Scottish Parliament Culture & Education Committee inquiry into BBC Charter Renewal

pact.

November 2015

Introduction

1) Pact is the trade association which represents the commercial interests of the independent television, film, digital and children's & animation production sector in the UK.

2) The UK independent television sector is one of the biggest in the world. Independent television sector revenues have grown from £1.3 billion in 2005 to around 2.9 billion in 2014.[1]

3) UK TV exports are also a success story with international revenues from the sale of UK TV programmes and associated activities, up to £1,207m in 2014/15.

4) The original production market in Scotland is worth around £190m and since 2009 has grown by 9% per year. The majority of this investment goes to BBC in-house or the larger Indies based in Scotland.

5) The independent production sector in Scotland is more diverse than other nations. The average business annual turnover is around £3.2 million, with around 1,700 people (both permanent and freelance)[2] employed in the broadcasting sector (including in independent production).

6) Pact's vision for an independent sector in Scotland is one that is vibrant and sustainable; leading both Scottish cultural content but also content that is attractive to the UK and a global audience too. TV is a regular provider of work in Scotland and the sector is wider than just the broadcasters.

7) Pact attaches its recent report '*A new model: building a sustainable independent production sector in Scotland*' by way of supplementing its submission to this inquiry.

8) It is crucial that the BBC maintains the nations and regions quotas in the future and Pact welcomes positive steps taken by the BBC in realising the target set of 17% nations spend by 2016, including 9% in Scotland.

9) For further information, please contact Pact's Head of Nations and Regions, Rosina Robson, at rosina@pact.co.uk or on 020 7380 8248.

[1] Pact Census Independent Production Sector Financial Census and Survey 2014, by Oliver & Ohlbaum Associates Limited
[2] Market Assessment of the Broadcast and Television Production Sector in Scotland 2011/12, EKOS report for Scottish Enterprise (Feb 2013)

Inquiry scope and questions

Pact in Scotland is made up of around 40 member companies (from a membership of around over 400 producers across the UK) including both companies solely based in Scotland and those with a London or UK base too. TV and film production is a key part of the creative industries in Scotland and feeds into the success and skills development of other parts of the creative industries too.

1. Scale and scope of the BBC

- **How should the charter reflect the BBC's priorities and output in Scotland?**

1.1 It is crucial that the BBC maintains the established nations and regions quotas in Scotland; 9% out of the 17% nations and regions spend by 2016. Pact feels that this intervention in the market is still relatively new and needs more time to embed in order to develop sustainable sectors in the nations, including in Scotland.

1.2 Pact's view is that the BBC and the independent production sector in Scotland should be producing content that appeals to a Scottish, UK and global audience.

1.3 The BBC should be a positive catalyst for the creative industries in Scotland including independent production, and through investing in the local production sector this will bring a range of quality and diverse content to audiences in Scotland, the UK and internationally.

1.4 The BBC could achieve this in the following ways:
- *More effective local commissioning*: Greater support from local commissioners to help Scottish producers to monetise, with commissions that drive scale, volume and secondary revenues; more active support of co-commissioning and the championing of local producers (an approach used by S4C in Wales). To date we have seen local BBC commissioning in Scotland too narrowly focused on content which is only attractive to the audience in Scotland.
- *Network commissioning*: UK commissioners being more active to engage with Indies in Scotland and vice versa and building strategic relationships over the longer term.

1.5 There is a debate around the option of devolving network spend decisions to BBC Scotland but Pact believes that the reality is that there is expertise on both sides and that local and network commissioners need to share experience and work together. Both local and network commissioners have an appreciation for what works and what audiences actually want respectively in both Scotland and the UK.

1.6 The key issue for independent producers is for them to secure returning series. Only when they are able to do this can they build sustainable businesses into the future and have the ability to invest development funding into their business, develop new ideas and their business for the longer term.

- **Should in-house production quotas and Terms of Trade allow greater competition and what impact could this have on the Scottish broadcasting industry?**

Production quotas and BBC Studios

1.7 Pact has serious concerns around the proposals for BBC Studios and believes that this could have a detrimental impact on the independent production sector in Scotland.

1.8 Pact is responding to the BBC Trust consultation about the BBC Studios and has expressed its serious concerns in particular about competition and State Aid issues which we do not consider are adequately addressed in the BBC's proposal.

1.9 Whilst we welcome competition in the market which we believe drives diversity and quality of content for the audience, we are extremely concerned about the lack of details around how the regulation of the new commercial entity will work in practice.

1.10 The level of scrutiny and regulation which would be required in order to enable the establishment of BBC Studios would go far beyond the existing framework which is required in order to govern the Window of Creative Competition (WoCC) where BBC and independent production companies compete for commissions. BBC Studios would have a significant impact on the supply chain for the whole of the broadcasting sector, both in the UK and internationally. The mechanisms for ensuring transparency and fairness must therefore go far beyond the existing compliance framework.

1.11 It is crucial that BBC Studios is treated in exactly the same way as all of its commercial competitors by the BBC public entity. Any difference in terms of preferential commissioning terms or information would constitute a breach of State Aid and could have serious effects on the market. There must be full transparency and regulatory oversight on this issue.

1.12 The particular issue for Scotland is that BBC Studios would essentially be a publically funded 'Super-Indie' and represent a £400m intervention in the market (if you consider the value of existing strands of programming to be transferred from BBC in-house). This new company would be in direct competition with companies in Scotland for the network quota.

1.13 Some producers in Scotland may struggle to compete for network programming against BBC Studios which essentially means that independent production companies will be reduced to being 'second class tier' businesses that are only in a position to compete for local commissions. This would confine the Scottish sector to a state of permanent stagnation.

1.14 Pact's response as set out in its submission to the BBC Trust is to maintain the 25% in house guarantee and 25% Indie quota but enlarging the WoCC to 50%. We believe this would increase rather than crush competition in the sector and have a positive impact.

Review of Terms of Trade

1.15 Pact is also seriously concerned about the recent review ordered into Terms of Trade by the Secretary of State for Culture Media and Sport and the devastating impact that this could have on the sector in the UK and Scotland if Terms of Trade are withdrawn.

1.16 The Communications Act 2003 introducing Terms of Trade is an effective and flexible piece of legislation which has allowed producers to own and exploit their rights at home and overseas. Whilst we welcome the review, Pact is concerned about the potential to unravel this industry success story which has developed over the last ten years having a positive impact on the Scottish economy also.

1.17 Removing Terms of Trade could potentially wipe out the independent production sector in Scotland, the majority of which are small and medium sized companies.

- **Is the BBC's online presence damaging local and regional news outlets in Scotland? What could be done to ensure the BBC works more co-operatively with the local and regional news sector?**

1.18 Pact has no comment on news issues which do not affect its membership.

2. Serving the interests of the Scottish audience

- **How well is the BBC serving the Scottish audience (English and Gaelic speaking) and representing Scottish issues to the wider UK audience?**

2.1 As Pact has expressed, there are significant future opportunities for producers in Scotland and the rest of the UK to maximise international export opportunities. The UK TV Exports report[3] shows significant growth potential such as Mexico, Brazil and South Africa where exports grew by more than 30% in each territory. Well established markets such as the US, Canada, Europe and Australia continue to perform well.

2.2 With a static UK market, there are significant opportunities for production companies to sell internationally in the future and drive exports, international growth and jobs. As we have explained, producers can only be supported in developing content that appeals to Scottish, UK and global audiences through more effective local and network commissioning.

- **Could Scotland receive a fairer share of BBC spending?**

2.3 Pact's view is that Scotland already receives a good share of BBC spend; £190m is spent by the BBC in Scotland on an annual basis in addition to the value of the excellent facilities and studios at Pacific Quay. However we would note that the majority of the investment is targeted at BBC in house or the larger Indies with a base in Scotland.

2.4 We maintain that the focus should be on <u>how</u> the investment is spent rather than the quantity and whether this is helping to drive a long term and sustainable production centre in Scotland in the future. We note comments made recently by Fional Hyslop, the Cabinet Secretary for Culture and External Affairs highlighting that investment in an additional platform for Scotland was not necessarily the right option. The important point is to ensure that more investment goes into <u>content</u> for Scotland and not necessarily new infrastructure.

2.5 In light of wider cuts announced by the BBC that are still to take effect, Pact would be wary of increasing budgets in some areas which would inevitably reduce content budgets in other nations or regions or content budgets across the BBC.

- **How well does the BBC support distinctive Scottish content and could it do more in this regard?**

[3] UK TV Exports 2014/15 by Pact, BBC Worldwide, ITV Studios

2.6 As expressed, Pact believes that the future lies in developing content that works for a Scotland, UK and global audience. This will drive a range of quality and diverse content in the future and a healthy export market.

- **How could the BBC enhance support and development of talent and skills in Scotland?**

2.7 We refer you to the recommendations in the enclosed report. We think there is scope for both the BBC, Channel 4 and other broadcasters in Scotland to develop skills, training and mentoring initiatives that help develop both the middle tier talent and next generation of leaders in Scotland e.g. Executive Producer level and also new entrants to the market to keep the supply of new talent fresh and diverse in Scotland.

3. Governance arrangements

- **How could BBC governance be improved to enhance the Scottish voice?**

3.1 Pact is not in favour of the proposals put forward by the Scottish Government and the other Devolved Assemblies to create a more federal system of governance within the BBC. As a publicly funded UK institution, we believe that it is appropriate that the UK Government and Parliament are responsible for setting the licence fee and the BBC Charter. Beyond this, the BBC should remain independent from all Parliamentary interference.

3.2 However, Pact continues to welcome oversight by the Scottish Parliament and the other Devolved Assemblies to the BBC Annual Report and for them to play a constructive role in continuing to query how the broadcaster quotas are being spent in Scotland. The option for an Ofcom board member to represent the interests of the nations and regions is also a positive move.

3.3 The UK Government has an important role to play during BBC Charter Renewal negotiations to make sure that the nations and regions, including Scotland, are well represented in consultation with the Scottish Parliament and other assemblies. Pact supports a continuation of the nations and regions quotas that are important to both reflect the diversity of voices around the UK and support production companies in Scotland. Pact wants to see a strong PSB (Public Service Broadcasting) system in Scotland which includes the BBC.

4. Cost savings

- **What would be the impact of any further cuts to BBC spending in Scotland?**

4.1 Pact is aware of further cuts announced by BBC that will take effect over the coming months. We hope as far as possible that they will not affect content budgets and be achieved through further efficiency savings and a reduction in back office costs. Pact maintains that the established nations and regions quotas should continue into the future.

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A new model: building a sustainable independent production sector in Scotland

ekos
Economic and Social Development

Prospero

November 2015

Foreword and Recommendations


John McVay, Chief Executive, Pact


Jane Muirhead, Director of Scotland, Pact

With the debate around BBC Charter Renewal in full flow and the Scottish Government taking recent steps to offer support to the independent production sector, now is an important moment for Pact to set out its model for a sustainable industry for the future.

The original production market in Scotland has grown over the last few years but is currently in danger of stagnating. We now have an opportunity to build a sustainable production base and Pact has commissioned the consultancies EKOS and Prospero to develop models of both an 'optimal' Indie and outline the ideal model for the sector in the future.

The report analysis is based on interviews with a representative cross section of producers in Scotland and across the UK that can demonstrate successful growth strategies. In addition there has been a range of conversations held with key stakeholders.

The analysis, conclusions and recommendations are targeted at broadcasters and commissioners, Scottish Government, public agencies and producers themselves and we look forward to working together to realise these aims over the coming months.

Pact's Recommendations:

- **Broadcasters and commissioners:**
  - More targeted local commissioning: greater support from local commissioners with commissions that drive scale, volume and secondary revenues; more active support of co-commissioning and the championing of local producers. This will help companies build their business to develop capacity for network production too.
  - More strategic and commercial network commissioning: focussed commissioning of smaller local producers in key genres that deliver volume, continuity for business planning and support the development of centres of excellence.
  - Greater embedding of UK commissioners: more visibility and presence of UK commissioners across Scotland. Commissioners should be open to developing both new and existing relationships with Indies.
  - Investing in talent: develop existing programmes to support both the next generation leaders and new talent through setting up shadowing schemes for key executives and mentoring and training.

- **Ofcom:**
  - More rigorous application of quotas: Pact is keen to work with Ofcom to encourage more transparency in reporting by both broadcasters and producers as to how they have met the Out of London production definition in Scotland. Pact can support Ofcom in playing a stronger role in monitoring and auditing how the definition is interpreted and we welcome oversight by the Scottish Parliament too. Pact will work with Ofcom to clarify and reissue the Out of London production guidance to producers.

- **Scottish Government and public agencies:**
  - Dedicated agency for TV and film sector: the Scottish Government should designate a single agency, either Creative Scotland or Scottish Enterprise to be a champion for the TV and film sector with a sufficient budget attached to help incentivise production at home, growing digital capabilities and supporting international sales.
  - Creative Scotland: should develop a strategy for growing and supporting the independent production sector in Scotland, arguably the most commercially successful sector in the creative industries.
  - Scottish Enterprise/Scottish Development International (SDI) should reshape their current strategy of only targeting support to 'high growth' firms to ensure that the TV and film sector is covered by support to international markets too.

- **Producers:**
  - Create partnerships: To consider creating partnerships with other independent production companies in complementing skills or genres to create scale.
  - Develop relationships: Take time to develop commissioner relationships in London.
  - Develop an export plan: take advantage of international export opportunities and build sales beyond the UK and the US in emerging markets where future growth lies.

About Pact

Pact is the trade association representing the commercial interests of production companies in film, television, digital, children's and animation media.

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Executive summary

- Total investment in original production in Scotland (both in house and independent) has grown by over 9% per annum over the last six years and Scotland now has a base of scale producers able to compete nationally and internationally across multiple genres.
- However, there remains a long-tail of small Scottish producers who are highly dependent on BBC local commissions and who have limited ability to invest in the business development necessary to grow.
- Analysis of successful producers from across the UK identified a number of factors that are key if small producers are to grow effectively.
- A sustainable model requires multiple genres, a diverse client base (including the US) to reduce dependency on public service broadcasters, high margin secondary revenues (to fund overheads) plus depth and breadth of commissioner relationships.
- Investment in development is essential (at least 5% of revenues plus significant senior time) and is difficult to achieve without multiple executives and revenues of at least £5 million.
- At a market level, Scotland needs to build a centre of excellence in one or two programme genres, expand capacity in scripted (particularly drama) and create an energetic and creative environment in which young talent want to stay and build their careers.
- Achieving such a model will require focussed support from commissioners to build local capacity; more effective intervention from Scottish Government agencies, investment in training to develop new Executive Producers and partnerships between large and small Scottish producers.
- At the same time ensuring the ongoing health of the BBC and Channel 4, who are so key to the ecology of Scottish production, remains essential.
- An optimal Scottish sector would see the development of a new wave of scale Scottish production companies who would in turn invest in and employ the next generation of talent to build sustainability.

1. INTRODUCTION

While production in Scotland has grown significantly over the last five years, the industry continues to face challenges both structural and operational.

Pact commissioned Prospero and Ekos to undertake a review of the market. The focus of the work was to:

- Interview a representative cross section of Scottish production companies and other local stakeholders to identify views on the strengths, weaknesses and challenges facing Scottish independent production both at a company and at a market level.
- Interview a selection of successful small and medium-sized production companies from across the UK to identify optimal model(s) and growth strategies for independent producers.
- Combine the results of these interviews to illustrate what an "optimal" Scottish indie could look like; the ideal shape for the sector and the key components that need to be addressed to facilitate such developments.

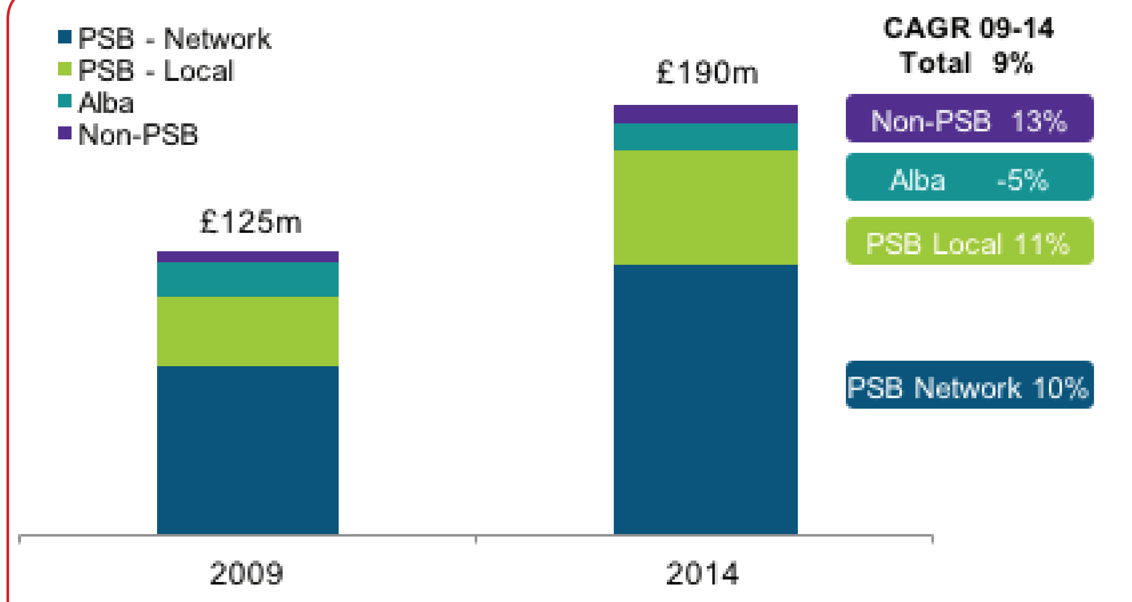
Prospero and Ekos interviewed 20 production companies and stakeholders in Scotland and 20 production companies and stakeholders in the rest of the United Kingdom. The work was conducted over eight weeks in August and September and was supported by analysis of data already in the public domain from Ofcom and COBA (the Commercial Broadcasters' Association).

The report seeks to reflect as accurately as possible the views expressed during the interviews which may not directly reflect the views of Pact.

2. CONTEXT

The Scottish original production market is worth approximately £190 million, and, since 2009, has grown by 9% per annum. This compares with broadly static spend in the rest of the UK.

FIGURE 1:
GROWTH IN FIRST RUN ORIGINAL PRODUCTION SPEND IN SCOTLAND (£M)



Notes: PSBs = Public Service Broadcasters (BBC, Channel 4, ITV (STV), Channel 5)
Excludes news;
Local Spend covers local opt outs for BBC and ITV (STV), Network Spend covers network spend for all PSB channels
Source: Ofcom Commercial Market Surveys, COBA 2014 Census, Prospero analysis

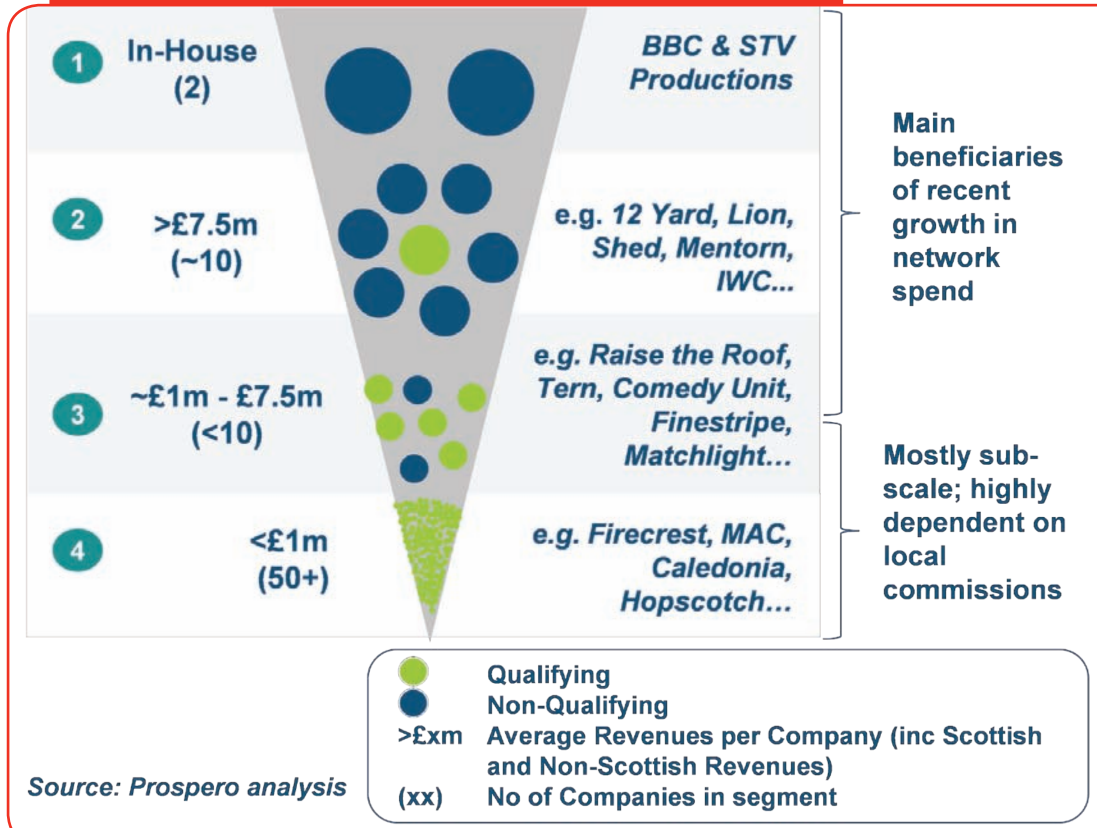
Scottish growth was triggered by acknowledgement in 2008 that PSB network spend in the Nations was too low. As a result, the BBC and, more recently, Channel 4 committed to increase investment in the Nations.

- In 2008 the BBC committed to increase spend across all Nations to 12% by 2012 and 17% by 2016; specifically, by 2016 8.6% of BBC network spend must be in Scotland.
- In 2013, as part of its licence renewal, Channel 4 agreed to increase its production in all Nations from 3% to 9% by 2020 (the proportion going to Scotland is not specified).

The Scottish Production market splits broadly into four segments:

- **1. In-House:**
  The in-house production arms of the BBC and STV.
- **2. Large Independents:**
  These have been the primary beneficiaries of recent growth in network spend. Most are subsidiaries set up by larger groups; some of which are well-entrenched and core to the Scottish production sector; others are less well established, and a small number come up to Scotland just to produce a particular programme or series.
- **3. Medium Independents:**
  Typically, production companies headquartered in Scotland, some of whom are now part of larger groups (such as the Comedy Unit) but most of whom are still standalone independent producers.
- **4. Small Independents:**
  Approximately 50 local Scottish producers; these are typically sub-scale and highly dependent on local commissioning from BBC Scotland and MG Alba.

FIGURE 2: SHAPE OF THE SCOTTISH PRODUCTION MARKET



Source: Prospero analysis

Prospero and Ekos estimate that the top two segments (in-house and larger independent producers) account for approximately two thirds of the value of Scottish commissions.

3. DYNAMICS IN SCOTLAND

Our interviews in Scotland covered a mix of Scottish subsidiaries of larger groups, medium-sized and small local producers, in-house producers and other stakeholders including commissioners and public bodies, such as Creative Scotland and Scottish Enterprise.

A. Market Challenges

In most areas, there was consensus about market dynamics and challenges; but in some, notably Lift & Shift (where established high volume shows are moved into Scotland for production) there were conflicting views.

- **Local Market too discrete:**

The BBC and ITV group spend £63 million on local channels and opt-outs; 27% of original production spend in Scotland. This has grown at 7% per annum since 2009. This market is the main stay of the majority of smaller Scottish producers but is seen as very discrete; arguably focussed too much on local cultural needs to the detriment of producers' commercial model. As a result, there is limited transfer of programmes from local to network and local commissions do not deliver credibility with network commissioners. In addition, it was felt that, though improving, the PSB commissioners could do more to support capacity building in the sector.

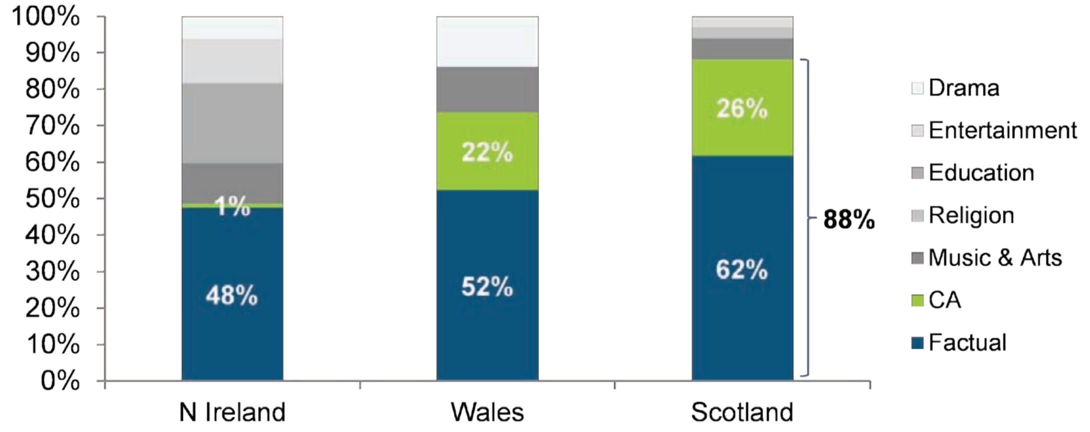
- **Local Players are sub-scale:**

While the market has grown, it is still seen to lack sufficient players of scale. Scale is key to sector health as it builds talent and provides the continuous employment necessary to foster a vibrant and strong freelance community. There are too many sub-scale players (typically with revenues of less than £1 million). Many of these are corralled in local programming; unable to invest sufficiently in development and build the credibility to secure volume commissions. Some of these smaller players are perceived to be not sufficiently commercial and could diversify further. It is interesting to note that despite these challenges, there have been very few mergers and acquisitions amongst producers in Scotland.

- **Insufficiently Diverse:**

The market was felt to be inadequately diverse in terms of genres. While there is a growing presence in network commissions of daytime and comedy, there is little volume of scripted and no notable drama presence. In particular, the base of activity for smaller players is too narrow; strongly skewed to specialist factual and current affairs where spend is declining and which do not deliver volume production. This perception is confirmed by BBC Trust data on BBC local commissioning, 88% of which is in factual and Current Affairs; less diverse than in Wales or Northern Ireland.

FIGURE 3: SHARE OF BBC LOCAL INDEPENDENT COMMISSION HOURS BY GENRE



Source: BBC Trust: The Supply Arrangements for the Production of the BBC's Television Content, Radio Content and Online Content and Services, June 2015, Prospero Analysis

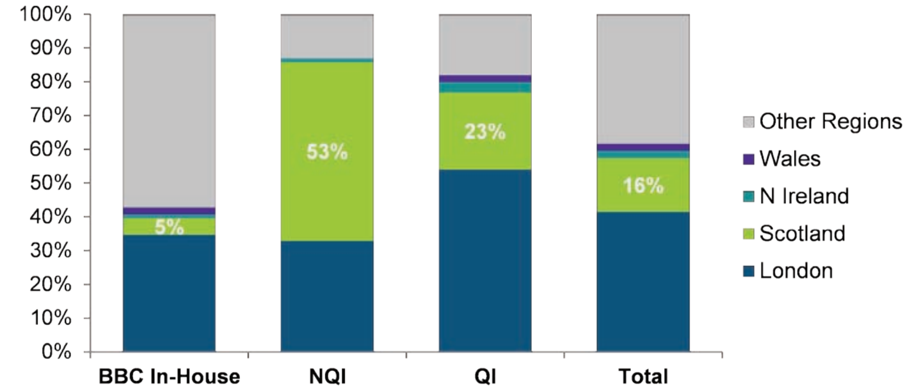
Note: Excludes Sports Commissions

Local Commissions are programmes commissioned for local opt-outs rather than for broadcast across the network

- **Lift & Shift:**

Views on the definition and impact of Lift & Shift were diverse. There was consensus that the subsidiaries of bigger production groups have disproportionately benefitted; Scotland now accounts for 53% of all hours commissioned by the BBC from NQIs. Some interviewees saw the overall effect as highly negative, with Lift & Shift giving shares of the Scottish production quota to London-based companies not committed long term to Scotland. Others felt that while smaller producers had been squeezed, the sector as a whole has benefitted from increased volume and new genres leading to more opportunities to build and retain the skill base crucial to the industry. Many (though not all) of the larger group subsidiaries were seen to be committed to Scotland, but there remained concerns about "pop up" companies who come to Scotland just to produce a particular programme or series and take a slice of the Scottish production quota.

FIGURE 4:
REGIONAL SHARES OF BBC NETWORK COMMISSION HOURS BY PRODUCER TYPE



Source: BBC Trust: The Supply Arrangements for the Production of the BBC's Television Content, Radio Content and Online Content and Services, June 2015, Prospero Analysis

Notes: Other Regions includes a small amount of multi-region hours
QI = Qualifying Independent; BBC must commission at least 25% of qualifying hours from QIs;
NQI = Non-Qualifying Independent owned by a group controlling a UK broadcast channel
Network commissions are programmes commissioned for broadcast nationwide
Qualifying hours excludes new, continuity and repeats
NQIs can only compete for 25% of qualifying network hours and accounted for 9% of total qualifying hours in 2013/14

- **Insufficient Senior Talent:**

There was consistent feedback (from large and small players and commissioners) about the shortage of senior talent (notably Executive and Series Producers). This was seen to undermine credibility with network commissioners and the willingness of channels to take risks, particularly on long-run shows, in Scotland. In addition, lack of depth in key genres was seen as limiting development of the next generation of Scottish talent.

- **Lack of a Centre of Excellence:**

Scottish production was seen to have grown and diversified. However, when compared to Bristol (home to the BBC's Natural History Unit) and Cardiff (which houses the BBC's long running dramas) Scotland was not seen to have one important genre where it has a national centre of excellence to act as a focus for commissioners and a magnet for talent.

- **Ineffective Public Support:**

Public support for the independent production sector in Scotland was not viewed to have been successful, with lack of a clear strategy and goal and with the existing interventions being seen as unfit for purpose. Intervention was seen to having failed to support a vibrant start-up base, to facilitate consolidation with the sector or stimulate international engagement. This approach was contrasted with the perceived success of Northern Ireland Screen in driving production in Northern Ireland and stimulating inward investment.

FIGURE 5: CHALLENGES FACING THE SCOTTISH PRODUCTION MARKET

"Market is sub-scale, low margin and under-capitalised"
"Too many indies are competing in the small declining factual space"
"The big groups take IP and profit out of the Scottish market"

"Not enough of the quota is going to smaller local players"
"Lift & Shift has built market capacity but been a disaster for local indies"

"Credibility in local means little to network commissioners"
"Local commissioning is not designed to build sector capacity"

"The pool of people with insight and commissioner credibility is too small"
"There is a strong crew base but senior resourcing is very tricky"

"Public investment needs to focus on investment for growth, not grants"
"There is a lack of strategy, vision and investment to support the sector"

	Issues	
Supply	Not enough players of size	4
	Too many sub-scale players in same genre	4
	Too few genres, too much factual	4
	Smaller players not sufficiently commercial	2
	Group subsidiaries not contributing to local growth	2
	Lift & Shift has undermined smaller indies	2
Network Demand	Lack of a Centre of Excellence	2
	Insufficient commissioners in Scotland	4
	Lift & Shift taking large share of quotas	4
	Over-dependence on pressured PSBs	4
Local Demand	Local discrete from network	4
	Local commissions too skewed to factual	4
	Commissioning not focused on building capacity	4
Talent	Lack of senior talent	4
	Few execs with strong network credibility	4
	Insufficient work to support freelance market	4
	Insufficient development of next generation	4
Public Support	No clear leadership, strategy or resourcing	4
	Lack of effective incentives for drama	4
	Public support not focussed on needs	4
	High cost of accessing subsidies	4

4 High level of Consensus
1 Low level of Consensus

B. Small Producer Challenges

The interviews revealed a broadly consistent set of challenges with the business model of the small producers who make up the majority of Scottish production companies.

- **Narrow Focus:**
Local Scottish producers are typically narrowly focussed on one, often sub-scale, genre (usually a factual sub-genre) and overly-dependent on a single key executive.

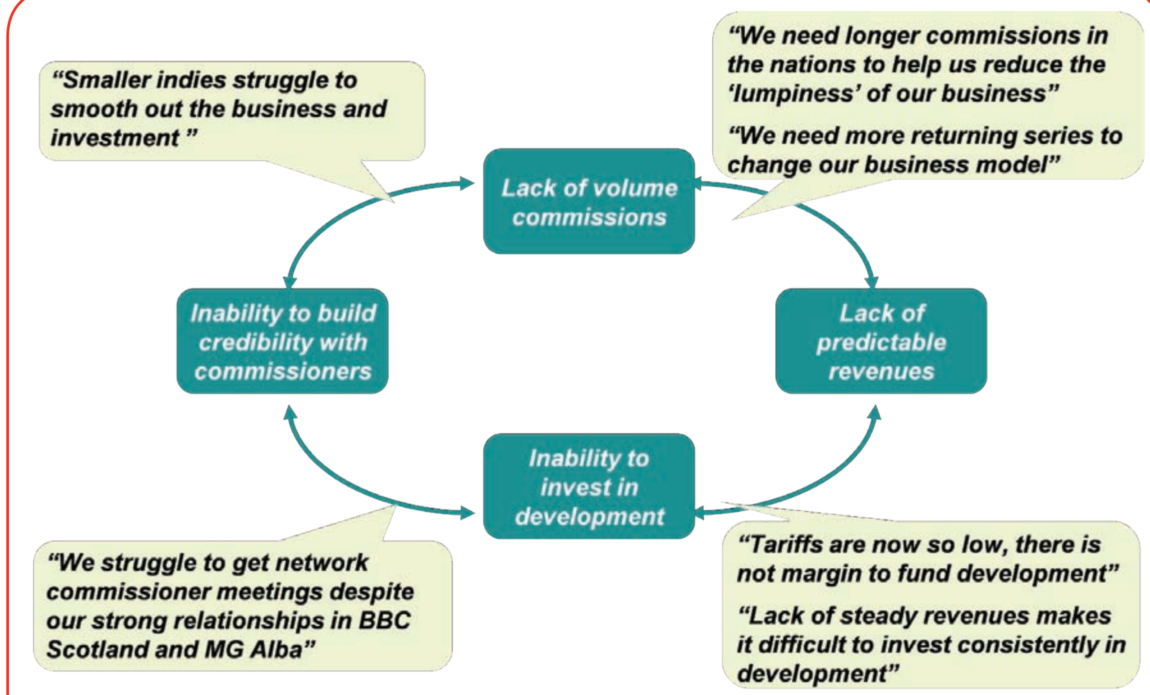
- **Limited Commissioner Relationships:**
Small producers have inadequate depth and breadth of commissioner relationships (particularly within the network).

- **Over-dependence on PSBs:**
The vast majority of the revenues of smaller Scottish producers come from the BBC (local and network) and Channel 4 who have quotas for Scottish production. As a result, the indigenous sector is highly exposed to any downwards pressure on programme spend at Channel 4 and the BBC in particular.

- **Lack of investment in Business Development:**
These small producers get stuck in a vicious circle: they lack predictable returning revenues which means they cannot invest sufficiently in development which, in turn, means they cannot build network credibility to attract the volume commissions that would help them break out of this cycle.

As a result of these dynamics, revenues for the many Scottish Producers are low (typically below £1 million); margins are low and long-term sustainability unsure. With no long-term visibility, it is difficult to consolidate and build scale with partners.

FIGURE 6: THE VICIOUS BUSINESS CYCLE FOR SMALL PRODUCERS



Source: Prospero and Ekos interviews and analysis

4. OPTIMISING BUSINESS MODELS

Prospero and Ekos interviewed a number of successful medium-sized production companies across the UK (including Scotland) to identify best practice. While dynamics vary by genre, a broad optimal model emerged that needs to be replicated in Scotland if the sector is to drive to the next level of growth and sustainability.

A. Revenues and Margins

Interviews confirmed that it is difficult to have a sustainable business with less than £5 million in revenues. The vast majority of Scottish producers earn less than £1 million.

- **Secondary Revenues:**
Successful production companies look to secure at least 10% of revenues from secondary markets (programme or format sales to third party broadcasters) as these deliver high margins that can fund development. However, these are increasingly difficult to secure outside PSB commissions where agreed Terms of Trade guarantee producer IP ownership. Small Scottish producers typically have low levels of secondary income.

- **Diverse Customers and Global Focus:**

A diverse customer base is key to mitigate risk and deliver complementary business models. Small Scottish producers are almost exclusively dependent on UK PSBs (particularly the BBC) whose ability to invest in original production is increasingly under pressure. Successful production companies ideally look for at least 20% of revenues from non-PSBs (such as Discovery and Sky), at least 10% from the US or abroad and a growing base of digital commissions. While non-PSBs usually demand all rights (limiting access to secondary income), they commission higher volumes and are increasing their original production spend. US players also have higher budgets and want longer runs than PSBs.

- **Target Gross Margins of 20%:**

Optimal gross margins are less easy to extrapolate as they vary by genre, volume, one-offs and returning series, and the extent to which a producer can leverage an amortised base in post-production. Gross margins for the successful production companies interviewed ranged from 35% to 10% and averaged between 20-25%; these are significantly higher than those of most small Scottish producers.

FIGURE 7: OPTIMAL REVENUE & MARGIN DYNAMICS FOR PRODUCERS

Revenues & Margins		Indicator	Comment
	Scale	£5-10m + <£1m	• Most Scottish producers have less than £1m or £1m in revenues • Below £5m it is difficult to fund development • £10m should ensure long term sustainability
	Secondary	>10% <5%	• High margin secondary can fund development • Demand for all-rights deals from non PSBs • Successful producers target 10%+ of revenues from secondary sources
	Split of Clients	Non-UK >10% Non-PSB >20% PSB >40% <10% >90%	• Scottish producers are very dependent on PSBs • PSBs allow rights retention & secondary income • Over-dependence on falling PSB budgets risky • Ideally 10%+ from US; budgets are bigger, runs longer , but there is no secondary income
	Gross Margins	35% 20-25% 10%	• Vary by genre, volume, 1st and 2nd run, and operating model • Target 20% - 25%
	Hours	>20-30 <10	• Varies by genre but below 20 lack the volume to support regional talent base • Ideally, at least one 6 plus episodes series and one returning series

Target Model
Small Scottish Indies

B. Business Development

Our interviews showed that significant investment in business development is essential to build a sustainable, scalable production company. Companies need to get to the size where they can have executives in complementary genres and can manage approximately ten in-depth commissioner relationships across several broadcasters.

- "The producers who are successful are those that really listen to our requirements, have insight into what works on our channels and ensure they are 'front of mind'" Commissioner
- "Of four senior executives only one focusses primarily on delivery; the other three spend 70% of their time focussed on development" Regional Producer
- "We invest significantly in development, building capabilities in our younger team and allowing them to shadow the senior team to become credible" Regional Producer
- "We don't have an office in London but on average at least 50% of our senior time is spent in London, which is both a financial and a time cost but is essential" Regional Producer

Successful production companies typically invest 5% of their revenues directly in business development, and between 40-60% of executive time on building and managing commissioner relationships. This is a model smaller Scottish producers struggle to replicate.

FIGURE 8: BUSINESS DEVELOPMENT

Development		Indicator	Comment
	Genres	Adjacent genres	• Focus on one narrow genre is risky • Moving too far from core capabilities undermines credibility • Extending genres may require multiple execs
	London Office	Not necessary	• London presence "nice to have" but not essential if senior time is committed as below
	Commissioner Relationships	10-15	• Over dependence on one or two relationships is high risk • Too broad a focus means lack of depth • Relationships should be across 3 – 4 broadcasters and adjacent genres
	Development spend	>5% Revenues *(excluding senior time)*	• Includes development staff and direct spend • Some spend may be funded by broadcasters or distributors • Much will need to be funded by profits/ investment
	Time in London	20%+	• Must commit senior time with commissioners in London • A high cost partly offset by lower cost regional operations
	Senior time on Development	50%+	• Need to focus senior time on development not delivery • Requires a strong delivery team
	Multiple Execs	2-3+ Execs	• Need complementary capabilities (creative, sales, finance…) • Need strengths in complementary genres

Achieving Scale

The optimal models identified above can only be achieved with scale. Success is, inevitably, predicated on the talent and reputation of the key individuals behind a production company. However, in addition, our analysis identified a number of different strategies that successful companies have used to enhance growth. The models can typically be grouped into three:

- **1. Focus on and build reputation in key areas:** "Producers who come in to see me need to be able to articulate their unique selling points as much as their ideas." Commissioner
- **2. Optimise the commercial model:** "We have been highly commercial in our approach, bringing on complementary talent to expand our portfolio, being very pragmatic about where and how we focus our business development to drive volume and margin." Regional Producer
- **3. Secure investment to facilitate expansion:** "We merged with another company to deliver us the scale to attract either investment funding or an output deal with a key distributor." Regional Producer

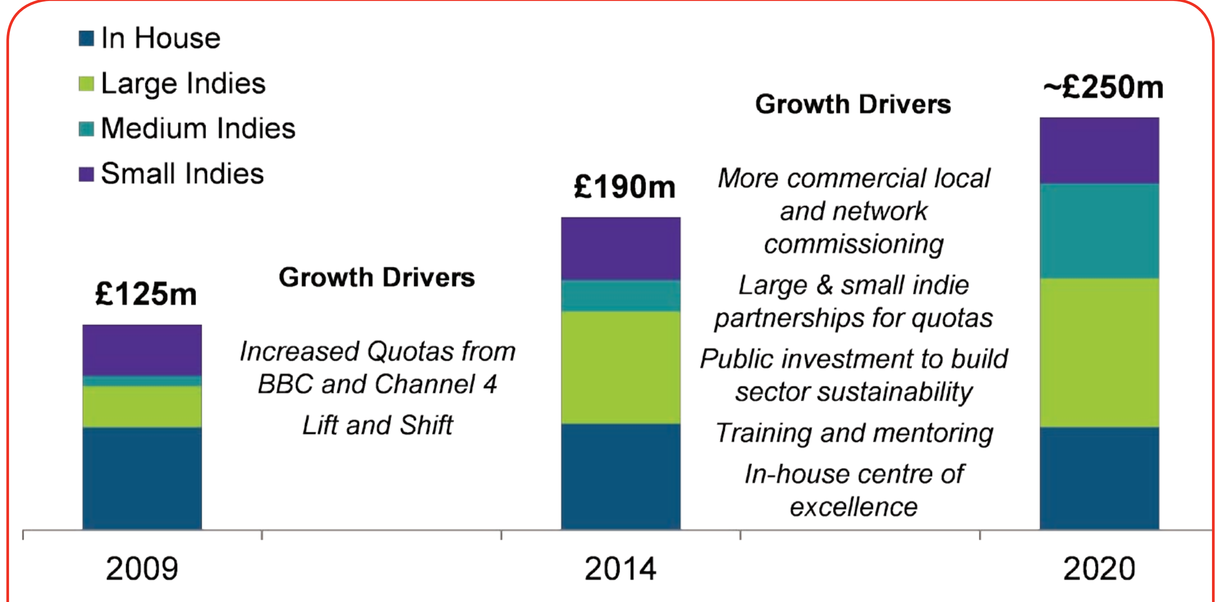
FIGURE 9: STRATEGIES FOR GROWTH

	Options
1. Build Core USPs	Structure to attract on screen talent
	Focus on digital and agency commissions
	Focus on high volume / Returning series
	Focus on writing talent
	Focus on special techniques (e.g. multi cam; UHD; animation)
	Focus on formats
2. Enhance Model	Develop international clients / reach
	Invest in post to drive margins (on long runs)
	Expand into complementary genres with new executives
	Extend to ~10 core commissioner relationships across at least 4 broadcasters
	Invest in time and relationships in London
	Partner with other small indies to share overhead and back office functions
3. Secure Investment	Join with groups in other regions
	Investment from international distributor
	Secure growth fund (C4) / minority stakes (BBCWW, Studios)
	Merge to secure scale

5. THE FUTURE SCOTTISH PRODUCTION MARKET

The last five years have seen significant growth in Scottish production; however, the next five years need to match growth and extend the benefits into the broader Scottish production base.

FIGURE 10: GROWTH TARGETS FOR THE FUTURE OF SCOTTISH PRODUCTION



Source: Ofcom Commercial Market Surveys, COBA 2014 Census, Prospero analysis

The interviews identified a number of market interventions that could help secure a more robust Scottish production sector. These include:

- **More targeted local commissioning:**
Greater support from local commissioners to help Scottish producers monetise, with commissions that drive scale, volume and secondary revenues; more active support of co-commissioning and the championing of local producers (an approach used by S4C).

- **More commercial network commissioning:**
Focussed commissioning of smaller local producers in key genres that deliver volume and continuity for business planning and support the development of centres of excellence.

- **More rigorous application of quotas:**
More rigorous measurement of what constitutes a Scottish production and proper oversight to prevent quotas being accessed by companies not committed to a long-term Scottish presence.

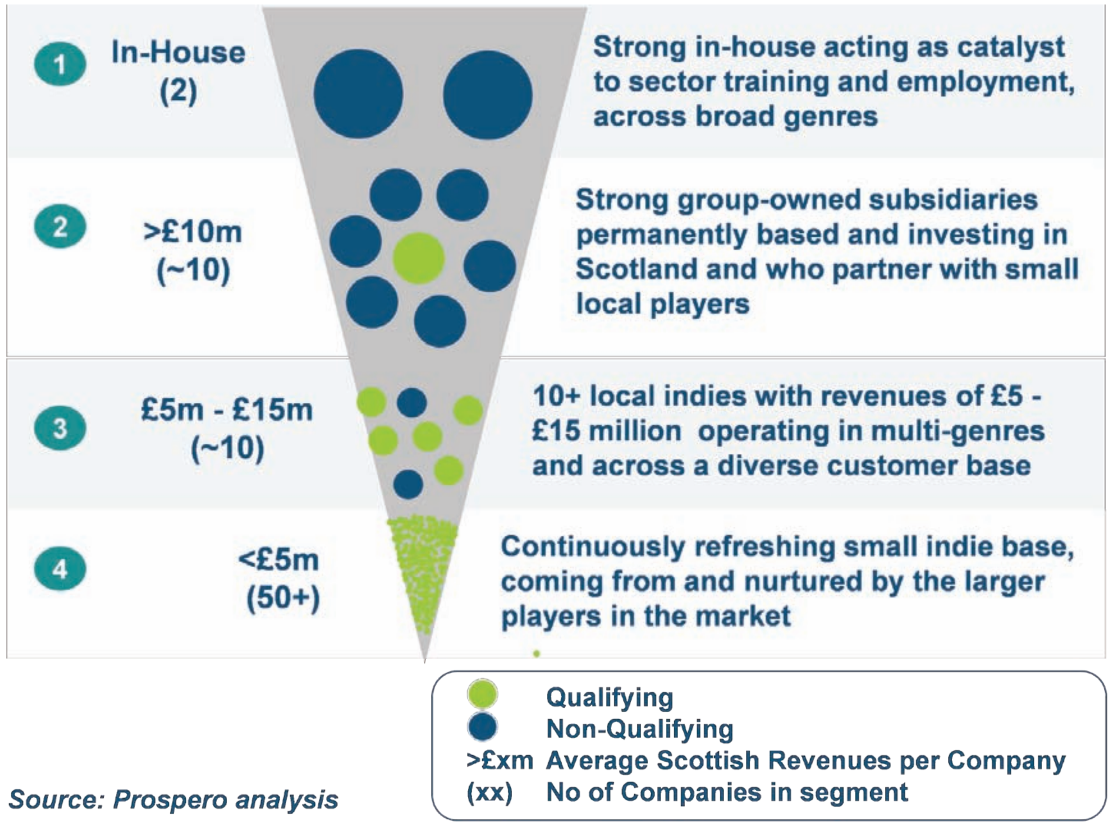
- **Partnerships:**
Partnerships between large and small players and amongst small producers in complementary areas; possibly as a precursor to further Lift & Shift.

- **Training:**
Models to support next generation leaders that include shadowing of key executives, mentoring and formal training programmes.

- **Focussed public intervention:**
Support from Creative Scotland and Scottish Enterprise that is more routed in the reality of production and is focussed on delivering long term inward investment (drawing on lessons from Northern Ireland Screen) and growing digital capabilities in the production sector.

Ultimately, a successful model would see growth of scale Scottish producers who would in turn invest in the next generation of talent to build sustainability.

FIGURE 11: IDEAL MODEL FOR THE FUTURE OF SCOTTISH PRODUCTION



Source: Prospero analysis

APPENDIX: Selected Interview Quotes

Talent

"Finding good Scottish Executive Producers is hard." Large Scottish Producer

"There is a shortage of talent. There are too few outstanding Executive Producers and not enough Series Producers in Scotland. They have not succeeded in growing the next generation." Commissioner

"It took a lot of work to build our skill based in Scotland but we worked with local players and have succeeded in doing that. We now only use local talent." Large Scottish Producer

"The pool of people who have real credibility with network commissioners is too small in Scotland." Scottish Producer

"There are not enough big companies which makes it hard for writers and directors to build a career in Scotland." Large Scottish Producer

"Scotland needs to develop a bigger base of trusted executives and can win and deliver business." Large Scottish Producer

"It took us a long time to find the right, credible directors in Scotland. There is a strong crew base but finding the senior resource is tricky." Scottish Producer

"Finding the right people is difficult. We don't want to bring people up from London, but it is not always easy." Large Scottish Producer

"There is insufficient experienced, credible production talent in Northern Ireland so we have to bring in people from London which destroys our cost model." Regional Producer

"The pool of executives is thin; CVs are less specialist than in London, and commissioners don't like that; failure to develop this pool reflects network commissioning practice." Large Scottish Producer

"There is not enough depth of talent in Scotland and we have difficulty in keeping the next generation in Scotland." Scottish In-House Producer

"There is insufficient on-screen talent living in Scotland." Scottish In-House Producer

"We need an ambitious talent strategy supported by the broadcasters to bring new execs through the system." Scottish Stakeholder

Development

"Of four senior executives one focusses primarily on delivery and the other three spend 70% of their time focussed on development." Regional Producer

"We invest significantly in development; building capabilities in our younger team and allowing them to shadow the senior team to become credible." Regional Producer

"We spend a lot of time in London. Development is the life blood of the company." Regional Producer

"We are too small to justify investment in dedicated development, and consequently are trapped in a sub-optimal model." Scottish Producer

"Our lumpy business model makes it difficult to invest consistently in development or to achieve the scale required for sale or acquisition." Scottish Producer

"Our work is highly regarded but it is all one-offs and we have difficulty funding development." Scottish Producer

Tariffs & Rights

"It is getting harder and harder to retain distribution rights with non-public service broadcasters." Regional Producer

"The rights model is under pressure. Increasingly we need to pre-sell to a distributor just to fund the deficit." Regional Producer

"International players are now insisting on all-rights; Netflix just complicates the market." Regional Producer

"Production tariffs are now so low that there is not margin to fund development." Scottish Producer

Lift & Shift and Quotas

"Lift & Shift was initially very difficult. It required significant reconfiguration of the team and investment in training local talent. However, we now have a good indigenous model." Large Scottish Producer

"We were originally Lift & Shift but are now developing and making shows out of Scotland." Large Scottish Producer Studio

"Lift & Shift was a necessary evil to bring scale, capacity and diversity" Large Scottish Producer

"We believe not enough of the Scottish quota is being delivered by genuinely Scottish indies." Scottish Producer

"Lift & Shift has built employment, but the IP and profits go to London." Scottish Producer

"We would like to see quotas more effectively targeted at the true Scottish sector." Scottish Producer

"There was a lot of negativity about Lift & Shift, but the vast majority was in genres not well represented in Scotland. We believe it helped bring in new skills and experience that has grown the market." Large Scottish Producer

"The quotas have helped and Channel 4 now has new targets in comedy and entertainment which should grow investment further." Large Scottish Producer

"Quotas have encouraged inward investment and helped bring in skills and experience that were previously absent." Large Scottish Producer

"We need to close down the loop holes in the quotas that allow brass plating, but without over-regulating." Large Scottish Producer

"Lift & Shift has been a disaster for Scotland and had not created sustainability. Shed pulling out as soon as it hit a fallow period is an example." Scottish In-House Producer

"Lift & Shift companies need to be required to partner locally." Scottish In-House Producer

"Lift & Shift created jobs but cannibalised the quota income of local indies." Scottish Producer

"The Lift & Shift companies are in genres, such as entertainment, where it is difficult for local producers to compete." Scottish Stakeholder

"The failure of Lift & Shift is reflected in the static nature of local players." Scottish Stakeholder

London

"The cost of maintaining two offices, one in the region and one in London means our overheads are very high." Regional Producer

"We don't have an office in London but on average at least 50% of our senior time is spent in London, which is both a financial and a time cost but is essential." Regional Producer

"We go to London weekly to build, nurture and manage our commissioner relationships and insights." Large Scottish Producer

"Our business model is helped by the fact that one of our partners is London-based." Scottish Producer

"One of our senior executives spend two days a week in London to manage commissioner relationships." Large Scottish Producer

"Our head of development is in London, but we do most of our work from Scotland." Scottish Producer

Group Synergies

"There are some back office cost synergies as part of a small group, in terms of market presence, business, legal and admin support." Regional Producer

"Being part of a studio group gives us financial security and, crucially, clout and credibility in the US. It has also helped with co-productions." Regional Producer

"Being part of a group brings advantages, there can be collaboration across adjacent areas; cost synergies around the back office and access to distribution." Large Regional Producer

"Sharing post production and back office with another indie has allowed us to reduce costs and increase flexibility." Regional Producer

"Being part of a global company has allowed us to access greater distribution revenue and facilitated expansion of formats internationally." Regional Producer

Commissioner Relationships

"We are consciously expanding our commissioner relationships, four is too few." Regional Producer

"The reputation of our founding partner has been absolutely essential; it has meant the commissioners do not think of us as a regional indie at all." Regional Producer

"You mustn't be too scatter gun with commissioners; you need to have focussed in-depth relationships." Regional Producer

"You have to ensure that the business model is not dependent on too small a commissioner base." Regional Producer

"We are focussing on some of the smaller channel commissioners (such as E4, Discovery) to build our network credentials and to secure longer runs." Regional Producer

"New commissioner relationships take time; you have to be in it for the long haul." Regional Producer

"You need to be very commercial; know where commissioners have gaps and focus on meeting those needs." Regional Producer

"With some exceptions the small indies don't seem to invest in really understanding what we are looking for and building insight; they just pitch their 'idea-of-the-moment'." Commissioner

"Producers need to expose themselves continuously to the commissioners, they need to be front of mind when ideas and requirements come up." Commissioner

Public Interventions

"Northern Ireland screen paid a key role in supporting business development but we had to demonstrate that we were going to bring new business into Ireland." Regional Producer

"We need public incentives to encourage more factual investment." Scottish Producer

"The sector is becoming more collaborative; for example, the Scottish Production Talent Forum is very good." Large Scottish Producer

"Public funds need to focus on encouraging start ups; we need investments not grants." Scottish In-House Producer

"There is not adequate television support from Creative Scotland and Scottish Enterprise sees the sector as too risky; this compares dramatically with the effectiveness of Northern Ireland Screen" Scottish Producer

"We moved our show out of Scotland to Northern Ireland when it was re-commissioned because there was the right public investment which was not available in Scotland." Large Scottish Producer

"There is no cohesive investment strategy for the sector; Scottish Enterprise and Creative Scotland are not leaning in enough." Scottish Stakeholder

"It is very difficult to get Regional Selective Assistance as funding is based on the creation of permanent jobs, also the funding is a claim back so the company has to cash flow initially" Scottish Producer

Small Producers

"I am keen to commission new indies, they are the future of UK creativity; but I would like more mentoring from larger indies or key execs within the region, to help me de-risk smaller player on their initial commissions." Commissioner

"The smaller indies can be the most exciting - they have the 'fire-in-their-bellies' that the studio-owned indies often lack." Commissioner

"Our extensive work in the region and with Alba is not sufficient to give us credibility with network TV." Scottish Producer

"For me, with a very limited budget, it is all about having the confidence that a small indie is going to deliver what was agreed and on time and on budget." Commissioner

"Producers need to know their USP and not try and be all things to all people. Know what you stand for and have a clear proposition." Commissioner

Larger Producers

“STV could do much more to help build the indie sector.” Large Scottish Producer

“Scotland needs more companies of greater scale to build capacity within the sector” Scottish Producer

“It would be good if London companies doing Lift & Shift were required to partner with local companies to help build local capabilities” Scottish Producer

“We need more companies of scale and we need a drama capability in Scotland.” Scottish Producer

“Would like to see the larger Scottish producers act as feeders and mentors to some of the next generation of talent setting up.” Commissioner

“While Scotland is growing in importance it lacks the centre of excellence that gives stability and focus. By comparison Bristol has the Natural History Unit and Cardiff has the BBC's long run dramas.” Commissioner

US and New Commissioners

“To ensure sustainability we have had to build a broader base of relationships, looking outside the UK to key players in the US.” Regional Producer

“The US is a big pond for a factual indie; US players don't care whether you are regional or not.” Regional Producer

“You have to have an agent in the US, though it is arguable how useful they are” Regional Producer

“We have focussed on building our business in the US as the UK market for specialist factual is too small. The only major buyer is the BBC” Regional Producer

“The US offers bigger budgets per hour and longer runs – 10-part series versus the BBC's one or two-part series.” Regional Producer

“We don't need a US office to be successful there, but we do have to have an agent and commit to spending time there, not just relying on the markets.” Regional Producer

“We have been trying to broaden our base, with work for media-buyers like 3M, but the margins are wafer thin.” Scottish Producer

Growth Strategies

“We have grown our business by bringing in a new executive allowing us to expand into adjacent areas and reduce our dependence on too few commissioners.” Regional Producer

“We have invested in UHD / 4k to differentiate our product.” Regional Producer

“Investment in post-production has been key. Now the investment has amortised we can increase our margins and can invest in post production to ensure our product (and our pitches) are outstanding.” Regional Producer

“Bringing in new execs in complementary genres has been a key plank of our growth strategy.” Regional Producer

“We have used long running shows to build experience, retain and refresh talent and fund business development.” Regional Producer

“Investment from an international player has allowed us to scale up and invest in very high-end international drama.” Regional Studio

Local Commissioning

“The BBC has not actively sought to develop the sector in Scotland. The failure of Lift & Shift is evident in the static position of the Scottish industry.” Sector Expert

“It is a great benefit having a local market with an extra commissioner (BBC Scotland) but track record in local production is not taken seriously enough by network commissioners” Scottish Producer

“BBC Scotland comes in for flack but it is better than it has been – less tartan TV” Scottish Producer

“It is a big leap from local to network and London commissioners are reluctant to take risks on regional indies” Scottish Producer

“BBC and C4 commissioners has failed to develop capacity in Scotland” Scottish Producer

“We spend a lot of time convincing London we can deliver network quality” Large Scottish Producer

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