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MEDIA ECONOMICS AND TRANSFORMATION IN A DIGITAL EUROPE

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Business models under pressure

In contemporary media and communications industries, competition is intensifying following an explosion of digital content and platforms, on-going globalisation and market fragmentation, and constantly changing media consumer preferences and habits. Despite the growing concentration of ownership (i.e., more media are in the hands of a few groups), the total amount of media outlets in Europe continues to grow, and creates fierce competition for consumers and advertisers. The omnipresence of digital intermediaries (i.e., online distribution platforms that distribute content produced by others), such as Facebook, Google and Apple, and the disruptive potential of online and mobile technologies are further eroding the economic base of traditional media organisations. Digital technology is undermining the foundations of media organisations' business models (i.e., the logic of how organisations make money) that have been highly successful for the past decades (Macnamara 2010). The main business model for most media industries, especially newspapers and audiovisual media, is advertising-supported and built upon the idea of a 'dual marketplace': Provide (nearly) free content to attract audiences, and 'sell' these audiences to advertisers (Küng 2008). In spite of new yet immature consumer revenue sources related to digital services, advertising remains at the core of the European media industries' success and survival.

However, this high dependence on the advertising industry may become a major threat to the media business for two main reasons. First, the European advertising market was hit hard by the recent economic downturn: In the 2008-2009 period TV advertising expenditures fell dramatically by 16 per cent to about €27 billion gross revenues (European Audiovisual Observatory 2012). The recession affected national markets to varying degrees (minus 32 per cent in Spain, plus 8.3 per cent in Portugal), confirming the thesis by Picard (2011a) that the economics of small and large media markets differ significantly. Operating revenues and profit margins of TV broadcasters went down by 14 per cent and 52.1 per cent, respectively. As a result, the downturn in European TV advertising led to cost cutting and efficiency measures, ultimately reducing staff costs and investments in high-quality productions. Whereas TV markets have relatively recovered from this decline, newspaper and magazine advertising has failed to do so (Table 1). Second, and in addition to the aforementioned volatile conjunctural dip, advertising markets are experiencing a structural decline that challenges the ad-supported business model. Between 2009 and 2014, print advertising revenues of European newspaper publishers declined from €17.2 billion to €12.9 billion (minus 25.6 per cent) and are

expected to drop further to €10.4 billion (minus 39.5 per cent) by 2018 according to analyst PricewaterhouseCoopers (2014).

Table 1: Evolution of media advertising market in Europe (PricewaterhouseCoopers, 2014)

	2009	2010	2011	2012	2013	2014	2015
TV	21.239	23.034	23.164	21.989	21.531	22.004	22.542
Radio	4.345	4.498	4.494	4.397	4.389	4.434	4.503
Newspapers	18.065	17.753	17.245	15.875	15.064	14.453	13.903
Magazines	8.291	8.445	8.383	7.824	7.672	7.596	7.520
Online	13.606	15.795	18.376	20.762	23.545	26.130	28.549

Advertisers are starting to move significant budgets to online and redirecting their money from print to digital platforms. Internet advertising is rapidly growing, but at this moment unable to compensate for the decline of traditional business units: Print advertising revenues in Europe will have fallen with about €7 billion, digital newspaper advertising revenues are projected to grow from €927 million to €2.2 billion by 2018. It is acknowledged that the growth of the online advertising industry is largely at the expense of the newspaper industry: A growing number of online platforms and search engines provide opportunities for specialized classified advertising, such as real estates, employment and dating (Evans, 2009). Advertisers love the targeting efficiencies, opportunities for personalized offerings, accurate measurability of consumption and lower costs of online advertising. Half of the online advertising revenues comes from paid search advertising, which is controlled by US online giants Google and Facebook. The dominance of both platforms represents one of the main problems of the European media industries: Advertisers are turning to digital intermediaries that are not owned by traditional media organisations and that piggyback on media organisations' investments in high-quality information and entertainment content.

The decline of advertising revenues who form the main pillar of the media business model, however, induces media organisations to look at alternative revenue sources and to consider consumer payments through subscription and pay-per-use models (Evens 2010). Cable and satellite operators have benefited from the transition to digital TV services, and have seen their revenues steadily rising since the mid-1990s. Waterman and Han (2010) empirically show that consumer expenditures for pay-TV have been on the rise for many years, and prove quite persistent during economic downturns. The shift towards consumer payments, however, has not proven evident for all types of media organisations. As the circulation revenues of European newspapers fell from €21.6 billion to €17.9 billion between 2009 and 2014 (despite price increases), digital circulation revenues increased from €11 million to €937 million – but still accounting for no more than 4.9 per cent of total newspaper revenues. The number of paid digital news services is growing rapidly, but digital consumer payments are by far not enough to compensate the decline in print sales. In literature, it has been regularly shown

that people's willingness to pay for digital news is relatively low, and that digital subscriptions are no sustainable model at this moment. Hence, monetising digital content, or managing the 'free-to-fee' transition, remains a tough challenge for many media organisations (Kammer et al. 2015).

The difficulties to respond to the changing economic conditions are eroding the financial stability of European media organisations. Picard (2011b) notes that when the environment of an industry changes, so do the factors that support the business model. The shift to digital and the erosion of traditional revenue streams therefore urges media organisations to re-design their current business model and adapt to the new economics of digital media. Although it is hard to contend that the entire media business is in crisis – European media organisations such as Sky and UKTV report record revenues and are more profitable than ever – it is fair to say media organisations have to prepare themselves for a digital future. Since digital intermediaries including Netflix, YouTube and Spotify have conquered, and in some instances disrupted, the European media market, these platforms are changing the 'rules of the game' and tilting the power balance (Simon 2014). They increasingly control digital distribution of media services, hindering traditional media organisations to go in direct touch with and learn more about their consumers. Hence, media organisations need to re-invent themselves and transform to become digital proof. This is what this chapter is all about.

Digital media economics

The advent of the Internet is turning the media industries completely upside down and is changing the rules of the game. New media platforms such as search engines (Google), e-commerce services (eBay) and/or social networking sites (Facebook) bring a significant change in the dynamics of the sector and pose huge challenges for the traditional industry players. The economics of the digital media environment are the inverse of the analogue, and are affecting the legacy media business logic. In the analogue media world, content (supply) was scarce and attention (demand) was abundant: Competition and consumer choice were limited as it was difficult to enter the industry (high entry barriers). However, digital technology has almost eliminated entry barriers and the supply of information and entertainment sources available online has exploded. Hence, content becomes abundant, but media organisations find it much harder to attract the attention of the audience (Webster and Ksiazek 2012). Legacy media organisations have to learn to play by the following rules of the digital media economy in order to build a sustainable business model:

First, digital media become detached from any physical medium (DVD, CD, newspapers, etc.) and can therefore be unbundled from traditional media packages at negligible costs. The 'atomisation' of content allows that micro-content is consumed in smaller chunks than before. Fuelled by digital distribution, unbundling is prevalent in the digital media economy, and is reshaping distribution models and pricing schemes (Elberse 2010). Whereas music fans had to buy full albums in the past,

iTunes and Spotify enable them to buy/listen to individual tracks. Newspapers become unbundled since individual articles are put for sale, or freely available on other news websites. Even in TV, the ‘great unbundling’ has started since TV channels such as HBO and RTL launch stand-alone streaming services (i.e., separate from pay-TV subscriptions), YouTube allows for content snacking and Netflix promotes à la carte viewing of TV series (Lapowsky 2014). The explosion of content implies that media organisations must rely on powerful brands to pop out in this ocean of content and to aggregate consumer attention.

Second, the abundance of digital content is made available via a multitude of platforms and devices. With the spectacular growth of the Internet and mobile media, media content is now available on multiple platforms. Hence, media organisations have responded by migrating towards a diversified multi-platform approach to production and distribution of content: content is now accessible via all possible platforms and devices. Newspapers such as the Financial Times and the Guardian are in the process of adopting a ‘digital-first’ approach and tailor content to specific digital platforms and formats (Doyle 2013). In TV, the concept of ‘connected viewing’ is used to describe the larger trend across the media industries to create a multiplatform, more interactive entertainment experience by integrating digital tools (e.g., Twitter or Facebook) with traditional screen media practices. Moreover, pay-TV operators such as Sky and Vodafone are betting on mobile TV and streaming apps to team up with changing viewing behaviour. Certainly, this fundamental shift in the digital media ecology challenges conventional understandings of how media content is created, distributed and consumed (Holt and Sanson 2014).

Third, disruptive business models are increasingly based on the sale of ‘access’ rather than ‘ownership’ since consumers search for the best experience and flexibility. The declining costs of unlimited storage helped increasing the popularity of cloud services so that consumers have access to media content from each device. A decade ago, consumers preferred collecting music or movies so as to store digital files on their computer. Nowadays, consumers prize ‘access’ over ‘ownership’ and want to have instant access to as much content as possible (Wikström 2014). In the music business, streaming service Spotify is replacing the download model pioneered by iTunes, which was a welcome alternative to the slacking CD sales. By subscribing to online video platforms such as LOVEFiLM and maxdome consumers secure unlimited access to an impressive library of video content. In the Netherlands, initiatives such as Blendle and Elinea are experimenting similar ‘streaming’ models for newspaper and magazine content. Despite consumer popularity (Spotify has over 75 million active users; about one third pays for access), most streaming platforms are still struggling with profitability due to high licensing and copyright costs.

Fourth, the vast amount of content available in the digital space, helped by the low costs of digital storage and distribution, creates opportunities to cater for an unlimited variety of unique tastes. Whereas physical media are constrained by limited space (e.g., newspapers have a maximum amount of pages), digital outlets have endless space: The Internet theoretically offers a wider range of content than offline media. Anderson (2006) introduces the concept of the ‘long tail’ to show there is a mass market potential for niche content that is not delivered by physical media. The immense supply of niche content, he further argues, will lead to the demise of the blockbusters that attract the most attention. Hence, the long tail is basically about the economics of abundance. Online video and news portals can provide more information, even without geographical constraints, at considerable lower costs. News providers including the Huffington Post and Politico present high-quality journalistic content via the web, and benefit from the low costs for production and digital distribution. Digital kiosks such as Blendle enable access to all Dutch newspaper articles under a micropayment model (Graybeal and Hayes 2011).

Fifth, digital intermediaries are far ahead of traditional content providers with advanced technology strategies and analytical know-how. In contrast to traditional media organisations, most online platforms are technology firms in first instance, and maintain digital infrastructure that carries information and entertainment content (similarly, Uber is no taxi company, but a high-tech company). These intermediaries are harvesting the power of big data – vast amounts of data about media consumption patterns, personal data, etc. – to personalize offerings and make content recommendations. Netflix shows how big data is influencing the TV industry by using its massive amount of data on viewership – more than fifty data points about every movie or TV show being consumed – to predict which programs it should license and/or commission (Havens 2014). Similarly, YouTube, heralded one of the largest big data ventures in the world, incorporates all Google’s expertise in gathering and analysing consumer information to effectively target video users with relevant videos, marketing and advertisement (Sathi 2014). Big data is certainly changing the way media organisations will create value in the digital economy.

The developments sketched above suggest that digital intermediaries operate under totally different economic logics and, hence, business models than traditional media organisations. In contrast to traditional media organisations, digital intermediaries are not hindered by legacy business models and operate under organisational structures that were designed for digital business from their conception. These ‘pure players’ operate under lower cost structures (e.g., the Huffington Post has no need of printing offices resulting in lower distribution costs) and pressure legacy media organisations to re-allocate resources from traditional to digital business units. Doyle (2015) discusses the example of Future Publishing, one of the largest magazine publishers in the UK, and shows how the shift to delivery across multiple platforms affects patterns of staff activity. Whereas 10 per cent of staff effort

was devoted to digital activities in 2009, the equivalent had risen to about 40 per cent by 2013. The fact that audience attention is migrating to online and mobile platforms has been the driving force of company renewal, and should induce media organisations to bet on digital activities, not only as a matter of survival but as the basis of future growth. Hence, digital transformation is no longer a matter of luxury, but will be at the heart of successful media organisations in the 21st century.

Experiment new business models

In the digital media ecosystem that is marked by high velocity and disruptive innovation from pure players such as Buzz Feed and the Huffington Post, media organisations are pressured to abandon the dominant logic that underlies their business models. A report by Pew Research Center (2012), however, shows how newspapers are reluctant to change their legacy business models: For every \$1 gained in digital, \$7 are lost in print revenue. Media organisations will need to learn how to embrace the evolution towards digital media, and take benefit from its revenue opportunities. Rather than an ‘industry stampede’, McPhillips and Merlo (2008) argue that the industry will experience an evolution, as old and new business models first co-exist until they ultimately converge. They suggest a transition period during which the dominant logic will be gradually adapted to digital media economics. But developing new business models is a difficult challenge: Several scholars emphasize its experimental character (trial-and-error), and stress that failure offers learning opportunities (Chesbrough 2006). Hence, media organisations need to develop capabilities to identify and experiment new business opportunities, and act highly entrepreneurial (Achtenhagen et al. 2013).

Axel Springer, one of the largest publishers in Europe (Bild, Die Welt, etc.) acts as a textbook example of how to manage the digital transformation process. In 2006, the German publisher started realising that its print activities would not be enough to sustain the business model and looked for new ways to monetize and distribute its news brands. This required re-evaluating its activities and adapting its organisational structures to successfully compete with online giant Google, while continuing to balance traditional and digital strategies. Axel Springer decided to divest over 30 operations (including regional newspapers and TV magazines), embrace entrepreneurship and bet on revenue growth through three business models: paid content, marketing and classified advertising. It started investing in new digital ventures with growth potential including Stepstone (job classifieds), Idealo (e-commerce), SeLogger (real estate listing), Immoweb (real estate classifieds) and Blendle (news à la carte). The financial results suggest that the digital transformation process is paying off: In 2012, digital revenues took over newspapers revenues for the first time. In 2014, the company reported that digital media activities account for 54.5 per cent of the group’s total revenues (€3.1 billion) and that about three quarters of total advertising revenues (€1.8 billion) were generated by digital activities (Axel Springer 2015).

ProSieben.Sat1 Media, a German media organisation that operates free-to-air TV channels across Europe, bet on digital media after it witnessed growth in TV advertising market was slowing, and pursued a diversification strategy (i.e., entering a market or segment which the business is not in). In the past five years, the organisation successfully transformed itself from a TV broadcaster into a broadcasting, digital entertainment and e-commerce powerhouse. The digital diversification activities include all revenue models that not directly depend on TV advertising. Two years ahead of iTunes, maxdome was launched as the first online video-on-demand platform in Germany; it quickly became the market leader. Recognising a large gamer base amongst its audience, ProSieben launched a gaming business that has achieved rapid growth. Moreover, it started investing in digital start-ups, especially in media and adjacent e-commerce platforms, such as Zalando (fashion) and Trivago (travel). Although such diversification strategy deemed risky, the organisation successfully positioned digital as key of its growth strategy. It lessened its dependence on TV advertising, which share declined from 86.7 per cent to 71.7 per cent of total group revenues between 2011 and 2014. Simultaneously, the share of digital activities grew from 11.6 per cent to 21.2 per cent, and is expected to contribute between 25 per cent and 30 per cent of all revenues by 2015 (ProSiebenSat.1 Media 2015).

Developing digital platforms and expanding into new business areas often implies partnerships with competitors, either fellow legacy media organisations or pure players (Evens 2014). In the UK, free-to-air broadcasters BBC, ITV and Channel 4 united with Internet service providers BT and TalkTalk to develop the on-demand video platform YouView and strengthen their digital presence. Increasingly, legacy media organisations close partnerships with pure players (and vice versa): Online platforms need the branded media content to pop out of the digital ocean whereas media organisations benefit from online platforms as distribution channel. In this context, Facebook recently launched two remarkable initiatives as part of a ‘charm offensive’ towards traditional media. First, Facebook Instant Articles provides readers direct access to news content from the Facebook platform instead of clicking through to the respective websites of the news publishers (in return, Facebook will offer the publishers 100 per cent of the ad revenue sold around the articles). In addition to five US publishers, BBC News, the Guardian, Bild and Der Spiegel are the first European publishers to trial the new service (Sweeney 2015). Second, Facebook started sharing 55 per cent of ad revenues with some video creators, including HBO, for uploading their clips to the platform because Facebook surpassed YouTube to become the biggest video service (in total views)(Foxx 2015).

Data-driven business models

Owing to the erosion of the existing business model, together with the growing importance of online and mobile platforms, media organisations have to undergo a digital transformation process. This means organisations have to rethink structures and activities, and adapt to the economic logic of the

digital media environment. Media organisations have traditionally focused on the supply side (e.g., pricing, product portfolios, etc.) to create efficiency and cut costs. Digital intermediaries, on the contrary, give priority to creating an optimal user experience and building a large customer base (demand). In digital media, powerful network effects – the fact that the utility people derive from using Facebook or Twitter increases as family and friends join the network – are the key to winning competition over another platform (Vukanovic 2009). With attention becoming scarce, the supply of more content will not help media organisations in gaining a competitive edge. As Berman et al. (2011) notice, focus on the user, in the form of a detailed understanding of the media consumer and building a close relationship with the consumer, should be put central in media organisations' digital transformation strategy and development of new business models.

First, media organisations are establishing platforms (online video platforms, digital kiosks, e-commerce, etc.) to reconnect with media consumers and control new types of revenues. This implies that media organisations are transforming into intermediaries themselves and become the primary interface with their consumers. The rise of the platforms in media and communications industries faces legacy organisations with a threat of 'disintermediation'. This entails the process of eliminating business activities by disruptive innovators (e.g., iTunes and Spotify replace music stores, Netflix disrupts pay-TV operators, etc.). Distribution gets controlled by digital intermediaries, increasing media organisations' dependency on these platforms. By launching digital platforms as part of new business models, media organisations try to off-set the disintermediation danger, adapt to the digital economy and bet on 're-intermediation' (Bustamante 2004). In addition to stand-alone streaming video services, TV broadcasters are launching companion apps via second screens (tablets, smartphones, etc.) so as to provide enriching content to and interact with their viewers. According to Lee and Andrejevic (2014), interactive TV apps play an important role in re-aggregating audiences and bring back viewers to real-time TV viewing. The hope is that social network discussions promote viewership by encouraging viewers to tune in to what their friends are watching, and generate real-time information about viewing behaviour.

Second, media organisations are collecting detailed information about their consumers so as to pursue data-driven strategies to create value. According to Stone (2014), big data represent one of the biggest opportunities for the media industry, and will certainly become one of the cornerstones of media organisations' future business models. Hence, media organisations have started experimenting big-data strategies so as to engage with their audience more deeply by suggesting personalized content recommendations, serving targeted advertising and/or improving the user experience. Sky, UK's biggest pay-TV operator, uses its AdSmart platform to tailor advertising based on customer data, set-top box data and information from external consumer databases. By increasing the effectiveness of ad campaigns, Sky hopes to keep the amount of TV advertising investments at a comfortable level.

Moreover, newspapers hire tech-savvy journalists that know how to use databases of leaked documents, such as Wikileaks, or data sets made accessible by public and private organisations (e.g., open data) to produce compelling news stories (Fink and Anderson 2015). The proliferation of platforms is leading to extreme audience fragmentation: Audiences are ‘inherently cross-media’ and increasingly turn to alternative information sources such as social networking sites and blogs (Schrøder 2011). This evolution urges newspapers to follow their readers across different platforms, measure cross-media news consumption (smartphones, tablets, etc.) and provide them personalized offerings.

Since digital intermediaries have become the primary touch point for media consumers, establishing platforms and deploying big-data strategies would allow media organisations to claim back the media consumer. In the digital media environment, legacy organisations have lost the control of the customer relationship and therefore have no clue who their readers/viewers/listeners are. Whereas Facebook, Google and other digital intermediaries have a detailed understanding of the consumers’ identity, interests and behaviour (browsing, purchases, etc.) and can address them in a personalized manner, newspapers and broadcasters heavily rely on these platforms to gain insight in consumer behaviour. Legacy media feed online platforms by uploading content on YouTube, licensing programmes to Netflix, sharing articles with Facebook and/or selling newspaper editions via iTunes, but receive little back in return. Legacy media organisations therefore need to use digital technology so as to monitor consumer activities that are tracked, recorded, stored and monitored for marketing purposes. However, the transformation process does not stop with collecting and producing large data sets; most organisations, especially local and regional players, continue to struggle how to make sense of these data and make them actionable.

Conclusions

This chapter elaborated on the wave of digital change for legacy media organisations, and discussed the challenges the dominant media business logic faces from digital intermediaries. Advertising revenues are slightly migrating to digital platforms so that media organisations have to rethink their main business model. It was contended that online platforms such as YouTube and Netflix are changing the rules of game, and that media organisations have to adapt to the digital media logic in order to fulfil their role in the media economy and, to a wider extent, society. Business models need to change over time, and their underlying factors need to be in line with the wider trends in business. A collapse of traditional media organisations such as news publishers and TV broadcasters would not only cause economic damage – media industries account for about 2 per cent of GDP in European countries – but, probably more important, would also do major harm to society: The erosion of quality journalism and the limited supply of information would threaten democracy and diminish

the role of the media as the fourth estate; lack of locally-produced programmes would reduce the cultural richness of the European media landscape. This text has predominantly addressed the challenges for media business models from an economic perspective, but it cannot be stressed enough that a solid economic base of the media industries is a vital condition for a flourishing press and healthy audiovisual sector that guarantees consumers and citizens with the provision of quality journalism and original, often domestic, entertainment productions such as movies, fiction series and documentaries .

The main message of this chapter, albeit implicit, is that the impact of digital technology in media and communications industries, not only in Europe but all over the world, is growing and challenges the legacy business model. In the past, media organisations had to focus on the production of information and entertainment content that met the expectations of the audience, and relied on distribution companies to take care of the technological infrastructure that brought the content to the audience. In the digital media economy, however, the dematerialisation of media content has made the boundaries of the distinct technologies – TV, radio, print, etc. – completely obsolete and marks the crucial importance of digital distribution, in most cases the Internet (fixed or mobile). As a matter of fact, control of digital distribution is a major advantage in contemporary media and communications industries. Although Internet service providers continue to control the physical infrastructure (e.g. wires, cables, base stations), intermediaries such as Google, Facebook, Apple and Amazon – the Gang of Four – have become dominant service platforms in Europe: Google has a market share of over 90 per cent in the European search engine market, Google and Facebook control over 80 per cent of the online advertising market, etc. The fact that European media organisations crucially depend on these US-based platforms to be successful, could be problematic for the sustainability of the European content industries. Hence, they have to close partnerships with these platforms and change business models so as to remain competitive in the digital media ecosystem.

Declining advertising revenues and intense competition from pure players is putting pressure on the legacy business models. Media organisations therefore need to undergo a transformation process and put digital technology central in their daily business operations. The Internet will gain even more importance as distribution channel, and the leading digital intermediaries will only strengthen their position. However, it would be wrong to predict the collapse of the traditional media business: The impact of digital technology on the media industries comes as an evolution, not a revolution. People will continue to read newspapers – with a slow migration to digital editions – and view their favourite TV shows in a traditional, possibly old-fashioned, way. This implies that media organisations have the time to gradually adapt their business model and need to learn how to progress with their digital activities without cannibalizing their still profitable analogue operations. Digital intermediaries will not substitute legacy media, but there will exist a mutual dependency between both. The many

examples in the text do suggest that established media organisations are already learning how to respond to the digital challenges, how to deal with innovation and transformation, how to integrate digital technology, how to expand digital activities and how to secure a solid future. There is probably a lot of work to be done, and it might be that the challenge of digital intermediaries will grow, but chances are likely that European media organisations will be able to re-invent themselves and continue to provide high-standard information and entertainment content in the future.

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