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DYNAMIC CAPABILITIES AND SUPERIOR FIRM PERFORMANCE IN THE UK MEDIA INDUSTRY

Abstract

The past decade has seen a transformation in the way television broadcasters have managed their businesses. This paper examines the theory of 'dynamic capability' in two UK television broadcasters, BskyB and ITV, and their attempts to transform themselves into multi-product, multi-platform media companies. Using Comparative Financial Analysis and Content Analysis in a time series, this paper illustrates how the strategic management of media firms can be significantly different for two companies operating in the same sector. This research demonstrates an original contribution to knowledge by providing evidence of the dynamic capability performance effects of significant players in UK television broadcasting.

Key words: Dynamic Capabilities, Media Organisation, Media Management, Corporate Performance Management, Strategic Management.

The emergence of the new media environment has paved the way for new technologies, digitalisation, the proliferation of television channels, time shifted viewing habits and multiple platforms to consume television content. Albertazzi and Cobley (2010:179) noted that the "transformational changes" in this new competitive environment may have felt like an unwelcomed revolution to some television broadcasters, whilst to others, it is likely to have provided them with a unique sequence of evolutionary opportunities. This transformational context raises a number of questions for business and management researchers. Firstly, how have television broadcasters managed their businesses and responded to the challenges presented in a new media environment characterised by change and uncertainty? Secondly, how have they managed and adapted their resources and capabilities to remain competitive?

This paper examines the theory of 'dynamic capability' in UK television broadcasters and their adaptation to a competitive landscape heavily influenced by new media technologies. Colapinto (2010:60) set the tone for this discussion arguing that traditional media companies have been required to "adopt dynamic responses to the challenges of a multi-platform television market". As such, the concept of dynamic capability is ideally placed to investigate the strategic management practices of media firms. This theory has generated a range of definitions, interpretations and strands of inquiry in literature, making for an eclectic mix of knowledge, and bearing this in mind, this paper has opted to focus on four fundamental principles. Firstly, that dynamic capability is concerned with change. Secondly, that this change process is centred on a firm's ability adapt and renew their resources, capabilities and competencies. Thirdly, that this process requires deliberate resource investment in new organisational learning and processes that aim to produce positive effects on corporate performance and competitive advantage over time. Fourthly, that this process of adaptation occurs in a compressed timescale due to the fast changing nature of market conditions.

In particular, this research sought to explore the question of why some organisations are better at managing their resources to produce superior performance than others. Ghobadian, Liu, O'Regan and Thomas (2008) noted that understanding firm performance been an important area for researchers, and to illustrate this aspect of strategic management, this research compared and contrasted the dynamic capabilities of two UK broadcasters, BskyB and ITV, their adaptation in response to the new media environment, and how this has lead to differing corporate financial performance.

LITERATURE REVIEW

The idea that television broadcasters may or may not have a dynamic capability arose from theorists questioning how firms sustain competitive advantage and superior performance in such high velocity conditions (Oliver, 2012) where "the increasing dynamism of the environment" (Pettigrew, Thomas and Whittington, 2007:143) makes it increasingly difficult to remain competitive. Many scholars (Mintzberg, 1987; Senge, 1990; Leavy, 1998; Zollo and Winter, 2002) concluded that superior performance is driven by a firm's ability to learn, adapt and change their resource configuration in order to produce a series of temporary competitive advantages. Lawton and Rajwani (2011:167) took this line of thinking further and concluded that "dynamic capabilities are the bridge between firm resources and business context" and as such, this concept provided a useful lens through which to examine superior organisational performance.

The central tenet of 'dynamic capability' is a consideration of the renewal of firm resources and capabilities. It suggests that tangible resources are configured and utilised to generate value and rents, and that intangible resources in the form of skills, experience, learning, systems and processes create competitive advantages that cannot easily be imitated by competitors. Ambrosini and Bowman (2009:30-35) argued that dynamic capabilities "specifically focuses on how firms can change their valuable resources over time". They go on to argue that the words dynamic capability refer to the drive and enthusiasm of a firm in their "renewal of resources". This perspective echoes the earlier work of Teece and Pisano (1994), Zollo and Winter (2002) and Lal and Strachan (2007) who emphasised that a changing external environment required firms to adapt and reconfigure resources, assets, operating routines and competencies in order to improve its effectiveness and competitiveness in the pursuit of superior performance. In a sense, the idea that firm capabilities need to be dynamic is a consideration of the competitive environment, its future direction, and how a firm can take advantage of the opportunities provided in their existing and future markets.

The theoretical frame for this research identifies and differentiates the concept of dynamic capability by considering the discrete, but inter-related definitions of 'capability', 'core competence' and 'dynamic capability'. Whilst Ljungquist (2007:394) noted that these terms are often amalgamated in literature, there is more value in understanding each concept and "distinguish(ing) them by their characteristics". Although many organisations have access to similar resources, it is their ability to manage, as Grant (1991:119) suggests, "a team of resources to perform some task or activity" better than competitive rivals and extend the resource potential that differentiates one organisations capability and performance over another. Winter (2003:991-993) developed this argument suggesting that capabilities had a hierarchy. Starting with 'zero level capabilities' he suggested that this low level capability described the ability of an organisation to "earn its living by producing and selling the same product on the same scale, and to the same customer population, over time". He went on to point out that dynamic capability governs the rate of change in zero level capabilities, and that they have a faster rate of change, and therefore, are different to zero level capabilities.

In their review of strategic management literature, Pettigrew et al (2007:39) noted that the idea of firm 'capability' should also be extended to a consideration of competition in the market place, and therefore, comparisons of long term superior performance. As such, firm capabilities can be considered as a minimum threshold of resources that are required to satisfy market requirements. They proposed four fundamental principles of capability-based competition between firms; corporate strategy should be built on business processes, not products and markets; competitive success depends on transforming a company's key processes into strategic capabilities that consistently provide superior value to customers; companies create these capabilities by making strategic investments in a support infrastructure that links together and transcends traditional SBUs and functions; a capabilities based strategy is championed by the CEO.

Bitar and Hasfi (2007) support this overarching view and suggested that capabilities arise from a range of organisational elements including the interaction of people, structure, systems and values. It is this conceptualisation of organisational capability providing a means of competitive advantage that gives rise to the notion of unique and distinctive business processes that provide customer value, thus extending the debate into the realm of core competence.

A generation of researchers have been exposed to, investigated and developed the conceptual thinking of Prahalad and Hamel's (1990:82) idea that core competencies are "the collective learning in the organization, especially how to coordinate diverse production skills and integrate multiple streams of technologies". We know that core competencies provide sustainable competitive advantage through their unique ability to provide customer value. However, we must acknowledge that all competitive environments change over time, this raises the question of whether or not organisational capabilities and competencies can remain relevant to a new competitive landscape? Whilst investment in, and development of, resources and core competencies provide an opportunity for embedded operational routines and learning (Leonard-Barton, 1992) in high velocity environments this type of routine behaviour can also present a dilemma for organisations. On the one hand, they have to invest in and exploit their existing capabilities and competencies, whilst at the same time, they need to be mindful of the necessity to refresh and adapt their resource base in line with strategic environmental changes. Otherwise, these existing competencies could become core rigidities and barriers to change. In contrast, Danneels (2002:1097) provided a more encouraging perspective on embedded operational routines, arguing that rather than restricting the firm, existing core competencies could be successfully used to "leverage" new competencies.

Explaining superior organisational performance through the lens of dynamic capability originated in the work of Teece, Pisano and Shuen (1997:516) who argued that firms needed to renew competencies in line with changing competitive conditions and that it was "the firms ability to integrate, build, and reconfigure internal and external competencies to address changing environments" that explained variations in inter-firm performance.

The differences in the definitions of capability, core competency and dynamic capability may at first glance look like a small matter of semantics. However, closer scrutiny draws the eye to two words that suggest that dynamic capability can be differentiated from core competence and capability. The words "reconfigure" and "changing environments" in the Teece et al (1997) definition suggests that core competencies, whilst providing unique customer benefits, may in fact decay or become irrelevant due to structural changes in the competitive environment. As a consequence, they would not provide a means of sustaining competitive advantage as they decay through lack of market relevance and subsequent organisational dis-investment. This line of thinking has subsequently been supported by a number of scholars including Eisenhardt and Martin (2000) and Ambrosini and Bowman (2009).

Another focal point in literature is concerned with the idea of whether or not it is possible for organisations to reconfigure their resource base without having a dynamic capability. Winter (2003:992-3) answered this issue by arguing that organisational change can occur outside the realm of dynamic capability where unusual environmental challenges in the form of "force majeure" act as a driver for change. What differentiates these acts from dynamic capability is that the latter require "long term commitments to specialized resources" which incur higher investment costs for the organization which adapts to, and benefits from, opportunities presented by new competitive conditions. This point is illustrated in the account of how the Wall Street Journal, built dynamic capabilities for the online provision of journalism content. Steinbock (2000:184) noted that building these new capabilities required, "bold resource commitments" and "innovative responses in times of market turmoil and technological change".

Adapting firm capabilities to create dynamic capability

The bibliographic and co-citation analysis of dynamic capability research by Di Stefano, Peteraf and Verona (2010) presented several significant areas of inquiry by researchers over the past decade. Firstly, researchers have tended to focus their activities on strategic organisational change, adaptation and the transformational processes that deliver these changes. Secondly, the creation of dynamic firm capabilities requires a long term commitment to resource renewal that bears higher costs over a sustained period of time. Thirdly, that there are certain factors that enable or inhibit the development of dynamic capability, organisational renewal and adaptation. The work of Post, Berger, Eunni (2005) found significant differences in firm performance between the most and least adaptive firms in the telecommunications equipment industry. Those firms that internally aligned their strategy and resources to the external environment produced superior performance measures than those that did not align their firm to the external environment.

The factors that enable the development of a dynamic capability has been presented by numerous authors (Colapinto, 2010; Macher and Mowery, 2009; Winter, 2003; Danneels, 2002; Steinbock, 2000; Eisenhardt and Martin, 2000; Helfat, 2000; Karim and Mitchell, 2000) who have argued that this reconfiguration and refreshing of a firm's resource base can be achieved by four tangible resourced based approaches; investment in new organisational processes and routines; product innovation and development; forming strategic alliances; corporate acquisitions and mergers.

In addition, Winter (2003) argued that intangible firm resources in the shape of managerial cognition and aspiration levels created a context for these tangible resources commitments to be evaluated and ultimately acted upon. Tripsas and Gavetti (2000) illustrated this idea by suggesting that whilst a firm could invest in new organisational processes and routine, and research and development to successfully innovate new products, management could indeed fail to capitalise on this resource investment when competing in the market place.

Measuring dynamic capability

Interestingly, the review of dynamic capability literature undertaken by Di Stefano *et al* (2010) showed that strategic change, organisational adaptation, and transformational processes have been significant areas of inquiry by researchers for more than a decade. Yet the notion of measuring a firm's dynamic capability, their impact and ability to deliver superior firm performance has largely been ignored. As Lawton and Rajwani (2010:167) pointed out, researchers may have avoided this issue given that there is "difficulty in establishing causality with performance". The few studies that did seek to provide a measure of superior firm performance derived from new and dynamic firm capabilities included: Macher and Mowery (2009:41) whose empirical research of semi-conductor manufacturing found defect rates could be reduced following the introduction of new technological processes, research and development, organisation and IT practices. They argued that building these new dynamic capabilities provided evidence of "firm-specific performance differences" in the sample by way of a firm's capability in managing novelty; Miller and Shamise's (1996) longitudinal study of major U.S. film studios measured dynamic capability by using a number of performance indicators including return on sales, market share, profits and even the number of Academy Awards won; and Ahuja and Katilia's (2004) work measured dynamic capability in the form of innovative practices in US chemical firms that resulted in patent applications.

METHOD

This research used a multi-method approach. Fielding and Fielding (1986); Guba and Lincoln (1989) and Saunders et al (2000) considered this approach beneficial as it can improve the credibility and trustworthiness of findings. Kirk and Miller (1986:15) also considered the multi-method as a complimentary technique since the qualitative methodology *"identifies the presence or absence of something"*, whereas the quantitative methodology *"involves the degree to which something is present"*.

Quantitative Method: Comparative Financial Analysis

Corporate financial operating ratios provided a practice-led method to assess and measure the dynamic capability of BskyB and ITV. Firstly, by comparing corporate performance longitudinally in the form of time series to see how capabilities evolved over time (Helfat and Raubitschek, 2000) and secondly, by using cross sectional analysis, this performance could then be benchmarked against both companies in the sample. Kung (2008:90) rightly argued that the dynamic media environment "makes it hard to undertake longitudinal studies...since boundaries and definitions shift so frequently" and it is with this in mind that a rigorous and systematic approach to the data collection was used.

Ellis and Williams (1993:203) provided a useful framework to operationalise the research. They argued that Comparative Financial Analysis focuses on "an individual company, using both horizontal and vertical analysis, which facilitates the measurement of how an organization is performing when compared with its past achievements" and whether "this improvement (is) at the same rate as it's rivals". However, they also warned that when these inter-firm comparisons are attempted, researchers should ensure that companies in the sample should ensure that there is rigour in data compatibility and business context otherwise false comparisons will be made. As such, they suggested a four step approach to justify the comparison of one UK television broadcaster against another.

Step 1 – Identify the companies core activities. The aim of this research was to present analysis on the dynamic capabilities of two UK commercial television broadcasters. Yet, when considered over time, a company operating in one sector a decade ago, could conceivably end up in multiple sectors, and therefore, a wider industry definition ten years later. As such, this research focused on two companies whose primary revenue source has been derived from television broadcasting between 2000-2011. The reason being that television broadcasters, as traditional media, were a key target for adaptation and “migration” (Aris and Bughin 2009:262) to the new media environment as they had invested in new media technologies, distribution platform, markets. They do, therefore, provide a good insight into the notion of dynamic capability.

Step 2 – Compare competitors’ core activity. Both BskyB and ITV derive the majority of their corporate revenues from television broadcasting and can, therefore, be considered as direct competitors operating in the same industry.

Step 3- Do competitors pass the test of compatibility? Ellis and Williams (1993) considered compatibility in terms of the accounting framework used by competitors, which in this case is broadly similar. However, perhaps a criticism for this research is that the two companies are not compatible as they have different business models, one subscription based television broadcasting, the other, advertiser funded television broadcasting. Having said that, the researcher does not believe that differing business models have a significant effect on a media organisation’s ability to renew their resource base. Also, as ITV only came into existence in 2004, so there are four years (2000-03) were there is no comparative data.

Step 4- Do competitors pass the test of business context? This requirement ensures that companies predominantly operate in similar product markets, that is, within UK television broadcasting. Again both BskyB and ITV satisfy this requirement. Ellis and Williams (1993:208) readily acknowledge that “this approach to inter-firm comparisons is undoubtedly judgemental” but argue that it is none the less an attempt to make the selection of companies in sample frame as rigorous as possible.

Units of Analysis

Bitar and Hafsi (2007:404) argued that capability and performance analysis was like a “black box” of speculation and yet there has been research that has linked and measured capabilities and firm performance. These included: Miller and Shamise (1996) use financial ratios, revenues, profits and Academy Awards for US film studios; Ahuja and Katilia’s (2004) work on the patenting activities of global US based chemical firms; and Macher and Mowery’s (2009) investigation into the introduction of new process technologies in semi-conductor manufacturing. This research, however, measured superior performance in terms of financial operating ratios. Return on Capital Employed (ROCE) was used as an overall measure of corporate performance as it reflects the assets used by the company to generate profit. ROCE measures the return on an organisation’s total assets. One criticism of this measure is that corporate assets are liable to depreciation, so as they devalue, the ROCE will rise even though operating profits may remain at the same level. One further problem with this ratio is that it can be defined in many ways. For example, the phrase 'capital employed' can be a calculation of: fixed assets plus current assets, less current liabilities; or, share capital plus reserves, plus borrowing which may include lease obligations, bank loans, overdraft, interest, provisions, associates and investments. This research employed the use of the term capital employed as being total assets (fixed and current) as it was felt to be a more appropriate measure of firm assets. ROCE was therefore calculated as: Operating Profit/Total Assets X 100.

Net Profit margin (NPM) which measures the percentage profit of each £ of turnover after direct and indirect expenses have been deducted. Inter-firm comparisons of this ratio are likely to reveal a number of strategic management issues like: the way they compete in the market place; their pricing strategy, and their ability to manage costs. Net Profit Margin was calculated as: Operating Profit/Turnover x 100.

Asset Turnover (AT) is a measure of how efficiently a business uses their assets to generate sales revenue. A high AT figure indicates that the firm is generating a high level of sales from its resource base, although a note of caution should be made. High AT figures can also be an indicator of 'overtrading' where sales volumes are too high to be sustained from an existing resource base. Equally, a low AT figure is a good indication that the company may not be reaching the level of sales that it should be from its resource base. The Asset Turnover ratio was calculated as: Turnover/Total Assets.

Qualitative Method: Content Analysis

This research followed the example of Miller and Shamise (1996) who used company Annual Reports, including the statements made by the respective Chairmen and Chief Executive Officers. These were used in order to understand and assess how these organisations had adapted to new competitive conditions. Helfat (2000:958) argued that the identification of dynamic capabilities in fast moving markets, like the media, could be difficult to identify as they tended to be "less structured and less complex".

In terms of this research, the review of literature provided a list of sampling units for selective inclusion in the content analysis (Krippendorff, 2004:99). These included; Aspirational statements made by the Chairman/CEO (Winter, 2003); Managerial Cognition (Tripsas and Gavetti, 2000); R&D costs (Helfat and Raubitschek, 2000, Steinbock, 2000, Macher and Mowery, 2009); An indication of product development (Helfat and Raubitschek, 2000), Steinbock, 2000, Winter, 2003, Danneels, 2002, Eisenhardt and Martin, 2000); Significant Investment in people, and or, processes (Zollo and Winter, 2002, Winter, 2003); Acquisition of other companies for their capabilities (Eisenhardt and Martin, 2000, Winter, 2003, Colapinto, 2010).

RESULTS

The content analysis of each company's Annual Report and Accounts revealed a number of interesting media management issues, using the variables previously listed.
Aspirational statements made by the Chairman/CEO

By their very nature, corporate Annual Accounts tend to act as a vehicle to for a positive interpretation of firm performance in trading conditions. At the start of the new millennium, BskyB Chairman Rupert Murdoch set an aspirational tone for the company as it entered the dawn of the new media environment. He said that the company were;

"changing the way people watch TV and the way we communicate, empowering consumers with tomorrow's technology today" and that they will *"anticipate what consumers want and how they want to access it"*
Rupert Murdoch, Chairman, BskyB (2000:1)

With a record breaking 21% increase in subscribers to 3.6 million in 2000, BskyB were not content to rest on their success and continued to set ambitious subscriber figures of 7m by 2003 and in 2004 set a target of 10m subscribers by 2010. Their ambition of *"sky in every home"* (Murdoch, R, 2003:1) would seem to be an aspiration too far. However, they continued to achieve their subscriber targets ahead of schedule and argued in 2005 that the pay-tv sector penetration in the UK and Ireland was only 44% and in the *"long term penetration levels can increase to around 80%"* (Murdoch, J, 2005:3).

The statements made by three successive BskyB Chief Executive Officers for more than a decade are testament to a risk taking corporate culture that sees opportunity in the seismic challenges presented by the new media environment. The words, *risk taking, opportunity, adaptable* and *invest* act like beacons of confidence in successive annual reports. These aspirations are illustrated in the following statements;

"Sky therefore seeks to invest and adapt in order to remain competitive."
Rupert Murdoch, CEO, BskyB (2003:3)

"This has been a year of significant changes- not just for Sky, but for the entire industry. Throughout the year, our focus has been on setting the pace of change, and re-affirming our appetite for doing so."
James Murdoch, CEO, BskyB (2006:4)

"We challenge ourselves constantly to be a business that is adaptable and embraces change."
Jeremy Darroch, CEO, BskyB (2008:4)

The various leaders of ITV on the other hand, have tended to provide statements that are more pragmatic an insular rather than being aspirational. Following the merger of Carlton and Granada to create ITV in 2004, the Chairman and Chief Executive Officer statements tended to focus on two areas; making the business more efficient and developing new revenue streams for the company;

"Our actions have been based on achieving a number of the goals...these included increasing efficiency, reducing regulatory costs and placing news at the centre of ITV's public service programming".
Sir Peter Burt, Chairman, ITV (2004:1)

"We have continued with our programme of developing our business and changing our operations to enable us to take advantage of the rapidly evolving digital television world. In early 2006 we re-branded our operations, from a fresh new look onscreen for our channels through to new signage and logo for our ITV production business".
Charles Allen, CEO, ITV (2005:19)

The introduction of Michael Grade as Executive Chairman in 2006 did not change the tone of these less than aspirational statements. He greeted stakeholders not with a rallying call to action, but;

"Having been in post for two months it is too soon to conclude

definitive plans for the business, but generally I have developed more positive impressions than negative ones, and the latter are mostly within our control to remedy".
Michael Grade, Executive Chairman, ITV (2006:1)

In 2009 and 2010 ITV were still looking for a glimmer of light in their Turnaround Strategy. Their reports and accounts for these years were entitled *"Platform for change"* and *"Transforming ITV"* and introduced another new management team. The new Chairman and Chief Executive Officer were placed at the helm of a company to find a new strategic direction in a media landscape characterised by change. Once again, the statements tended to be cautious and low key;

"There is a shared recognition that the business will need to change substantially going forward if we are to return to sustained growth."
Archie Norman, Chairman, ITV (2009:3)

"We require clarity of vision and a clear road map for change. Transformation requires a sense of 'time and place' because it is vital that everyone at ITV knows what is required of them and where we are in the journey".
Archie Norman, Chairman, ITV (2010:2)

Managerial Cognition

Tripsas and Gavetti (2000) and Winter (2003) argued that the cognitive ability of managers to seek out, take advantage and capitalise on market opportunities can be regarded as an intangible resource that could deliver superior firm performance. Over the decade, the management of BskyB had made various strategic decisions that in the main appeared to be successful. These included formulating strategy and navigating an uncertain media environment, making resource investment decisions, developing new products and making corporate acquisitions and divestments. These variables will be explored in more detail later, but how the management of BskyB and ITV have viewed the competitive environment is interesting. On the one hand BskyB have invested heavily in new capabilities, made corporate acquisitions and have been robust their views on the accrued losses of £55m in British Interactive Broadcasting Limited and £11m in KirchPay TV in 2000. This corporate optimism is also reflected in their statement on the global economic crisis of 2008;

"In a dynamic market place, it is the work of the business to continue to adapt and refresh itself...over the years Sky has reintroduced itself, reinvented itself and revitalised its appeal."
Rupert Murdoch, CEO, BskyB (2005:1)

"These changes are creating significant opportunities for companies that have the capability and appetite to adapt their businesses."
James Murdoch, CEO, BskyB (2008:2)

In 2007, ITV stated that their Turnaround Strategy would involve making the transition to digital media markets. This strategy, however, appeared inconsistent on two counts. Firstly, their new corporate vision did not include any reference to a new media world;

"Our vision is for ITV to be the UK's favourite source of free entertainment."
Michael Grade, Executive Chairman, ITV (2007:2)

Secondly, the wholesale recruitment of a new executive management team included a wealth of accumulated experience in television broadcasting, marketing and production. Yet, these appointments, on the face of it, there appeared to be an obvious error as this new team did not include executives with new media experience;

"The ITV Senior Executive team was considerably strengthened in 2007. In Global Content, we recruited Dawn Airey, latterly of Sky and five. Rupert Howell, a major figure from the advertising sector, joined us in the crucial post of Managing Director of ITV Brand and Commercial. Carolyn Fairbairn, formerly of the BBC and McKinsey, leads our strategy and development function. Entering 2008, we have confirmed that Peter Fincham, the controller of BBC1 until October 2007, will join ITV as Director of Television".

Michael Grade, Executive Chairman, ITV (2007:2)

A decade after the advent of the new media environment, ITV acknowledge that they had not acted quickly enough to address the challenges, threats and opportunities presented by a changing market place. This lack of managerial cognition was acknowledged by the new CEO in his 2010 statement to shareholders;

"Adapting to this new media environment requires urgent change to ITV's strategy, management, culture and organisation. We have started to address the challenges we face but there are no quick fixes".

Adam Crozier, Chief Executive, ITV(2010:5)

In an attempt to address these challenges, and previous under performance, ITV stated that;

"About half of our leadership group has changed"

Archie Norman, Chairman, ITV (2011:2)

An indication of product development

Many researchers including Helfat and Raubitschek (2000), Winter (2003), Danneels (2002) and Eisenhardt and Martin (2000) have argued product develop is an important characteristic of dynamic capability and that for this to be successful, "bold resource commitments" (Steinbock, 2000:184) needed to be committed over the long term. Again, we see contrasting fortunes in both broadcasters. BskyB have transformed themselves from being one of the UKs leading television broadcasters into a multi-platform, multi-product entertainment and communications business that has been described as resulting in;

"...a step change in our capabilities..."

Jeremy Darroch, CEO, BskyB (2007:3)

In a decade BskyB have innovated numerous products including: Sky Active services incorporating shopping and betting on certain broadcast channels, interactive features on Sky Sports and Sky News, distribution of news and sports content on the Orange mobile phone network (2000); the UKs first personal television recorder in Sky+, the Sky Guide advanced electronic programme guide (2001); Sky Multiroom subscription, and an enhanced version of Sky+ (2004); Sky Gnome the portable device to listen to audio content (2005); Sky HDTV, Sky Broadband and Sky Talk, Sky+ access from customer mobile phones (2006); Sky Anytime an on-demand service (2007); Sky 3D television (2010) and Sky Go (2011).

ITV on the otherhand, has been led by a Content Strategy and has regarded innovation and new products and services as being programme and scheduling based. Again, this approach looks limited, insular and inhibiting as far as dynamic capability is concerned. As a content led company, one of the challenges they face relates to the path dependency argument of Jarzabkowski (2004) in so far as the recursive nature of ITV's aim to invest in *"established and returnable drama and entertainment series that can be sold internationally"* means that they are less likely to invest in innovative programming. They acknowledged this argument in 2006, stating;

"There is a lack of innovation in our programming, partly resulting from a fear of ratings".
Michael Grade, Executive Chairman, ITV (2006:1)

This is further backed up by their 2007 statement where they regarded the launch of their new ITV1 schedule as a *"commitment to innovation"*. There is no doubt that ITV have invested billions of pounds in programming from in-house, external and independent producers, as well as in content acquired from US distributors. But how much of this investment in programming can be regarded as new and innovative? In 2010 Adam Crozier was critical of the company's lack of an innovative edge and stated in his report to shareholders that;

"ITV Studios' creative content pipeline had depleted over time with no major new entertainment programme format created since 2006".
Adam Crozier, Chief Executive, ITV (2010:5)

However, by 2010, ITV had started to adapt to the new media environment and launched a number of new initiatives including: pay television with their digital channels ITV2, 3, 4 and HD; the launch of ITV Player on the PS3, Freesat and YouView.

R&D costs

Studies by Helfat and Raubitschek (2000); Steinbock (2000); and Macher and Mowery (2009) argues the creation of dynamic firm capabilities require a long term commitment to resource renewal that bear higher costs over a sustained period of time. However, one of the problems with using Annual Reports and Accounts is that these costs are not easily recognisable and are often obscured from obvious view. This has, therefore, made financial analysis of this variable difficult. Certainly the annual reports contain statements like;

"Opportunities for companies to acquire true market leadership are rare, and BskyB are uniquely placed to achieve this on the back of our investment in hardware, programmes and technologies."
Rupert Murdoch, Chairman. BskyB (2000:7)

"Our digital channels are the most successful free to air commercial family of digital channels in the UK, each with distinctive branding and programming. We must ensure that they have the investment they need to grow their leading market position".
Michael Grade, Executive Chairman, ITV (2006:1)

Significant Investment in people, and or, processes

Zollo and Winter (2002) and Winter (2003) reported that this type of investment was a good platform on which to build a dynamic capability through the reconfiguration of firm resources. Once again, the Annual Reports did not make accessing this type of information accessible or consistent over time. There were some statements, however, that did indicate this type of activity;

"We continue to invest consistently in the capital expenditure required to support our growth strategies...this included £341m invested in core services; information system infrastructure; broadcast infrastructure, broadband and telephony infrastructure, new product development...and customer service improvements. In addition, £114m was invested in new property and property improvements"
BskyB Directors Report (2010:15)

"We have invested more than 50% of our total revenues in programming, with the majority of this investment focused on ITV's unique selling point, original UK production".
Michael Grade, Executive Chairman. ITV (2008:2)

Acquisition of other companies for their capabilities

The renewal and reconfiguration of firm capabilities and competencies may be achieved through two means, organic resource investment or the acquisition of another organisations capabilities (Colapinto, 2010; Macher and Mowery, 2009; Winter, 2003; Danneels, 2002; Steinbock, 2000; Eisenhardt and Martin, 2000; Helfat, 2000; Karim and Mitchell, 2000).

Over the time period of data collection, BskyB have made investments in numerous joint ventures. As part of their corporate strategy in the early 2000s they made significant resource investments and joint ventures agreements (£1,512m in 2000 and £1,163m in 2001) in interactive services, customer relationship management and interactive broadcasting services. They recognised an opportunity for leadership in the pay-tv market noting that;

"We are now moving decisively into new media through organic development and acquisitions, partnerships and joint ventures".
Rupert Murdoch, Chairman BSkyB, (2000:7)

Between 2002-07 BskyB consolidated their earlier investment spending, with relatively small investments in the range of £22-£34m per annum. After 2007, this figure was not reported in their annual accounts.

ITV made a number of small global content production based acquisitions up until 2008, but the faltering advertising market and declining profits had reduced their ambitions. They focused on working in partnership with other UK broadcasters, for example, launching Freesat with the BBC, which included a high definition ITV service; and partnering with the BBC and BT to deliver itv.com and online video services.

Comparative Financial Analysis of Operating Ratios

The qualitative content analysis has presented insight into how BskyB and ITV addressed the challenges of the new media environment and the renewal of their resources and capabilities. This leads us on to a central tenet of dynamic capability theory, that is, that these new capabilities deliver superior firm performance. This research measured superior performance in terms Operating Ratios in the form of; *Return on Capital Employed* as an overall measure of corporate performance as it reflects the assets used by the company to generate profit. *Asset Turnover* as a measure of how many times a company's total assets have been turned over in terms of sale. *Net Profit Margin* which measures the percentage profit of each £ of turnover after direct and indirect expenses have been deducted.

Financial Ratio Analysis

Return on Capital Employed (ROCE) as an overall measure of corporate performance reflects the assets used by the company to generate profit. The ROCE for BskyB indicates an impressive and superior performance in leveraging their assets over a sustained period of time. The peak in 2005, is explained by a lack of any significant investment in corporate acquisitions and joint ventures, whilst at the same time, managing to achieve a decrease in a number of operating expenses in the form of programming costs, down £75m, as a result of re-negotiating sports contracts; and a reduction in movie costs down by £37m. Overall operating profit subsequently increased by 35% to £805m. Since 2005 BSkyB have managed to sustain impressive ROCE figures.

Perhaps the most striking figure in this analysis is the return posted by ITV in 2008. Here, a fall in their advertising revenues as a result of the global economic down turn had left them exposed in terms of their *"high operational gearing, which means that any reduction in revenues has a significant impact on profits"* (Michael Grade, Executive Chairman, ITV, 2008:2). The company also suffered an impairment charge of £2,638m as a result of their intangible assets being re-valued from £3,873m in 2007 down to £1,140m the following year. This was mainly the result of a calculation of goodwill being written down on their broadcasting, GMTV and Online businesses as a result of the economic downturn and outlook for growth in the TV advertising market. However, it is fair to say that ITV have improved their efficiency, mainly in programming spend, and this has delivered annual increases between 2009-11.

Table 1: Return on Capital Employed

ROCE (%)	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
BskyB	-0.63	2.39	2.50	12.54	20.35	30.26	23.24	20.79	17.74	17.79	22.81	20.04
ITV	n/a	n/a	n/a	n/a	3.18	5.46	4.32	3.36	-81.42	6.42	11.70	13.83

Net Profit margin (NPM) which measures the percentage profit of each £ of turnover after direct and indirect expenses have been deducted. Inter-firm comparisons of this ratio revealed that BskyB has consistently out performed it's rival. The downturn in total advertising market spend, as a result of the global economic recession, significantly affected ITV's performance in 2008. Yet, ITV have managed costs and grown revenues since then and have returned increasingly respectable net profit margin figures in the following three years.

Table 2: Net Profit Margin

NPM (%)	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
BskyB	-1.07	4.02	1.98	7.97	13.16	17.34	21.14	17.91	14.62	15.17	18.54	16.26
ITV	n/a	n/a	n/a	n/a	8.62	14.98	12.10	9.22	-130.46	10.43	17.64	18.87

Asset Turnover (AT) is a measure of how efficiently a business uses their assets to generate sales revenue. A high AT figure indicates that the firm is generating a high level of sales from its resource base, although a note of caution should be made. High AT figures can also be an indicator of ‘overtrading’ and that sales are too big to be sustained from its existing resource base. Equally, a low AT figure is a good indication that the company not reaching the level of sales that it should be from its resource base.

Whilst BskyB returns have been consistent over the past decade, ITV has become more efficient in the use of their assets as a result of their three-year cost reduction programme (2005-2008). This resulted in costs savings of £41 million per annum during that period and was followed up in 2009 when they delivered around £40 million in savings from regional services and £120 million in non-programming costs between 2009-10. ITV’s continued focus on revenue generation and cost reduction has certainly delivered a more efficient business in terms of assets generating sales revenue.

Table 3: Asset Turnover

Asset Turnover	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
BskyB	0.59	0.59	1.26	1.57	1.55	1.74	1.10	1.16	1.21	1.17	1.23	1.23
ITV	n/a	n/a	n/a	n/a	0.37	0.36	0.36	0.36	0.62	0.62	0.66	0.73

DISCUSSION

This research illustrates how two UK television broadcasters have managed their businesses in the same competitive media environment, but in very different ways, with different outcomes and performance effects. BskyB have adapted their business over the past decade, from being a television broadcaster to becoming a multi-platform, multi-product media firm. This successful reconfiguring of their resources and adaption of capabilities has been driven by: seeking opportunities in a changing media landscape, setting ambitious corporate objectives, taking risks, investing in R&D and corporate acquisitions that renew, refresh and leverage new capabilities and competencies in a way that has delivered new products and services to consumers. Their corporate mantra of *“invest and adapt”* has resulted in a step change in their business that has delivered superior financial corporate performance in a relatively short timescale. Quite simply, BskyB have satisfied all the criteria for an assessment of dynamic capability.

ITV on the otherhand have not adapted to the new media environment at the same pace. Their 2010 Annual report is entitled *“Transforming ITV”* and appeared a decade after the advent of the new media environment, and this statement alone is a good indication of a company struggling to adapt. They have not reconfigured and renewed their resource base to the same extent as BskyB, although they have reduced their previously cumbersome and lethargic total asset base by 44% over the past 7 years to become a far leaner business. Their corporate aspirations have lacked direction. They haven't been innovative, nor delivered superior financial performance, and as such, their response to the new media environment can be considered as a 'dynamic incapability'. There is no doubt that ITV are trying to make up for lost ground following the merger of 2004, and their biggest strategic challenge is to convince themselves and their stakeholders that they are not managing a business in decline.

Having read a sequence of annual reports and accounts for both companies, one cannot help but conclude that the fortunes of both companies have differed for a number of reasons. It would be an obvious conclusion to state that the differing business models have had a role to play. But it is striking to note that BskyB refer to their customers as their subscribers, whereas ITV refer to their customers mostly as their advertisers. In this sense, ITV may not be meeting the needs and wants of their audiences, which is a dangerous game to play. Another conclusion may be that ITV are battling the path dependency of a mature business operating in a mature industry, with the same business model and a focused content-led strategy. As such, they have not responded to a new media landscape characterised by: digital and pay TV, audience fragmentation, video on demand, mobile content, and advertising revenues slowly migrating toward online audiences.

CONCLUSIONS

This research has explored how UK television broadcasters have adapted to the challenges of the new media environment. We can conclude from this analysis and discussion that Dynamic Capability Theory does indeed provide media management researchers with a useful lens through which to examine media organisation adaptation. This paper has not set out to develop this theory, but to understand how theory can help us to better understand media practice. The research also sought to find a reliable measure of superior firm performance that indicates dynamic capability. As academics we often look for complicated solutions and intricate designs in our research methodology, when sometimes a simple solution would suffice. This paper concludes by arguing that Financial Operating Ratios can be considered as a reliable measure of superior firm performance that is indicative of dynamic capability. However, a criticism of using these ratios are that they tend to favour research into large corporations who are able, and have, to present financial data to various stakeholders and compliance bodies. An area of further research would be for researchers to identity dynamic capability in micro and small companies where financial operating ratio analysis would not be possible, simply because they do not have the resource or expertise to collect this type of data.

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