

Speech to Media Summit - Luke Johnson, Chairman, Channel 4

26th February 2009-02-26

CHECK AGAINST DELIVERY

Good morning. I thought we would start this morning's proceedings by enjoying a brief series of clips of some recent Channel 4 shows, some in the pipeline, and some recent film successes.

(Play film)

I hope you enjoyed that. It was a brief reminder of what Channel 4 is really all about – outstanding television and film across the genres.

I have been involved in a manner of speaking with Channel 4 almost since it started in 1982. Back then I was a trainee account executive at an advertising agency called BMP. We used to handle Channel 4's off-screen programme campaigns. I can recall Jeremy Isaacs telling me he thought Hunter S Thompson's *Fear and Loathing in Las Vegas* was a terrible book, and getting drunk with Keith Allen in Charlotte Street. Of course Mr Allen went on to be the dead man in *Shallow Grave*, which was the first feature directed by Danny Boyle – who went on to direct *Slumdog Millionaire* – both backed by Film4, as was his movie *Trainspotting*. An example of how Channel 4 has fostered screen talent both in front of and behind the camera.

But I was unquestionably a controversial choice as Chairman of Channel 4 when I was appointed in 2004. I was seen as an entrepreneur, rather than the sort of respectable broadcaster who might be expected to chair a statutory public corporation. Ever since, there has been a conspiracy theory that I was appointed with a brief to see through the privatisation of Channel 4.

But that belief doesn't really stand up to scrutiny. Firstly, I don't need the money. And secondly, I only took the post because I love Channel 4 and its output – what would be the point of being the person who sold off Channel 4 so it became just like any other purely commercial TV station? I'd like to think I was capable of a bit more enlightenment and sophistication than that.

I have always understood that Channel 4 is a remarkable hybrid that is all too rare – a state owned entity that is nevertheless self-funding, and a highly successful participant in the private sector economy. Although the government has been the sole shareholder for 26 years, it has never contributed any cash to fund the organisation. Instead it has forgone revenues from leasing analogue frequencies occupied by Channel 4 – and Channel 4 itself has competed in the marketplace for advertising revenue - and viewers.

Indeed given the extraordinary amount of state funding going on right now in sectors like the financial services industry, executives there and civil servants could do much worse than look at the long running success of Channel 4. It has remained independent, it has forged a hugely popular brand among difficult to reach constituencies, it has been highly creative in its output, and has grown significantly – all while remaining wholly in state ownership. If the bosses of Lloyds, RBS and the rest want some advice about how to deal with ministers and civil servants, I'm available.

Channel 4's status is unique among broadcasters. I have always felt an empathy with its culture – entrepreneurship ingrained alongside a public purpose. A sense of being non-conformist. A willingness to provoke and experiment. But overriding that, a desire to provide original and high quality British content from a huge cast of talents. Channel 4 has always had to survive on its wits, without a safety net of public funding or an ability to call on shareholders for fresh equity.

The tension within Channel 4 is a fascinating case study – the successful combination of commercial and artistic objectives. It has prospered by enshrining editorial innovation and diversity in its remit. It provides a regular supply of programmes that appeal to young, upmarket, light TV viewers who appreciate the feisty attitude that distinguishes Channel 4's output compared to other channels. Interestingly, our advertisers tend to like our unpredictable and somewhat mischievous output. They understand that we have fewer long running series than any other channel – it gives room in our schedule for more new shows than anyone else. This is at the heart of Channel 4's appeal, and why it is special. Younger

audiences are very attractive to advertisers because they are less entrenched in their buying habits; so advertisers pay a premium for them – which is a key element in the economics of Channel 4, and how its model has worked so well.

A tradition of self-reliance is at the root of Channel 4's broader independence of spirit, a quality that viewers identify as marking us out from our competitors – especially the BBC. It is worth noting at this juncture the revealing divergence in funding fortunes between the BBC and its commercially funded free-to-air television rivals. This year it is estimated the licence fee will be worth £3.6 billion. Meanwhile, assuming net advertising revenue declines around 12% this year, on top of decline last year, the combined total of ITV, Channel 4 and Five's revenues will be some £900 million less than that. No wonder the BBC does well – with that degree of funding it would be a scandal if they did not. The BBC very cleverly manages to perpetuate the myth that it got an unfair settlement in the last round of licence negotiations. They should try having to survive in the marketplace – then they would know what a tough settlement was like!

As you know well, there is currently an intense debate being waged about Channel 4's future funding. A bit of history might be useful here. Although Channel 4 has always been commercially funded, it has not always been entirely self-reliant. For the first decade of its existence, the programme budget was bankrolled by the various ITV companies in return for the right to sell airtime, together with a valuable cross-promotional deal. The founder, Jeremy Isaacs, had to worry about ratings and revenues, but in those days there were only four channels and no satellite TV or internet.

That system of funding changed in 1993, when Channel 4 started to sell its own airtime. For the next five years there was the safety net arrangement with the ITV franchise holders – a funding formula which required ITV to 'insure' Channel 4's programme budget in return for a share of the 'excess' revenues achieved. So Channel 4 paid out £412 million pounds to ITV in that five year period.

In 1998 Channel 4 became fully self-reliant, and has been ever since then. Until 2007, the Group mostly returned healthy annual operating profits. It reinvested in a

growing programme budget, which peaked in 2007 at £615 million, and a policy of ploughing any surplus into public service output. It also funded a digital diversification strategy, which led to the launch of E4, More4 and Film4 channels. In 2008 these channels produced a surplus in the region of £30 million.

But in the last decade the advent of digital TV has transformed the industry, and changed consumer behaviour. Audiences have fragmented, while advertising has shifted – partly to digital channels and partly to the online world. Despite this, the Channel 4 family had 12% of all viewing in 2008, which is close to an historic high, with more than 30% of its total viewing via E4, More4, Film4 and 4Music. But our principal source of revenue remains UK TV advertising. We have grown our share of the cake, and achieved over 24% of the TV advertising market in 2008 – a record.

Unfortunately the TV advertising market has shrunk considerably, especially in the last two years. From a peak of £3.7 billion it could fall as low as £2.7 billion this year. We have been forecasting a structural shift in the UK advertising market for five years. Only now, in the face of a major economic downturn, are stakeholders finally taking notice. For the market as a whole, there was a 10% fall in the second half of 2008. For the first quarter of 2009 the forecast is a slump of close to 20% in ad revenues; at Channel 4 we should stem that decline to around 11%. But we are forecasting an overall decline of at least magnitude for the year.

We have responded promptly to deteriorating market conditions. In September last year we cut costs by £50 million; we cut a further £75 million at the beginning of this year, including 200 job losses, or 20% of the workforce. Such actions are not much fun, but necessary if we are to cope with such challenging conditions.

This all matters to the outside world because Channel 4 is a major funder of British content – and TV revenues are no longer sufficient to sustain historic levels of that investment in original programming. Meanwhile online advertising in this country has grown in a decade to a likely £3 billion plus this year. The significant majority is earned by wholly US groups – parasitical organisations like Google, also Yahoo, MSN and AOL. They spend essentially nothing on content of any kind.

This siphoning off of advertising revenue by foreign organisations undermines investment in domestic content, and is a genuine threat to the quality of British television and our national culture. If we want home grown TV of a similar standard to that in Italy, then that's fine. But I would argue it's more important than that. Our nation's huge success in entertainment and media is in part due to our culture of public service broadcasting – and not just the BBC. To leave the BBC as a monopoly provider of such material would be a tragedy. It would lead to a blandness and uniformity which would be suffocating.

In recent and coming weeks the following shows have been or will be broadcast on Channel 4 – all are at risk if the current trends continue: in current affairs, Dispatches and Unreported World; in drama The Devil's Whore and Red Riding; in documentaries The Ascent of Money, Christianity: A History and Life and Death at 18; in comedy Free Agents and Plus One.

Now I should just make a special mention of Film4. Slumdog Millionaire, one of the most successful British movies in recent history and winner of 8 Oscars, would not have happened without Film4. We optioned the novel, developed the script, brought together the key talent including the director and scriptwriter, and co-financed it. Film4 has actually won 5 more Oscars in the previous 4 years for films like The Last King of Scotland and Motorcycle Diaries. And we have some exciting new productions like The Lovely Bones and new movies by Sam Taylor Wood and Kevin MacDonald. None of this would have happened without Channel 4 as its generous sponsoring parent.

In truth, this argument is not only about our positive influence on society. It is also about economics. The creative industries support around 2 million jobs and generate output of £60 billion. We are a key part of that – we work with more independent producers than anyone else and our suppliers never have to compete with favoured in-house production. Price Waterhouse Coopers estimates that our annual programming investment of around £500 million generates £2 billion of added value for the economy and supports around 22,000 jobs. And it fosters entrepreneurship in the 300 plus indies we work with each year.

British creativity enjoys a remarkable reputation for brilliant output across books, theatre, film, television, videogames, and music. We could do even better. But we need to invest in these industries – and that includes Channel 4. And the Digital Britain report is a great opportunity to equip the broadcast sector to compete more effectively in a global marketplace.

The Digital Britain interim report, and Ofcom's second public service broadcasting review were both published last month, and agree with our analysis of falling levels of British content investment. Both endorse the need for competition to the BBC in the supply of a full range of high quality programmes for British audiences. Both also accept that Channel 4 has an outstanding track record of public service delivery, but that its current institutional funding model is unsustainable.

A key recommendation of the Digital Britain report is that Channel 4 should be the cornerstone of a strong second force in PSB, but with sufficient scale and flexibility to sustain a viable, commercially funded business model to support a revised remit. We proposed a tie-up with BBC Worldwide as an attractive solution. And the Secretary of State Andy Burnham and Broadcasting Minister Lord Carter have agreed it is a sensible starting point to explore new structures.

So we are discussing with BBC Worldwide a broad, UK-based joint venture involving a range of commercial businesses. This may be the first step towards a wider combination. It would be a partnership of complementary public organisations – both focused on delivering public service ends through commercial means. Any transaction does not rely on the injection of public funds to work, although we do not discount possible access to contestable public funds to support Channel 4's extended public service remit.

There are complementary strengths, with Worldwide's distribution and content, and our brands, reach with key audiences and cross-promotional network. The arrangements we have been looking at deliver some considerable synergies, but also allow Channel 4 to retain its independence and boldness. It would deliver a stream of profits to protect our delivery of a public good. A joint-venture like this would diversify Channel 4's revenue stream, and would create a more robust

business. Channel 4 would remain publicly owned but predominantly commercially funded, preserving its ability to innovate, take risks and provide an alternative to the BBC. This would help to maintain the plurality of the broadcasting ecology in the UK and enhance the quality of British television.

Such a deal would build the value of public assets, and could reduce any possible calls on general taxation or the licence fee. We do not believe it would require primary legislation. But some of the benefits might take time to flow, and depending upon the state of the advertising market, Channel 4 might require some transitional underpinning.

It is clear that other options are under consideration to bridge Channel 4's funding gap. I am genuinely open-minded about any option that can help deliver a more sustainable business model and underpin our public service delivery. But the board of Channel 4 is concerned that there is an inherent conflict between maximising public service and profit – as ITV's long flight from seriousness and diversity in programming demonstrates. I worry that profit seeking shareholders would sign up to all sorts of PSB commitments as a price of gaining a stake in Channel 4 – and then lobby to remove them. I also fear that part privatisation by stealth of Channel 4 would mean there could only ever be one buyer for the rest – at a discount – and that taxpayer value would therefore be destroyed. My view is that if the political desire is there to sell off Channel 4, then do a proper auction and maximise proceeds. I happen to think, after extensive discussions with politicians on all sides, that there is currently no appetite to privatise Channel 4 at Westminster. But if our political masters decide to do that, don't fudge it with a messy deal that neither secures PSB output nor the highest price for the taxpayer.

So where do we go from here? Well after years of debate, there is now a relatively short window to make decisions about Channel 4. The Government has asked for responses to the Digital Britain report by 12th March. It hopes to publish final recommendations in a conclusive report by the early summer. And I believe there is goodwill to reach a worthwhile agreement between Channel 4 and BBC Worldwide within this timeframe. Other options must be considered, but this is the best bet so far in my opinion.

Channel 4 has been a magnificent intervention – it has made an enormous contribution to the range and quality of broadcasting and British cultural life for over a quarter of a century. It has informed and influenced all our lives. It is a classic example of using commercial means to deliver public goods that the market alone would not supply. Despite the intense pressure on its funding model, Channel 4 has maintained the quality and range of its creative output – with a huge haul of recent film Baftas for *Slumdog Millionaire*, *Hunger* and *In Bruges* as well as Golden Globes and Oscars. We continue to make and show stuff of real distinction and originality, involving new faces and voices. This is what Channel 4 has always been and can continue to achieve, with some help.

The debate about Channel 4's future has dominated my tenure as Chairman. But I feel confident that as I enter the last year of my job, a way can be found to preserve Channel 4's entrepreneurial spirit despite the structural issues and the economy, and that it will remain a public body of real cultural value and impact.

Thanks for listening.