite services.
- Even in the event PSB Freesat were able to achieve the highest possible expected level of take-up, such take-up is likely to represent less than 9% of the total number of households by 2012 and more realistically 4% of households<sup>16</sup>. Therefore, whilst PSB Freesat may exercise a competitive restraint on competing services, it is highly unlikely to deter significant levels of investment or result in market exit. On the contrary, it is conceivable that PSB Freesat may lead to positive effects for other operators, in the event such operators were to seek to provide pay packages as an add-on to PSB Freesat.
- For consumers, competition may also be further strengthened by the introduction of PSB Freesat, as it provides an alternative supplier of digital TV retail offering to almost all households in the UK. A proportion of these households can currently

---

<sup>16</sup> It is open to debate whether or not PSB Freesat's other customers (e.g. existing analogue households, pay refuseniks) would have eventually chosen an existing offering without some form of government intervention.

opt for one provider only. The impact of competition will be particularly strong in those areas outside of the current Freeview footprint.

- The principal effect of approval is therefore likely to be in areas in which Freeview is currently unavailable or less available, which includes the Borders area due to switchover in 2008. It should be noted that Digital UK marketing is encouraging consumers to switch now.
- PSB Freesat might lead to a change in pricing strategy by existing suppliers. For example, Sky might respond to its launch by lowering the price of its free satellite package. The Culture, Media and Sport Select Committee recently noted that<sup>17</sup>, “The BBC/ITV Freesat platform would also provide competition and potentially, lower prices...”

**BBC Governance Unit  
November 2006**

---

<sup>17</sup> “Analogue Switch-off: A signal change in television”, 29 March 2006