The economics of aggregation

Cas O'Connor, Media Analyst with Bain Securities, examines the economic pitfalls of the Government's policy on aggregation

The woes of the metropolitan television industry have been well publicised. A bigger bloodbath is now beginning to trickle. One which, unlike that currently lapping around the metropolitan operators' ankles, has neither significant controversy nor foreseeable drainage. The controversy will come, but the bath will continue to fill. This is regional television under aggregation.

Aggregation is the chosen route of the Federal government's Equalisation Policy which strove to introduce additional commercial television services to regional areas in order to bring the total number of services up to the three enjoyed in metropolitan areas. The current policy has forged four "approved markets" down the eastern seaboard, each of around 1 million viewers. Within each approved market, the number of operators will provide three services (amalgamating if necessary) each taking a "feeder" from the metropolitan networks

However, the current aggregation policy is far more onerous than its alternative, multichannel service (MCS). Most of the regional operators have formed a lobby group which is urging the Government to overthrow its aggregation policy in favour of MCS in which the incumbent operator in each area would be licensed to broadcast a second channel for 10 years. The second channel would eventually be sold to a new competitor. As a political sweetener, the licensees propose to fund the introduction of SBS programming into their area. They say SBS would be introduced by December 1990, and that they would give SBS 10 years to repay the funds.

Government television policy has traditionally been based on five major broadcasting objectives:

- maximise diversity of choice;
- maintain viability of the broadcasting system;
- encourage Australian production and employment;
- foster localism; and
- discourage concentration of media ownership and control of stations.

Each objective would seem to be better served by an MCS/supplementary licence scheme than by aggregation.

Maximise diversity of choice

Regional operators currently broadcast about 70 per centof metropolitan network first release programming. Hence, only two operators are needed in each area to increase this to 100%. Three operators would simply give viewers a greater choice of repeats.

Further, with each service largely carrying network transmission, regional viewers could actually see their favourite programs appear at the same time on conflicting channels courtesy of network counter-programming strategy. This would leave the viewer with less watchable population programming than under the current scheme.

Competition in regional areas is not best serviced by three "affiliate" service providers. Two operators who could cherry-pick from the three networks would provide better programs and stronger financial viability.

Maintain viability

Regional operators have traditionally enjoyed high levels of profitability because of their solus positions and the ability to play-off the three networks against each other in program negotiations. With aggregation the regionals will lose their negotiating positions forcing program expenditure, currently at around 40 per cent of the total expenditure, up towards the 60 per cent paid by the metropolitan operators. Revenues are unlikely to compensate: regional stations have a high reliance on local advertising (27 per cent total revenue as against 8 per cent for metropolitan stations) which will not expand simply because of a tripling of services.

Projecting these two factors forward, one can foresee substantial losses faced by the sector. At least one operator in each market will incur sustained losses. Most probably, it will be the station which is affiliated with the third rating network, which is why Ten's affiliates are among the loudest protestors. Further, each operator must raise between $12 - 20m for the privilege of being less profitable in order to purchase the necessary transmission equipment.

It is the viability issue which should be most closely scrutinised, particularly in light of the current position of the metropolitan networks and the flow-on effects that has had the ability of the regionals to raise either equity or debt financing.

Under MCS, the capital costs would not be as great (as each operator would only transmit into its own area), program negotiations would continue and full viability would be a possibility.

Content

Australian productions will be produced for as long as the stations can afford it. Such programs consistently rate better than foreign programs and thus draw more revenue. They are, however, expensive so the focus is affordability. The ABT's local content guidelines are a safety net under the wrong tightrope: the viability of any industry must be insured before conditions can be imposed on its operation. Aggregation's serious financial drain throws this prerequisite of viability into doubt.

Localism of content too, unfortunately, is an ABT requirement that licensee's must meet. The southern NSW experience is that one station's local news has been cut from the full 30 minute bulletin to a 5 minute adjunct to the network news. Community programs have been similarly cut. Again, MCS by its stronger financial advantage had lessened cut throat competition would help maintain localism.

Aggregation concentration of ownership

Back in 1985, the looming spectre of aggregation saw the regional operators form affiliations in order to forge stronger relationships with their inevitable metropolitan network partners. A flurry of merger and acquisition activity followed. Of the original 13 individual regional operators along the Eastern seaboard of Australia eight now remain. Under MCS the sunset clauses would have forced the second/supplementary service to be eventually transferred to a new operator, virtually ensuring the dilution of media ownership in the longer term.

Further, there is a damaging spillover to other media. To illustrate, we have the benefit of experience in one area. In southern NSW, some 30 second ad spots on breakfast television are currently selling at $20. This does not merely shatter the financial viability of regional television, it also damages the other local media operators, particularly in radio where spots are more than the $20 being asked by the television stations.

Add this to a separate government policy which will see the introduction of further radio licences to regional areas and we could see the radio industry as the next casualty in the growing media bloodbath.