



**THE CONTRIBUTION OF THE BBC'S  
CORE RADIO SERVICES TO THE  
OVERALL UK RADIO MARKET TO  
2014**

**A REPORT FOR THE BBC'S SUBMISSION  
TO THE INDEPENDENT REVIEW OF THE  
BBC (THE BURNS COMMITTEE)**

**BY OLIVER & OHLBAUM ASSOCIATES**

**OCTOBER 2004**



Oliver & Ohlbaum Associates Ltd  
105 Ladbroke Grove  
London W11 1PG  
Tel: 0207 616 8484  
Fax: 0207 616 8485  
[www.oando.co.uk](http://www.oando.co.uk)

## **THE CONTRIBUTION OF THE BBC'S CORE RADIO SERVICES <sup>1</sup> TO THE OVERALL UK RADIO MARKET TO 2014**

### **A REPORT FOR THE BBC'S SUBMISSION TO THE INDEPENDENT REVIEW OF THE BBC (THE BURNS COMMITTEE)**

**BY OLIVER & OHLBAUM ASSOCIATES**

**OCTOBER 2004**

#### **INTRODUCTION AND METHODOLOGY**

Oliver & Ohlbaum has been commissioned by the BBC to assess the market impact of its core analogue radio services (which are also simulcast in digital) for a submission to the Independent Review of the BBC (the Burns Committee) which is studying the future role, purposes and funding of the BBC as part of the Charter Review process.

The approach taken to this market impact study is broadly similar to that taken in O&O's reports on the impact of the BBC's digital only radio services, submitted to the DCMS in March 2004. However, we have also taken into account comments on general market impact methodology contained in the Graf Review of BBC Online (and subsequently adopted by Ofcom in its analysis for the Barwise and Gardam Reviews of the BBC's digital TV and radio services), which suggested looking at the broad impact of the BBC on the competitive dynamics and outcomes of the commercial market as well as any specific direct revenue and cost effects on individual commercial services.

To conduct our analysis we have drawn upon RAJAR audience data, surveys of BBC and commercial radio play lists commissioned by the BBC from an independent research company - Intelligent Media - and Digital Radio Development Bureau (DRDB) data on likely DAB take-up.

---

<sup>1</sup> These are the BBC's UK networks ( Radio 1, Radio 2, Radio 3, Radio 4, Radio 5 Live), BBC local radio 48 stations in England, the BBC's English language services for the Nations (Radio Scotland, Radio Wales, Radio Ulster/Radio Foyle) and the BBC's autochthonous services for the Nations (Radio n Gael and Radio Cymru). These will be referred to throughout this report as - the BBC "networks", BBC "English local" radio, BBC "National" radio and BBC "National Language" services respectively.

We have conducted our analysis in two parts.

**Part A** reviews the structure and economics of the current commercial radio market today and the likely evolution of the commercial market – analogue and digital – over the next 10 years given the BBC's current service output.

**Part B** provides an assessment of the contribution of the BBC's core services to the overall radio market offering in the UK and the market impact of these services.

This assessment is done both on a service by service basis, and then for the portfolio as a whole. The assessment for each service in turn covers:

- the current performance and distinctiveness of each BBC service;

- the indicative direct revenue and cost impact each BBC service has on the commercial market; and,

- the general impact each BBC service is likely to have on the overall commercial market offering and equilibrium.

The assessment of the overall BBC portfolio not only covers the overall distinctiveness of the BBC services combined, the likely overall impact on revenues and costs of the commercial sector, and the overall impact on the competitive market equilibrium, but also assesses the broader contribution BBC services make to the wider cultural and creative sectors of the UK and their overall impact on digital take up.

The net result of all this analysis is then summarized in an overall scorecard that provides a summary of the contribution and impact of each BBC service using all the criteria outlined above. For each service it assesses the degree to which it:

- takes audience and revenue away from the commercial market;

- inflates the costs of the commercial sector as a whole, or specific competitors;

- substantially changes the overall offering and dynamics of the commercial sector and the migration to digital;

- adds to the range, diversity and quality of the UK radio sector; and,

- adds significantly to broader cultural markets and the creative industries.

We have assessed the impact of the BBC services both at a national aggregated level and at a local/regional market level. When analyzing impact at a local/regional level we have taken a sample of seven local markets that between them reflect the range of choice facing different types of listener across the UK – they are: London, Central Scotland, Birmingham, Newcastle, Cumbria, Leicester and Southampton.

In assessing the direct impact on revenue and costs of the commercial market we have only been able to provide broadly indicative figures for two reasons. First, there is a general lack of authoritative research on the elasticity of demand for radio advertising (i.e. how much price and revenue respond to changes in overall commercial listening). Second, even if more thorough research existed on current radio market advertising elasticity, its

applicability to the very large scale changes in commercial listening that might result from the absence of a current BBC core radio service would still be the subject of a large degree of doubt.

# CONTENTS

## PART A: THE UK COMMERCIAL RADIO MARKET TO 2014

<b>SUMMARY</b>	<b>7</b>
<b>1. The UK Radio Market to Date</b>	<b>10</b>
a. General Background and Context	
b. Competition Regulation, Market Structure and Ownership in Commercial Radio	
c. The Radio Advertising Market	
<b>2. The Commercial Radio Sector's Likely Evolution to 2014</b>	<b>24</b>
a. The Growth of Digital	
b. The Evolving Regulatory Environment	
c. Likely Commercial Sector Share, Revenue and Segmentation	
d. Likely Competitive Dynamics and Structural Changes	

## PART B: THE BBC'S CONTRIBUTION TO, AND IMPACT UPON, THE UK RADIO MARKET TO 2014

<b>SUMMARY</b>	<b>34</b>
<b>1. The Current Performance and Distinctiveness of BBC Services and the Implications Of Commercial Market Developments to 2014</b>	<b>37</b>
a. Performance and Distinctiveness	
b. Likely Implications of Commercial Market Developments to 2014	
<b>2. The Framework for Assessing the Contribution and Market Impact of BBC Services</b>	<b>41</b>
a. The Service-by-Service Review	
b. The Broad Impact Review	

<b>3. Contribution and Impact by Service</b>	<b>43</b>
<b>a. Radio 1</b>	<b>43</b>
i. Performance and Distinctiveness	
ii. Indicative Direct Revenue and Cost Impact	
iii. General Impact on the Commercial Market Equilibrium	
<b>b. Radio 2</b>	<b>47</b>
i. Performance and Distinctiveness	
ii. Indicative Direct Revenue and Cost Impact	
iii. General Impact on the Commercial Market Equilibrium	
<b>c. Radio 3</b>	<b>52</b>
i. Performance and Distinctiveness	
ii. Indicative Direct Revenue and Cost Impact	
iii. General Impact on the Commercial Market Equilibrium	
<b>d. Radio 4</b>	<b>54</b>
i. Performance and Distinctiveness	
ii. Indicative Direct Revenue and Cost Impact	
iii. General Impact on the Commercial Market Equilibrium	
<b>e. Radio Five Live</b>	<b>56</b>
i. Performance and Distinctiveness	
ii. Indicative Direct Revenue and Cost Impact	
iii. General Impact on the Commercial Market Equilibrium	
<b>f. BBC English Local Radio</b>	<b>59</b>
i. Performance and Distinctiveness	
ii. Indicative Direct Revenue and Cost Impact	

iii.	General Impact on the Commercial Market Equilibrium	
g.	National Radio Services for Scotland, Wales and Northern Ireland	61
i.	Performance and Distinctiveness	
ii.	Indicative Direct Revenue and Cost Impact	
iii.	General Impact on the Commercial Market Equilibrium to 2014	
4.	BROAD IMPACT OF THE BBC PORTFOLIO	64
a.	Overall Indicative Direct Revenue and Cost Impact	
b.	General Impact on the Commercial Market Equilibrium to 2014	
c.	The Overall Impact on the Radio Market and Listeners	
d.	Impact on Broader Cultural and Creative Activities	
e.	Impact on Digital Take Up	
5.	THE OVERALL SCORECARD	68

## **PART A: THE UK COMMERCIAL RADIO MARKET TO 2012**

### **SUMMARY**

#### **THE UK COMMERCIAL MARKET IN 2004**

- **The UK's commercial radio market currently concentrates on offering a range of targeted music based services to the 15 to 45 year old listening market – and within that primarily to the 20 to 40 year age group.**
- **The commercial analogue radio sector is made up of over 250 local and regional radio stations across the UK, and three national stations. The average UK listener has access to 8 analogue commercial radio stations over terrestrial airwaves – the three national services and five local and regional services.**
- **Analogue commercial station choice varies significantly across the UK, with listeners in London and Home Counties able to receive over 20 commercial stations, but those in rural and more remote towns only able to receive 3 or 4 commercial services.**
- **UK commercial radio spends just over £150m of its £560m annual income on new programming (excluding music royalties) – about £125 per hour broadcast – and makes profit margins of about 20 per cent.**
- **The sector is still dominated by the “heritage”<sup>2</sup> 2LR FM analogue local services that account for about 35 per cent of the commercial audience and about 55 per cent of the available revenue.**
- **The three national commercial services which were licensed between 1992 and 1995 together account for about 20 per cent of the commercial audience but just 12 per cent of advertising revenue.**
- **Of the remaining commercial listening about 45 per cent is split between an average of 4 to 5 narrowly targeted local and regional analogue services per local/regional market. Commercial new digital services currently only account for about 4 per cent of commercial listening.**
- **Speech only analogue commercial radio services are limited to TalkSport nationally and LBC in London. Regional speech/music mix stations currently cover about 35 per cent of the UK population. Most local music based stations do carry local news, travel and events information, as well as national news – on average this accounts for slightly less than 10 per cent of their weekly output.**
- **Audiences over 55 currently sell at about an 80 per cent discount to average commercial radio advertising prices.**

---

<sup>2</sup> These were the stations that existed before 1989 – up until that year they were the only commercial FM services available in most markets ( the exception being London where a speech station LBC was also available).

- While there is no comprehensive assessment of the elasticity of demand for UK radio advertising, the work and reviews that have been conducted – notably for various Competition Commission inquiries and submissions - suggests that elasticity is likely to be about -2 (i.e. for every 10 per cent increase in the quantity of advertising impacts, price falls by 5 per cent and, therefore, revenue only increases by 5 per cent). However, this elasticity estimate is based on relatively small changes in commercial audience and/or price rather than large scale structural changes.
- It is likely that the elasticity of demand from local advertisers and broad national advertisers (“fmcg” brands etc) is lower than -2, while elasticity of demand from targeted national advertisers is higher.

#### THE UK RADIO MARKET TO 2014

- While new analogue commercial station licensing draws to a close over the next 2 years leaving the average UK listener with a choice of about 9 commercial services (3 national, 6 local), DAB digital terrestrial radio will increase effective choice of commercial services to those with the necessary receiving equipment and in a reception area to at least 21 services.<sup>3</sup>
- Commercial radio will move from a situation where it has only half the available analogue FM capacity to one where it has at least two thirds of the DAB capacity. The greatest planned expansion in services is in pop, rock, adult contemporary and easy listening services.
- Digital radio can also be received via the internet and digital TV platforms – although the latter does not yet allow for portable or in car reception. Digital satellite offers over 100 services and digital radio on satellite, cable and Freeview is already accessed regularly by about 18 per cent of UK households.
- Commercial radio is already taking 80 per cent of the listening to new digital services, and growth in digital radio reception – forecast to reach nearly 70 per cent of households by 2014 – should help commercial radio increase its share towards 60 per cent expanding its demographic focus to the 10 to 20 age group and the 35 to 50 age group – with some limited outreach to the over 50s.
- But commercial radio is still likely to under serve the over 50s, and to under provide the more expensive forms of speech and live music radio – indeed revenue fragmentation is likely to increase commercial pressures on individual commercial services with the average number of services per person increasing 2.5 to 3 times, but revenue probably only doubling to 2014 in real terms.
- The commercial radio DAB proposition beyond the five new national services on the Digital One multiplex is likely to develop through the creation of a series of quasi-national music led brands, gaining reach across the UK through access to

---

<sup>3</sup> Ofcom is currently reviewing the use of extra Band III and L Band capacity which can be used both to extend the effective reach of national and local DAB services across the UK and potentially introduce a new national digital multiplex – which could potentially take the average number of commercial channels across the UK – including simulcast - to 29 or 30.

**both local analogue and local/regional digital terrestrial frequency and at the same time being available on digital TV, internet and mobile telecoms platforms.**

- **Extensive local programming on these new digital services is likely to be limited, while the increased fragmentation of commercial advertising revenue also puts existing investment in local programming by traditional heritage ILR FM services under pressure.**

## 1. The UK Radio Market To Date

Set out below is an outline of the main recent trends in UK radio. The main aim of this section is to provide an understanding of the current economics of UK commercial radio, the sustainability and objectives of its digital proposition and the macro level factors affecting growth and profitability over the last few years so as to better isolate the likely specific impact of BBC services on the market. The section also provides a general assessment of the BBC's current contribution to the whole sector

The section covers four areas:

- general background on the size, growth and flow of funds through the commercial sectors' supply chain;

- an overview of the competitive structure of the UK radio market and the BBC's current role within it;

- an analysis of the UK radio advertising market and in particular how far revenue is related to changes in commercial audience share; and,

- an assessment of the current economics of digital radio.

### a. General Background and Context

***Radio is an expanding medium with average listening per head rising 10 per cent over the last 5 years***

Radio listening in the UK has expanded over the last 10 years while TV watching has stagnated. This growth has probably been fuelled by both an increasing range of services available - outlined in more detail below - and the general suitability of the medium to people's increasingly busy lives. Research suggests that people often listen to the radio while doing other things, and, of course, when travelling and commuting.

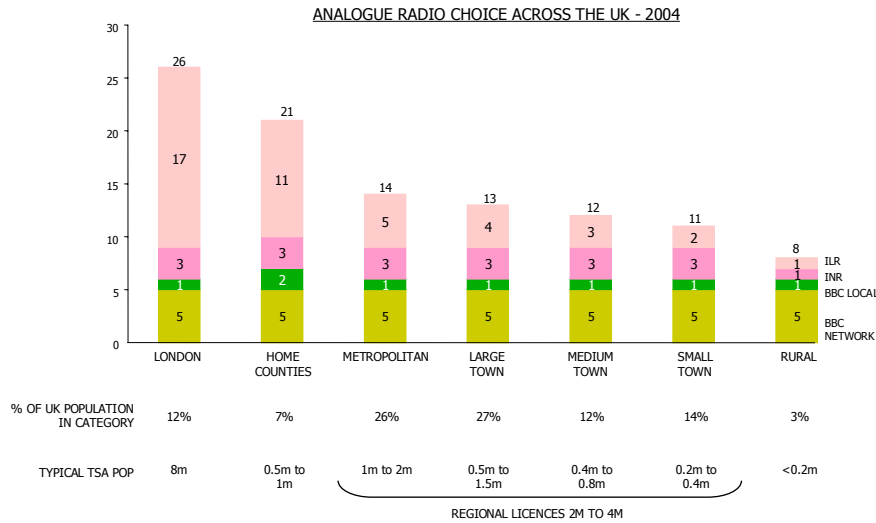
***UK Radio is a £1 billion sector bringing the average listener in the UK almost 15 analogue services – but this ranges from 26 services in London to just 7 or 8 in outlying areas***

UK radio broadcasting is a £1 billion sector, obtaining just over half its revenue from advertising and sponsorship and just under half through the BBC licence fee<sup>4</sup>. The number of analogue stations received varies across the country, with most individuals able to receive five national and one local BBC service and 3 national commercial services, but the number of local and regional commercial services ranges from only one in some rural areas to 18 in London and a similar number in the Home Counties. (See Exhibit 1).

---

<sup>4</sup> O&O has estimated that about £480m of licence fee income goes to radio services. There is no separate radio figure in the BBC's accounts. We have calculated this figure by calculating the proportion of all programme spending by the BBC accounted for by BBC radio services (at £345m this represents about 17 per cent of programme spending) and applying this to the BBC's total licence fee income of £2.8 billion.

**EXHIBIT 1**



Sources: OFCOM, RAJAR, O&O Analysis

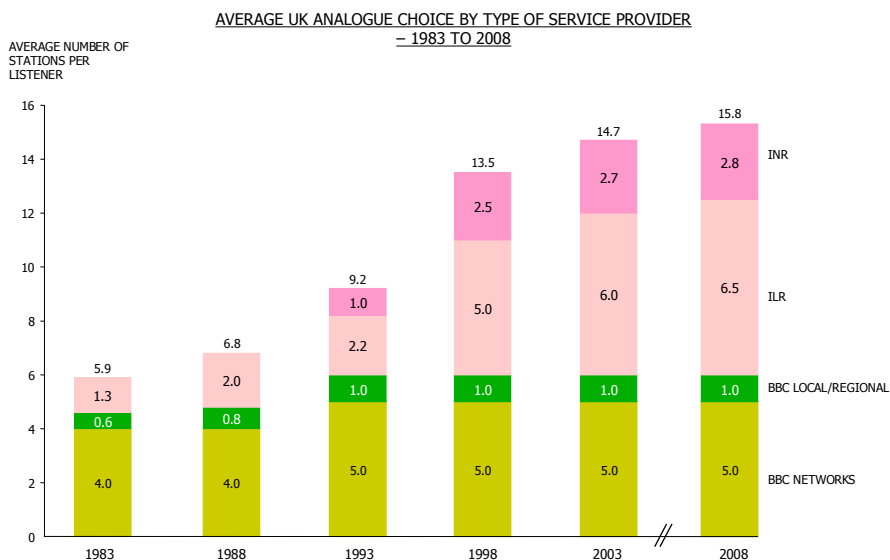
Across the UK the average listener has access to almost 15 analogue services – 6 from the BBC and almost 9 from commercial radio. This has risen from just under 6 services for the average listener in 1983, and just over 9 services in 1993. With the allocation of remaining analogue frequencies from 2004 to 2006, the average number should rise to just over 15 services per listener by 2007. There are no planned new BBC analogue services. (See Exhibit 2)

**Commercial Radio Currently Provides About 57 Per Cent Of The Analogue Radio Choice Available To The Average Listener, But Just 50 per cent of the FM Analogue Radio Capacity Available<sup>5</sup>. Commercial Radio Takes Just Under 50 Per Cent Of The Listening**

Average commercial sector choice has grown rapidly over the last 15 years from 2 stations to eight, and with this expansion in the number of services listening share has grown from 36 per cent of all listening to 47 per cent. But listening share has not expanded as rapidly as share of available services, as the commercial radio market has tended to concentrate on the 20 to 40 year old music listening market, leaving much of the older and younger markets, and the significant market for speech radio, to the BBC.

<sup>5</sup> FM radio is now the main frequency used to receive analogue services with many new radios only having FM tuning. FM in the UK offers stereo sound while medium wave only offers mono services. Mono broadcasts – especially of music – tend to be less popular with listeners.

**EXHIBIT 2**



Sources: OFCOM, RAB and O&O analysis

***The UK Radio Sector is Europe's Second Largest Radio Market in Terms of Value – behind Germany – Uniquely in Europe it has Thriving Commercial and Public Service Radio***

An analysis of the main European radio markets suggests that the UK is currently the second largest market in terms of revenue behind Germany. But Germany depends far more on licence fee funding for its regional network of ARD radio stations, leaving the UK with the largest commercial sector in Europe. Of all the leading European markets, the UK is the only market with both a developed public service and commercial sector - in terms of revenue, range and financial health (See Exhibit 3).

**EXHIBIT 3**

EUROPEAN RADIO SECTORS COMPARED 2001/2002 (Analogue Only)

	NET AID REVENUE	LICENCE FEE INCOME	NUMBER OF STATIONS					
			PUBLIC SERVICE		COMMERCIAL			COMMUNITY RADIO
			NATIONAL	LOCAL/ REGIONAL	NATIONAL	AFFILIATE NETWORKS	LOCAL/ REGIONAL	
GERMANY	€694m	€2,068m	-	50	-	-	190	-
FRANCE	€596m	€433m	6	47	3	14 (1,675)	2	1,570
UK	€800m	€780m	5	48	3	-	298	-
ITALY	€370m	€281m	4	5	-	27 (1,680)	2	1,500
SPAIN	€397m	€166m	5	16	-	11 (1,000)	8	200
NETHERLANDS	€170m	€125m	5	13	5	-	6	-
BELGIUM	€151m	Neg	-	10	-	4 (300)	33	-
SWEDEN	€50m	€50m	4	-	-	3	9	182

***The Analogue Commercial Sector in The UK is Based Primarily on Individual Local and Regional Stations whereas Many Overseas Commercial Radio Sectors Are Based Far More on Affiliate Network Structures.***

The structure of the UK commercial radio market has been largely determined by the licensing policy of the IBA, then Radio Authority and now Ofcom. It has sought to promote localness and regionality and to offer listeners in any one area a differentiated set of commercial services focusing on different tastes and demographics.

Licensing has also adapted the number of services to the size of market – with London and urban areas having more local stations, while smaller markets have fewer truly local stations (often only one or two), topped up by regional stations covering a number of local markets.

There exist significant restrictions on the ability of local and regional commercial stations of the same type or under the same owner to share broadcast output, and specific requirements for local programming and local studios. This has prevented the emergence of the affiliate networks that play an important role in the French, Italian and Spanish radio markets.

Commercial radio in the UK is, therefore, a product of managed competition, designed to encourage localness and to discourage the establishment of national networks – or quasi national networks. The three national services licensed in the 1990s – Classic FM, TalkSport (originally TalkRadio) and Virgin AM - were deliberately kept to formats that differed from what was being offered locally to limit audience and revenue substitution. Although Virgin's format is quite similar to that of the traditional ILR station, its AM frequency limits its effective reach and potential audience share.

## **b. Competition, Regulation, Market Structure and Ownership in Commercial Radio**

### ***In Many Markets Direct Competition Between Rival Analogue Commercial Services Is Limited***

Commercial radio licensing has in the past favoured a diversity of formats in any one locality or region, leaving each station with limited direct commercial competition for audiences.

This tends to mean that there are low returns to large increases in programme spend by commercial radio stations as there is relatively little pressure to compete for audience with a number of rival local stations offering very different formats.

Even in markets where there is a greater degree of direct competition between commercial services –such as that between Heart and Capital in London - this tends to feed through to higher star presenter salaries and rewards and larger marketing budgets rather than more complex and expensive programme formats.

### ***UK Commercial Radio Spends About £200 million A Year on Programming – Including Copyright Payments - An average of about £1m per station or about £125 per hour.***

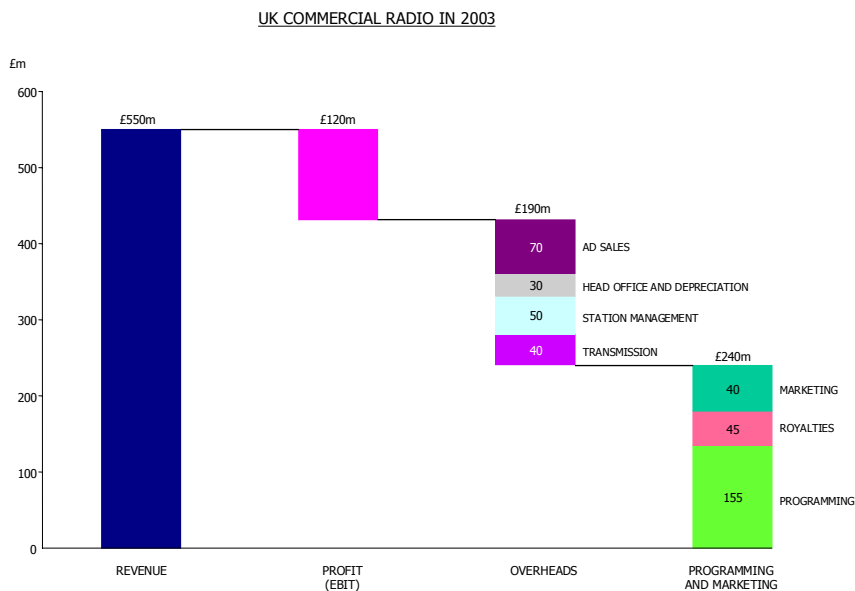
Commercial radio revenue was about £550m in 2003. Of this approximately £70m is spend on advertising sales and promotions, about £40m on transmission and about £30m on depreciation and head office costs. Station management and administration probably accounts for another £50m while royalty payments to music copyright holders add up to another £45m. Total fixed costs, therefore, amount to about £235m leaving about £315m for station programming marketing, programming and profits.<sup>6</sup>

Of this £315m, about £120m is currently earned in profits, about £60m is spent on marketing, and £155m a year in programming related activities. This means that together with music copyright payments for use of recorded music, commercial radio currently spends £200m on programming content. This averages out at less than £1m per station or £125 per broadcast hour. (See Exhibit 4).

---

<sup>6</sup> Royalty costs are not strictly fixed, as they are generally a percentage of revenue, and also vary by the amount of time music is played.

## EXHIBIT 4



**Station Budgets are Higher in London where the size of the London advertising market more than makes up for the larger number of local commercial stations.**

O&O estimates that the London station advertising market is worth about £130m, yielding average revenue per commercial local station of about £8.5 million, far higher than the £2m average revenue across the UK. This allows the average London station to spend £3m to £4m a year on programming, or about £350 to £500 per hour. In fact, stations like Capital and Heart, with disproportionately high shares of the London commercial audience and revenue, probably spend nearer £1,000 per hour.

**National Commercial Radio also Have Higher Programming Budgets But Also Have To Meet License Payments to the HM Treasury**

The larger coverage areas of national commercial stations do allow larger programme budgets even though they have quite high costs of transmission and their formats tend to be focused on narrower audience segments. Classic FM, Virgin and TalkSport all have programming budgets of between £8m and £10m, or £1,000 to £1,200 per hour.

National radio was also awarded by competitive financial bidding, which means unlike local and regional commercial radio, the national services combined pay about £10 million a year to HM Treasury in licence payments.

**Commercial Radio has Concentrated on the 15 to 45 year old Audience, and Within That Primarily on the 20 to 35 Audience**

Although each large radio market sustains a range of music types and formats with differing gender and music taste skews, nearly all of these are concentrated on age groups between 15 and 45, with little commercial analogue provision for the under 15s or over 50s.

Within the average of 6 local or regional commercial stations received across the UK, listeners usually face a choice including:

one local “heritage”<sup>7</sup> ILR station focused on commercial hits radio primarily targeting the 25 to 35 age group but with a broader reach of 20 to 40 year olds across the week (Capital FM, Metro Radio, Leicester Sound etc);

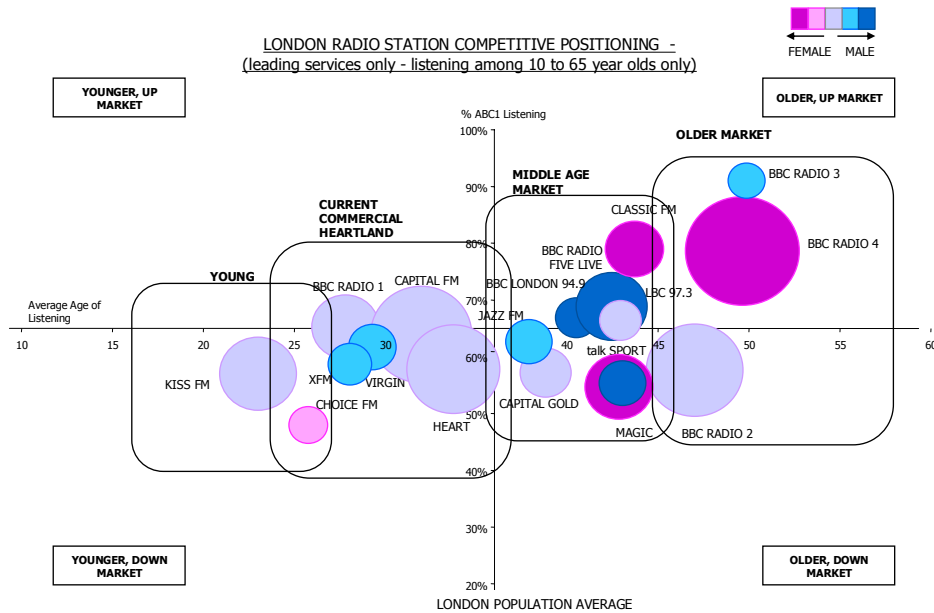
an oldies or an easy listening based station – one of which is often on medium wave - targeting the 35 to 50 age group (e.g. Classic Gold, Magic, Jazz/Smooth FM etc),

a local/regional dance/urban or pop music station targeting the 15 to 25 age group (Kiss, Galaxy, Vibe etc);

a regional or local adult contemporary music station – sometimes with some speech output mixed in – targeting the 30 to 45 age group (Heart, Real Radio, Century etc)

This is then usually complemented by reception of an overlapping heritage ILR station from a neighbouring market and or an extra adult contemporary or easy listening station. Even in markets such as London, where there are over 18 local commercial services, the commercial services themselves tend to cluster around the 15 to 45 age range, with a particular focus on the 25 to 35 age group. (see Exhibit 5).

**EXHIBIT 5**



<sup>7</sup> The phrase “heritage” ILR station is used by the commercial industry to refer to those single FM services that have existed since the 1970s and 1980s which use to account for nearly all commercial listening and still to some extent aim to cover a wider cross section of listeners – albeit focused on the 20 to 40 market – than most new more thematic stations.

The national commercial services then provide an additional news/sport service (Talksport), Classical Music (Classic FM) and – with more limited coverage – a commercial hits/adult contemporary service (Virgin).

This concentration on the 15 to 45 market is probably a result of a combination of at least three factors. First, as will be outlined below, radio advertisers so far have not valued audiences over 45, making it difficult to establish profitable commercial stations focused on the over 45 year old market alone. Second, over 50 year old audiences tend to require a greater proportion of speech radio in their overall consumption – which tends to be more expensive than music programming. Third, the BBC already provides a range of speech services which attract the over 45 audience.

***Commercial Speech Services Are Limited To The Largest Markets And Focus On News, Phone-Ins And Sport. Mixed Speech And Music Services Have Had More Success In Commercial Radio Although Are Probably Still Not Hugely Profitable.***

Commercial radio tends to concentrate its speech output on the largest coverage areas – national, regional and London – and focuses on phone in, news and sport formats whose costs can be kept at £500 an hour or less. Stations such as LBC in London, Century Radio in the Midlands and the North and Real Radio in Central Scotland and South Wales, either mix speech and music together, or concentrate on phone-ins, news bulletins and occasional live sports events.

While pure speech commercial stations tend to obtain 2 to 4 per cent listening share in relevant markets, speech and music mixed services have tended to gain 5 to 10 per cent share in relevant markets. However, the costs of such services are still higher than comparable and more music orientated services probably leaving them with lower than average profit margins.

***Commercial Analogue Local Radio as a Whole Devotes about 6 per cent of Its Airtime to Local and National News Bulletins, Local Weather and Travel and Local What's On and Public Information Bulletins***

A recent survey by the Commercial Radio Companies Association (CRCA)<sup>8</sup> of 218 local/regional commercial stations, suggested about 10 hours a week on average is devoted to local and national news bulletins, information on weather, travel and what's on as well as information on local campaigns and events.

***Richer Forms of Speech Output Are Simply Not Economic for Commercial Radio***

Richer forms of speech output (commonly found on BBC services as we shall note below) are simply not economic on commercial radio. New dramas and comedy can routinely cost between £15,000 and £20,000 per hour to make and sometimes more while magazine programming, features and news magazine programmes – as opposed to simple headline bulletins – can cost up to £5,000 an hour.

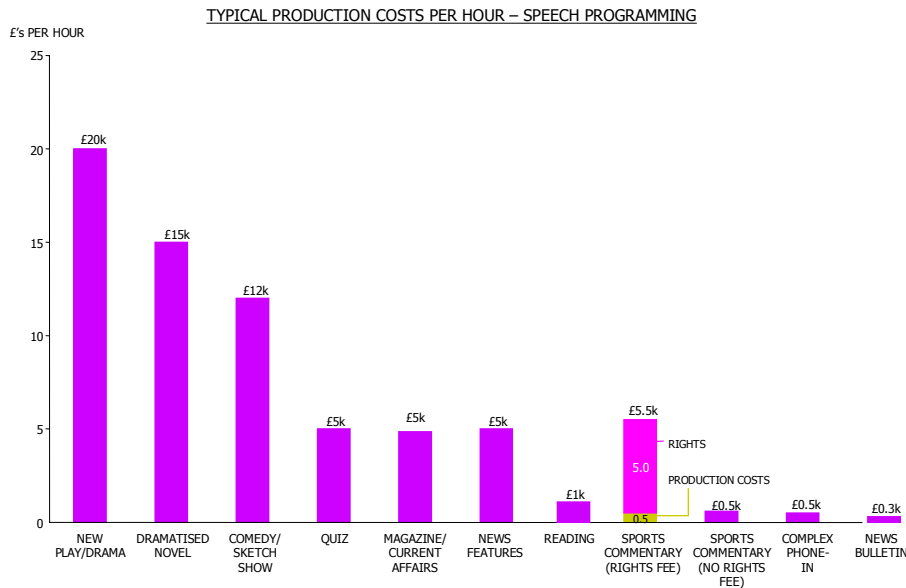
A simple analysis of the audiences available in London for example, coupled with the likely advertising price per thousand impacts that might be achieved suggests that to

---

<sup>8</sup> “Commercial Radio: In the Public Service – An Audit by the Commercial Radio Companies Association” September 2004

breakeven with this type of programming a London station would have to take a 10 to 20 per cent share of the peak time audience. While a national station might only have to gain a 5 to 10 per cent share to breakeven with this mix of programming, it would still be far less profitable – and more risky – than alternative formats.<sup>9</sup>

**EXHIBIT 6**



**c. The Radio Advertising Market**

***The Radio Advertising Market is Made Up Of Three Separate Sub-Markets.***

The £560m UK radio advertising market is really three different advertising markets. The largest market – about £270m - is driven by broad national advertisers seeking both strong national reach among the 20 to 40 age group, and the ability to weight that reach by region and locality. These advertisers are often looking to add frequency to high reach TV and press campaigns especially with the under 40 consumer.

This market is still dominated by the heritage ILR stations whose audience is at the core of the broad demographic demanded, and which often still command the highest reach among all local or regional stations. It is made up of about £177m spent by national campaigns on individual local stations plus about £60m out of the £95m spent by national campaigns on quasi-national networks, and about £30m of sponsorship.

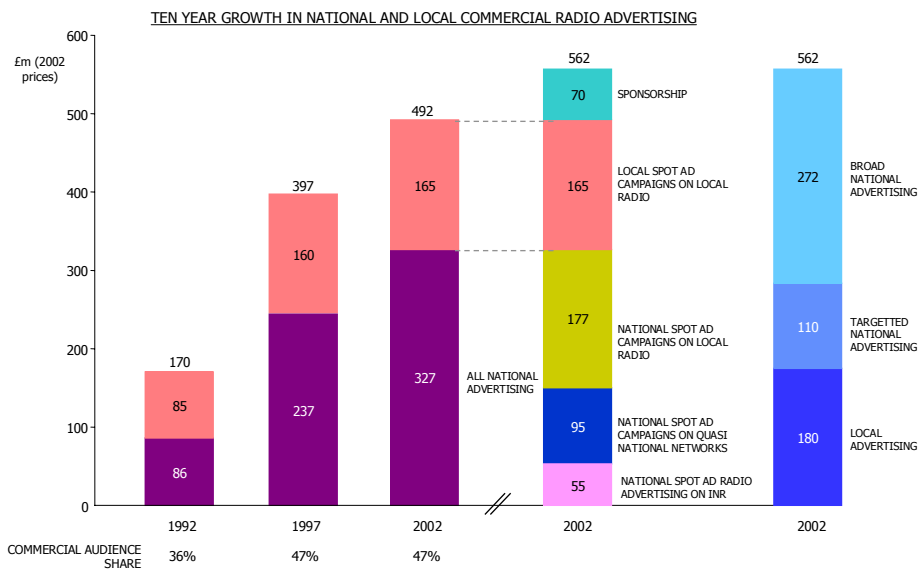
There also exists an important local advertising market – worth about £180m a year (£165m of spot advertising and about £15m of sponsorship)– where radio provides local retailers

<sup>9</sup> In addition, if this share were additional to existing commercial audiences – i.e. at the expense of the BBC, the advertising price would be likely to fall, increasing the necessary share for breakeven even further. Alternatively, if the share all came from other commercial stations, this would cause significant economic harm to other radio stations just in order to break even – probably a major reason why licensing authorities have not licensed such a service in the commercial sector.

and service providers the only effective choice to local press and transport as a way of advertising with limited wastage. This market is also dominated by the heritage ILR stations.

Lastly, there are targeted national advertisers, focused on a narrow and often more attractive demographic who are less concerned with weighting their campaigns by region or locality – worth about £110m per year (£90m of spot advertising and about £20m of sponsorship). This market is occupied by the national INR services and niche quasi national services with a network of local or regional licenses covering urban/dance music (e.g. Galaxy), indie/rock music (e.g. Xfm), jazz/easy listening (e.g. Smooth/Jazz FM and Magic) etc. (see Exhibit 7)

**EXHIBIT 7**



Local stations, especially heritage ILR stations, manage their inventory between local and broad national advertisers so as to maximize their revenue. In urban areas, where demand from broad national advertisers is strong due to their focus on the main population areas – local advertisers are often priced off the station. However, in smaller markets, local advertisers still play a very important part.

**Traditional “Heritage”<sup>10</sup> ILR Stations Still Command A Premium Within the Overall Radio Advertising Market**

Those radio groups with significant numbers of heritage ILR stations – GWR, Capital, EMAP and Scottish Radio Holdings – still seem to sell their advertising at a premium when compared with groups focused more on regional and niche stations – Chrysalis and Guardian Media Group – even allowing for differing levels of average income in the areas they cover and their demographic focus. (See Exhibit 8)

<sup>10</sup> A term that refers to the stations that have existed since the 1970s and 1980s which used to be the only FM commercial station in any given market and which are often still the leading brands within any one market.

**EXHIBIT 8**

COMPARATIVE PERFORMANCE

	GROUP	COMMERCIAL SHARE WITHIN MARKETS	AD YIELD RELATIVE INDEX*	AVERAGE NUMBER OF COMPETITIVE ILR STATIONS IN MARKETS	GDP INDEX
HERITAGE ILR GROUPS	CAPITAL	10.9%	377	7	114
	EMAP	11.9%	370	7	106
	GWR	21.4%	246	2	105
	SRH	23.7%	185	2	107
REGIONAL GROUPS	GMG	8.7%	110	5	101
	CHRYSLIS	12.5%	202	9	117

\* This is the advertising revenue per listening hour for the specific radio group relative to the average for the whole commercial radio sector

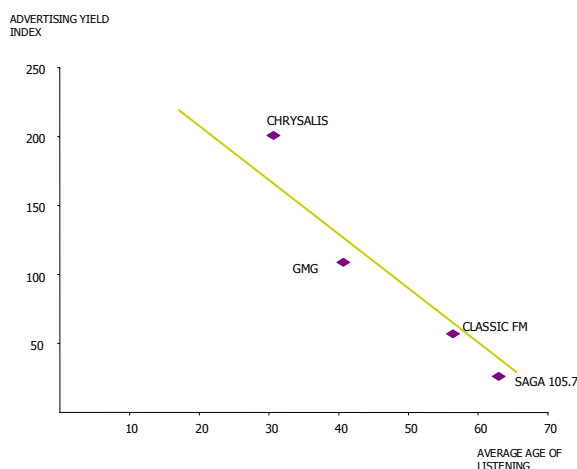
Sources: RAJAR, ONS, RAB, Company Accounts and O&O analysis

This would suggest that heritage ILR stations still enjoy an advertising premium over other stations based on the fact that while audiences continue to segment, they still retain the single largest commercial audience in any given market, making them attractive to broad national and local advertisers alike.

***Audiences over 45 Are Currently Attributed Low Value By Advertisers***

The evidence suggests that radio advertisers (local, broad national or targeted national) tend to attribute little value to audiences over 45. Comparing the advertising yield of targeted radio groups or stations – such as Chrysalis, Guardian Media Group, Classic FM and Saga Radio (in the West Midlands), with the stations' average listening age, suggests quite a steep decline in value. (See Exhibit 9)

THE RELATIVE ADVERTISING YIELD AND AGE PROFILE



### **High Historic Growth In Radio Advertising Has Been Driven by the Structure of the Radio Market as Well as Total Commercial Listening**

The 10 per cent per year real growth in radio advertising in the 1990s was a result of supply side changes in radio as well as demand growth. While general economic growth and the increased effective cost of network TV advertising helped boost demand, increased listening hours of commercial radio, greater audience segmentation and the arrival of new national radio stations all helped to bring in new money to radio by offering advertisers more for their money.

### **Overall Elasticity of Demand<sup>11</sup> for UK Radio Advertising Has Proven Difficult to Assess Using Standard Econometric Regression Analysis**

With so many structural supply side factors changing in the 1990's it is difficult to separate out the exact elasticity of demand from historic trend data.

In fact, unlike UK TV advertising, there has been no serious econometric study of the elasticity of demand for radio advertising in the UK because of these difficulties. In recent times the most extensive studies of the issue in the UK have come as part of debates over radio mergers but these have been based on advertiser surveys on potential reactions to price changes rather than historic analysis of trends in actual reaction to price and quantity changes.

<sup>11</sup> Elasticity of demand for advertising is the response in the price of advertising to changes in the volume of advertising impacts supplied. If the price of advertising drops by 5 per cent in response to a 10 per cent increase in the volume supplied, the elasticity is said to be -2 (+10 divided by -5). The volume of advertising is measured by the volume of advertising slots per hour multiplied by the audience for each slot. The price of advertising is the price of buying 1000 listeners to a 30 second slot – the so called “cost per thousand”.

### ***Hypothetical Price Surveys of Advertisers Suggest a Degree of Price Sensitivity and Fairly Elastic Demand with Elasticity of -2.5***

The Competition Commission itself has conducted advertiser surveys on radio advertising, and more generally the substitutability of local advertising media, in three inquiries over the last 6 years – *Capital Radio plc and Virgin Holdings Limited (1998)*, *Johnston Pres plcs and Trinity Mirror plc, (2002)* and *Scottish Radio Holdings plc and GWR Group plc (Galaxy Radio Wales and the West Limited) (2003)*.

In the most recent inquiry which involved looking at the Severn Estuary advertising market, the Competition Commission survey suggested that if radio advertising prices were increased by 5 per cent, one third of all advertisers would not change their advertising decisions, one third would cut out radio altogether, and another third would switch some advertising to other media. Amongst advertisers, it was local businesses that were least likely to change their advertising decisions.

A similar survey of the Severn Estuary advertisers was carried out by Indepen Consulting for a report commissioned by the Commercial Radio Companies Association (CRCA). Unlike the Competition Commission survey the Indepen survey tried to clarify whether the “no change” and “switch some” advertising responses given in the Competition Commission survey referred to spending or the volume of slots purchased (something which was not made clear in the Competition Commission survey and which has consequences for any advertising elasticity calculation<sup>12</sup>).

Using answers as to how many respondents would change their advertising budgets – and how much they would change them by – Indepen were able to extrapolate a likely change in spending in response to price changes. Working through the different responses, they calculated that a 5 per cent increase in advertising price would decrease spending by 8 per cent – implying a reduction in volume of about 13 per cent. This in turn implies an elasticity of demand of about 2.5.

Similarly, the survey suggested that a 10 per cent increase in price would lead to a 13 per cent reduction in spending, or a 23 per cent reduction in volume – an elasticity of -2.3.

These results do not necessarily contradict the results of the Competition Commission survey which also suggested that two thirds of respondents would adjust their use of radio downwards in response to a price increase, and those two thirds of respondents accounted for 86 per cent of advertising spend.

### ***The Competition Commission Believes Hypothetical Price Surveys Overstate Price Sensitivities***

However, in several places in the report on the Galaxy Wales and West acquisition by GWR and SRH, the Commission maintains that other evidence they collected suggested the survey overstates price sensitivity and substitutability. For instance, when respondents were asked how their behavior might change in reaction to a series of increasing price rises, only 8 per cent said they would change their behavior in response to 5 per cent change, and only 27 per cent said they would change behaviour in response to a 20 per cent price rise.

---

<sup>12</sup> A response of no change in volume would imply a 5 per cent increase in spending from a 5 per cent price rise from those respondents – elasticity of zero. A response of no change in spend would imply a 5 per cent reduction in volume – elasticity of -1.

In addition, when Severn Estuary advertisers were asked which, if any, media might provide a reasonable alternative to their current radio advertising on GWR, Orchard and Vibe, only 15 per cent said national or regional newspapers, only 6 per cent said outdoor advertising, and only 3 per cent said television. All this suggested a lack of substitution possibilities in reaction to a price rise, suggesting in turn that volumes bought would not reduce significantly and, therefore, price sensitivity would be less elastic.

***Econometric Analysis of the USA Market Suggests Elasticity estimates ranging from -0.25 to - 2.1.***

While no comprehensive econometric analysis has been done in the UK, there have been at least 4 recent studies of the USA advertising market. Of these four, one was conducted covering Beer advertisers alone, and therefore can not really be extrapolated to advertisers in general. Of the other three, one is a cross section analysis of all advertising across 110 different stations in 1995, another is a review of national advertising time trends from 1960 to 1994, and the last looks just at local advertisers in 45 markets in 2001. Of these three studies, elasticity estimates range from -0.25 to -2.1.<sup>13</sup>

***Overall an Elasticity of -2 is A Reasonable Estimate Although Probably Only Fully Applicable to Relatively Small Changes in Volume of Price.***

Given that surveys come out with implicit elasticity of -2.5, but that the Competition Commission believe this to be too high, an elasticity of -2 is probably a reasonable estimate to use when assessing revenue impact. However, this estimate is only very approximate and should be treated as indicative. It would also not necessarily apply to large scale changes in price and volume.<sup>14</sup>

***Elasticity of Demand for Radio Advertising is Likely to Vary Considerably Within Each of the Three Advertising Types – Local, Broad National and Targeted radio Advertising***

One of problems involved in estimating the elasticity of demand for advertising is the existence of the three very different types of advertiser demand noted above. Local, targeted national and broad national advertisers are all likely to react differently to volume changes and price rises. Over time the mix of advertisers may well change for given stations or in given markets.

In practice, stations able to provide local and national advertising opportunities will optimize the use of their advertising inventory by switching it between both markets until it maximizes its revenue. Since no data actually exists on how much inventory was sold to which type of advertiser, it is not possible to estimate these different price elasticities.

---

<sup>13</sup> Is Radio Advertising a Distinct Local Market? An Empirical Analysis – Review of Industrial Organisation 14 - Ekelund, Ford and Jackson (1999); Intermedia substitutability and Market Demand by National Advertisers – National Bureau of Economic Research Working Paper 8624 - Silk, Klein and Berndt (2001); and, On the Substitutability of Local Newspaper, radio and Television Advertising in Local Business Sales - A. Bush FCC Research Paper 10 (2002)

<sup>14</sup> Elasticity estimates – either through surveys or econometric regression analysis are only actually applicable for small scale changes. It is quite probable – in fact – quite likely – that elasticity will alter for different levels of commercial listening as the market gains more and more access to commercial audiences given the likelihood of diminishing marginal returns from more commercial impacts for advertisers. Indeed, the advertiser surveys conducted for Competition Commission inquiries deliberately concentrate on relatively small changes in volume of price.

However, evidence from the Competition Commission report did suggest that local businesses were less likely to have alternatives to radio advertising than national agency buyers, and that radio advertisers would be unwilling to switch from GWR – the main heritage ILR station – to other smaller niche stations. This might suggest that local advertising demand and broad national advertising demand – that tends to concentrate disproportionately on the high reach heritage ILR station – might be less elastic than targeted national advertising.

## **2. The Commercial Radio Sector's Likely Evolution to 2014**

The commercial radio sector is likely to undergo significant changes over the next 10 years driven by changes in technology and distribution, an evolving regulatory environment and demographic shifts in the UK population.

### **a. The Growth of Digital**

With the end of analogue licensing by 2006, the main driver of change in the UK commercial radio sector over the next 10 years will be the growth of digital reception through DAB, internet and digital TV distribution.

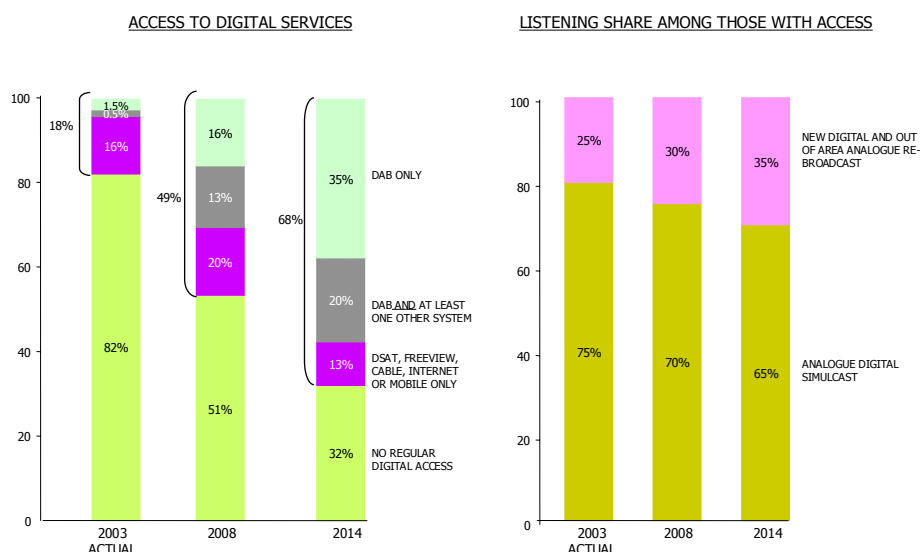
#### ***70 per cent of UK Individuals Could be Regularly Accessing Digital Radio Services by 2014***

Currently about 18 per cent of the UK population have some regular access to digital services – the majority through their digital satellite, cable and Freeview set top boxes, but a growing number through DAB enabled radio sets. Most industry forecasts suggest that the next stage of growth will depend more on DAB reception through cars, hi-fi and portable players than has been the case over the last few years. While the next 10 years are likely to leave the UK still well short of complete digital penetration – and even in those homes that have digital access a large proportion of listening is still likely to be through old analogue receivers – by 2014, about 70 per cent of UK households could have some regular weekly access to digital services. (See Exhibit 10).<sup>15</sup>

---

<sup>15</sup> The recent DRDB medium term forecast produced in October 2004 has suggested that terrestrial DAB could reach 28 per cent of UK households by the end of 2008.

**EXHIBIT 10**



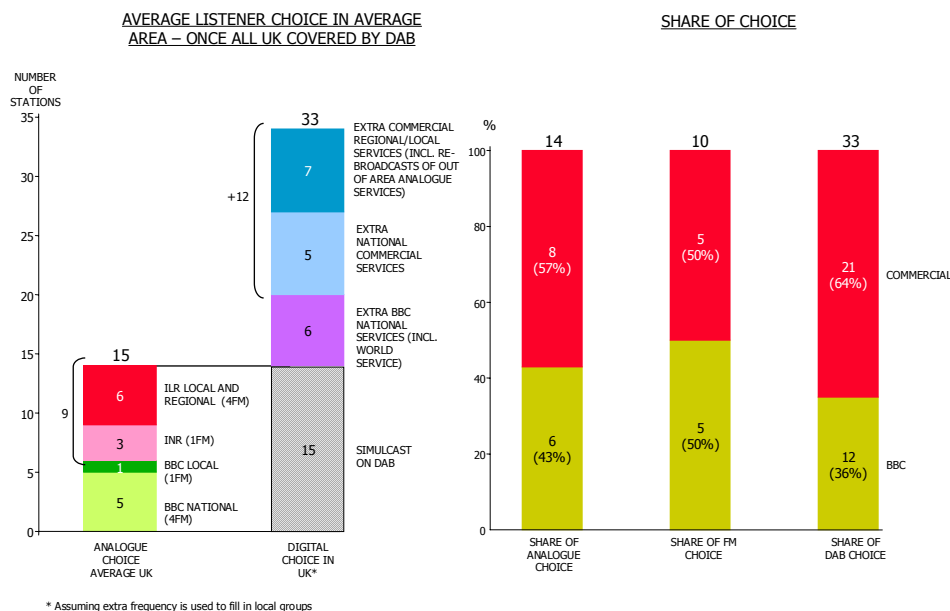
Sources: RAJAR, DRDB, O&O analysis

**DAB reception will increase the average number of radio stations available to the average listener in the UK from just under 15 to about 33 services. This could rise to about 40 services if new frequency is used to maximise choice for 90 per cent of the UK, rather than to reach almost 100 per cent of the UK.**

Currently, DAB national DAB signals carrying the BBC's new and simulcast digital services and the 8 new and simulcast commercial services of Digital One, cover about 85 per cent of the UK population. Regional and local service DAB multiplexes cover about 72 per cent of the UK population.

A decision is still pending on extra Band III and L Band frequencies which could either be used to provide almost complete UK coverage for regional and local DAB services – including simulcast of existing analogue services as yet not available in digital – which would offer an average of 33 services across the UK - or a new national multiplex covering about 85 per cent of the UK which could take the number of services to 45 for those in national multiplex reception areas, but leave some areas of the UK uncovered by DAB. (See Exhibit 11)

**EXHIBIT 11**



**Of the 18 New Services Available (if the Maximising Reach Option is Chosen), Commercial Radio will be Providing 12, and will therefore be Providing 21 out of the total 33 services Available.**

The BBC has access to one national multiplex – used to simulcast its five national services plus six others – and one space on relevant commercial multiplexes to simulcast its local and regional services. This leaves the commercial sector with at least one national multiplexes and almost all the capacity on local and regional multiplexes. In the digital age, commercial radio therefore has about 65 per cent of available frequency compared with it 55 per cent of analogue frequencies and its 50 per cent of FM analogue frequencies.

Beyond DAB distribution, digital satellite currently carries 104 radio services, the vast majority of which are commercial services.

**Current Digital Listening Figures Suggests Those Homes with Digital spend about 25 per cent of their Time Listening to New Digital Services, and of Time About 80 per cent is spent with new commercial services**

Early RAJAR figures on listening to new digital services, and out of area digital listening to existing local analogue services, suggests that about 25 per cent of listening of those with digital access is to new digital services. Of this only about 20 per cent is to the BBC's new digital services, leaving the commercial sector with 80 per cent of the listening.

**Many Of The New Commercial Digital Services In Any One Area Are Actually Rebroadcasts Of Existing Analogue Services From Another Area – Thereby Creating So Called Quasi National Networks**

Of the 13 new commercial digital services available to the average UK DAB digital listener 5 are national services carried on Digital One, about 4 services are re-broadcasts of existing analogue services to other parts of the country (e.g. Kiss FM, Xfm, Choice etc), with the remaining 4 being totally new to digital. These totally new services more often than not have multiple regional and local multiplex access, and so cover significant proportions of the UK.

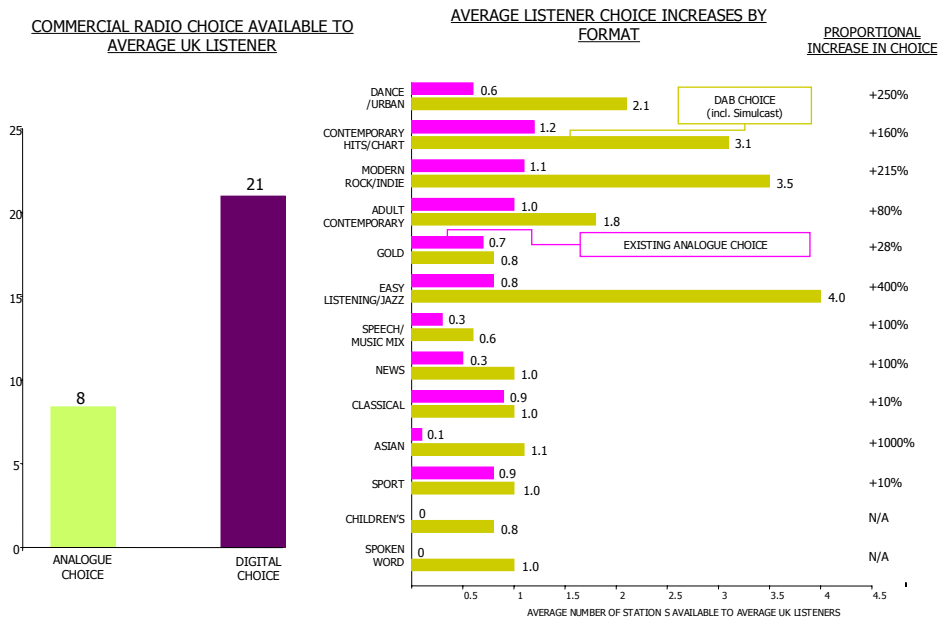
Many of the out of area re-broadcast networks enjoy well over 50 per cent coverage of the UK through their combined digital and analogue distribution and, therefore, provide the foundations for a number of "quasi-national" networks.

**The Current Commercial DAB proposition Suggests an expansion in Easy listening, Rock, Pop, Adult Contemporary and Speech Services for the Average Listener**

Current DAB commercial multiplex services provide the greatest levels of expansion in average consumer choice within the easy listening, urban, rock, chart/pop and adult contemporary formats. There is also a significant increase in speech and speech/music mix formats.

Taken together this represents an expansion of commercial radio slightly beyond its heartland 20 to 40 audience to a 15 to 50 audience, together with more choice within its heartland audience – often dividing that audience by gender – rock versus pop/urban – or age sub-group – chart/pop versus adult contemporary. (See Exhibit 12).

**EXHIBIT 12**



## **b. The Evolving Regulatory Environment**

### ***The Eventual Commercial Proposition That Emerges Will, However, Depend As Much on the Developing Regulatory Framework as on the Economics of Individual Services***

As noted above, the current commercial radio offering in the UK is as much a result of the licensing practices and principles of the Radio Authority and now Ofcom as it is of the comparative economics of different types of format. Regulators have sought to use licensing to bring range and variety to local markets, sometimes perhaps at the expense of local competition.

While the digital radio world has a slightly looser regulatory regime, there is still a requirement for multiplexes to offer a range of services, and for local and regional multiplex services to eventually offer some level of local programming. Together with continuing controls on the ownership of analogue services at a local level (the so called 2 plus 1 rule that limits any one commercial owner to effectively a maximum of 55 per cent of the ownership points in any one local market), regulation of radio in the digital age is still likely to have a significant impact on the likely commercial market offering.

### ***More Liberal Analogue Ownership Regulation May Well Enhance the Tendency to Quasi-National Network Brands***

The 2003 Communications Act removed any national share limitations on commercial radio owners, and restricted ownership limits to the local 2 plus 1 rule whereby any one owner can not own more than 55 per cent of the ownership points in any given local market.

This does allow for some more consolidation at a local level but overall puts the emphasis on consolidation between non overlapping commercial radio groups. When such groups come together they will often find that they have similar formats – in both analogue and digital – operating in different areas of the UK. One of the easiest ways of realizing post merger synergies will be to merge these operations and establish strong quasi national networks operating across analogue and digital.

For instance, the recently announced merger of GWR and Capital is likely to bring together Capital Gold and Classic Gold, and/or Xfm and The Storm. Similarly a future merger of EMAP and Chrysalis could bring together Kiss and Galaxy with combined digital and analogue coverage of 70 per cent of the UK.

### ***Loose Restrictions on Multiplex Formats Could Allow More Direct Head to Head Competition Among Commercial Services***

While there is a general requirement for local and regional multiplexes to have a range of services, controls are far less prescriptive than in the analogue world. This means that digital is likely to bring formats into local and regional markets which have significant overlap with existing heritage ILR and niche analogue service.

For the first time outside of London, heritage ILR services could face competition from a range of services targeting parts or all of the 20 to 40 year old audience. This could put the incumbent services under significant competitive pressure.

### ***Potential Strict Local Programming Requirements on New Digital Services are Unlikely to Be Sustainable***

At the moment, it is suggested<sup>16</sup> that local and regional digital multiplex services will have to include local programming once digital penetration increases to reasonable levels. The extent of these local programming requirements will have a significant impact on the commercial market equilibrium over the next 10 years.

High local programming requirements would be likely to make these local digital services struggle financially, yielding greater share to existing incumbent analogue services, and to national digital services. Most important, it would probably restrict the ability of the new local commercial service to challenge the incumbent ILR stations position in offering local and broad national advertisers high reach within each local market.

This in turn would force those local and regional digital services not already part of quasi-national networks to become so in order to share as many common costs as possible in order to be able to afford the local programming commitments.

### ***The Most Likely Outcome is an Easing of Local Programming Requirements and a Portfolio of Targeted and Differentiated Quasi-National Networks with Some Local Output***

The actual outcome depends on the position of regulators at the time. For now, the most likely result seems to be some lower level of local programming commitments for local and regional digital services which will exist within a series of quasi-national networks targeted for the most part on small incremental audiences (both outside the 20 to 40 range and sub-segments of it), with a gradual rather than drastic erosion of the premium position of the incumbent ILR stations.

### ***Community (Access) Radio is Likely to Focus on Small Population Areas and/or Communities of Interest Within Larger Local Areas***

While some of this potential shortfall in local programming could be made up for by a vibrant – and mostly volunteer staffed– community radio sector, such services are likely to focus on small sub markets within local radio areas or communities of interest within larger local areas.

### **c. Likely Commercial Sector Share, Revenue and Segmentation**

#### ***Commercial Sector Share is Likely to Rise Towards 60 per cent by 2014 and then to 65 to 70 per cent once Digital Conversion Is Complete***

With a portfolio of services designed largely to appeal to incremental and niche audiences, combined with access to 65 per cent of available frequency, the commercial radio sector should be able to push its share of all listening towards the 60 per cent level by 2014 (our actual forecast is 57 per cent in that year). Thereafter, share will continue to grow towards about 65 to 70 per cent once all of the UK population gain some access to digital services. (See Exhibit 13)

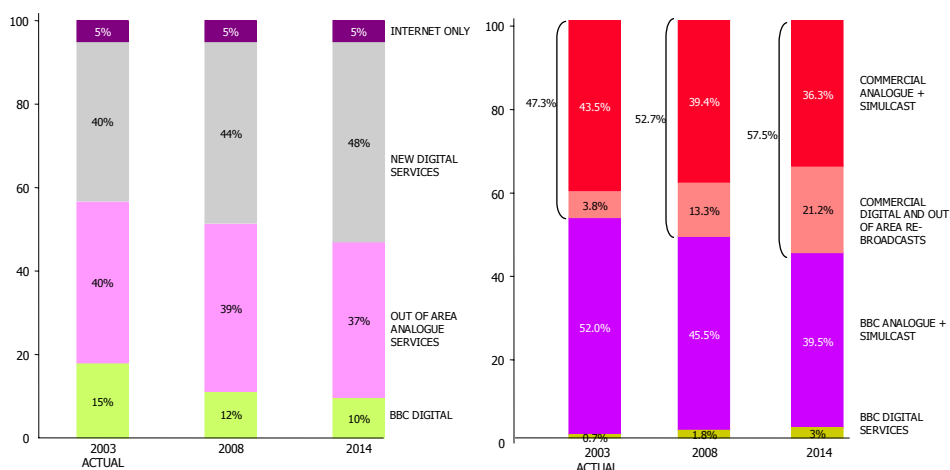
---

<sup>16</sup> In fact it is in the digital service licence that local programme requirements may be added.

**EXHIBIT 13**

LISTENING SHARE WITHIN NON  
SIMULCAST DIGITAL LISTENING

OVERALL LISTENING SHARE BY TYPE OF SERVICE



Sources: RAJAR, DRDB, O&O analysis

**More Services targeting the 35 to 50 year age group are likely to appear**

Overall there are likely to be more commercial services targeting the 35 to 50 year old age group (rather than the over 50s where audiences are likely to be difficult to monetize as shown in the previous section). This is likely to include at least one quasi national easy listening station, a quasi-national speech/music service combined with a national speech service.

**Services Targeting the Under 20s, and those Aiming to Divide Up the Current Heritage ILR Audience into Smaller Segments Are Also Likely to Appear**

Commercial radio will also target other incremental audiences around or within its 20 to 40 core audience. Services for teenagers and possibly children are likely to develop, as well as services aimed at primarily female of male segments of the 20 to 40 age range – i.e. rock formats or soft adult contemporary/soul formats.

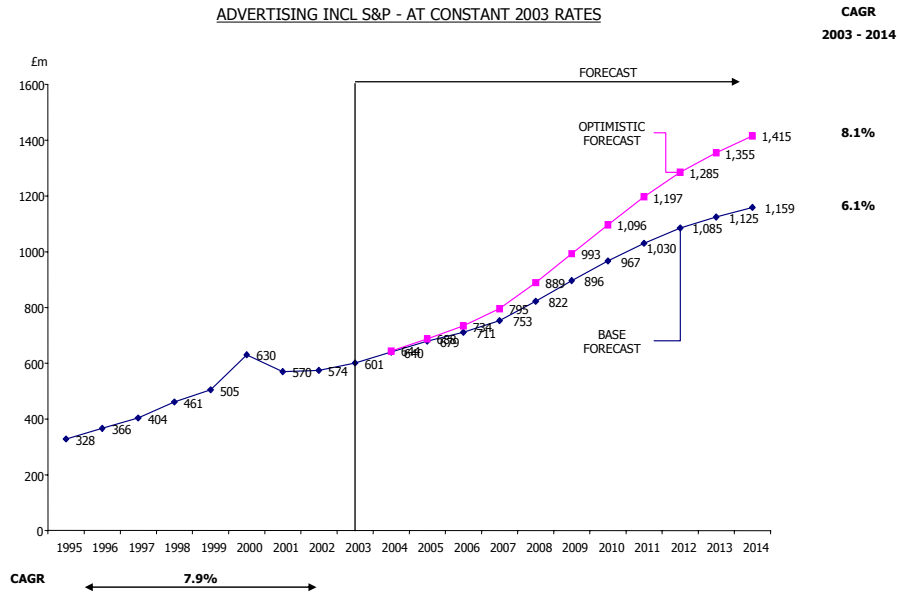
**Total Commercial Radio Revenue is Likely to Grow to Over a £1 billion in Today's prices by 2012 – growing by 6 to 8 per cent a year in Real Terms.**

With reasonable economic growth and no significant downturn in consumer spending over the next 10 years, combined with increased audience segmentation and targeting, larger commercial audiences, and new quasi-national commercial outlets, radio advertising should grow by 6 to 8 per cent a year in real terms from 2004 to 2014. Not as high a growth rate as the boom years of the mid to late 1990s, but still well above average advertising growth rates of 4 per cent a year in real terms.<sup>17</sup>

<sup>17</sup> This is only an indicative forecast and in the medium term is similar to current industry expectations, O&O has not produced a detailed revenue forecast model for this study.

The only potential structural downsides for radio are, first, the growth of the internet and niche satellite TV channels which might challenge radio's leading role in providing frequency and segmentation to advertisers, and second, the fragmentation of the heritage ILR audience which might drive away some broad national advertiser spending just as the growing number of niche services are attracting more targeted national advertisers. (See Exhibit 14).

**EXHIBIT 14**



**d. Likely Competitive Dynamics and Structural Changes**

***Niche Quasi-national networks are Likely to Become Increasingly Important Despite Some Regulatory Requirements for Local Programming***

The current licensing of digital services on DAB multiplexes already suggests that much increased choice will be the re-broadcasting of analogue formats outside their existing local transmission areas – about half the “new” local/regional multiplex commercial digital stations available to the average listener will be such re-broadcast services.

Stations such as Xfm and Kiss FM already achieve about 50 per cent reach of the UK population through their analogue and digital capacity across the country. Combined with their carriage on digital TV platforms, this makes them quasi-national networks.

***Heritage ILR services are likely to come under Increasing Pressure, Perhaps Eventually Losing Their Premium***

The advertising premium currently enjoyed by the leading commercial station in each market may well not just transfer to a new leading station but eventually might disappear entirely as broad national advertisers either have to look to other media for high reach or

have to achieve it through booking slots on a number of different local niche radio stations.<sup>18</sup>

***Most Digital Services will have to exist on less than 2 per cent share in areas they cover. Even the strongest quasi national networks are likely to have less than £30m in revenue by 2014.***

With the average UK radio market having 13 to 18 extra commercial digital services – depending on frequency use – taking between them about 21 per cent audience share, the average share per service is likely to be less than 2 per cent. This will make it difficult for totally new digital services to survive in even reasonably large local and regional markets, and increase the pressure to form quasi-national services with limited amounts of local programming.

If such a network was to gain 2 per cent share in each local market it had a presence in, and was able to reach most of the digital homes in 2014 – about 70 per cent of all UK homes - then it would gain about 1.4 per cent share overall, which equates to about 2.2 per cent share of all commercial impacts by 2014. With advertising selling at average market rates, this would be likely to yield £25m a year by 2014.

***The Commercial Radio Market Will Offer a Wider Range of Services Than Today But None is Likely to Have the Resources or Incentives to Spend Significantly on Programming – especially Local Programming***

Local radio markets will have a greater range of services available than today, with probably an extra easy listening or speech music/mix stations, a teenage focused station and a rock station in most large and medium sized markets. Some markets might even have competing – or at least overlapping – commercial hits radio or adult contemporary stations.

The age range covered is likely to be 10 to 50, with some outreach to the over 50s market through services like Saga and, of course, Classic FM.

But while radio revenue may more than double, the number of commercial services sharing that revenue in any one local market will have gone up by 2.5 times, while the heritage ILR premium may well have eroded leaving no one station in a position to afford much local programming.

***Where Head to Head or Significant Overlap Competition Does Encourage Spending, Most Spending Is Likely to Go on Marketing or Star DJs***

In larger markets where revenue might increase more than the number of stations available, and where there are more likely to be overlapping formats, monies available to compete are likely to end up in marketing and promotional spending and bidding up the price of top DJs.

---

<sup>18</sup> In the former case, the whole value of the radio advertising market will be reduced – or at least the growth rate will be lower – in the latter case, radio market growth will remain but no one station will enjoy a premium, this will reduce the revenue of the leading heritage stations and spread it across many niche stations reducing the capacity of any one station to fund new and especially local programming.

***Where Competition is Less Intense Their Will Be Limited Commercial Incentive to Increase Programme Budgets.***

In those local and regional markets where most the commercial digital and analogue stations are well differentiated from each other, station owners are unlikely to compete by increasing programming spend.

***Leading Commercial National and Quasi- National Networks Are Unlikely to Spend much More than £10m to £15m on Programming with Local Programming Limited to £200K to £300K per market.***

Even successful quasi-national and national networks are unlikely to spend more than £10m to £15m on programming. Local programming budgets of existing heritage ILR stations are likely to be squeezed – especially if ownership limits and advertising market concerns from the Competition Commission limit local level consolidation.

The local budgets of new local digital stations and quasi-national networks are unlikely to be much more than £200K to £300K per market.<sup>19</sup>

---

<sup>19</sup> O&O modelling suggests that the average local service is likely to have revenue of no more than £0.5m before 2009, which might build to a maximum £1.5m by 2014. In order to make a reasonable return, and with fixed running, transmission and marketing costs – they are unlikely to spend much more than £300k a year on programmes – or less than £40 an hour. Similarly, while quasi-national networks could see revenue rising from £7m a year on 2009 to £20m by 2014, many have access to 20 or more local markets – a spend of £200k per market would yield a total national spend on £4m, which when combined with network programming spend of about £4m – about half current INR levels – would represent a maximum amount of spend given fixed transmission, running and marketing costs.

## **PART B: THE BBC'S CONTRIBUTION TO, AND IMPACT UPON, THE UK RADIO MARKET UNTIL 2014**

### **SUMMARY**

#### **THE BBC'S PERFORMANCE AND DISTINCTIVENESS**

- To a large extent BBC radio and commercial radio services complement each other – commercial radio providing an increasing range of narrowly targeted music services focusing on the 20 to 40 market, while the BBC provides both rich speech networks and more broadly based music networks with a skew towards the over 40s market.
- BBC share has held up at just over 50 per cent over the last 5 years, with weekly reach of the UK population at 66 per cent. While Radio 1 has lost share to an increasing number of commercial rivals, Radio 2 has gained share – especially among the under 55s. The other BBC analogue services have seen their share hold steady over the last 5 years.
- The BBC's popular music based services – Radio 1 and Radio 2 -cover a wider range of tastes, demographics and interests than their more targeted commercial rivals. They have a wider playlist and devote more airtime to live music and UK artists than commercial radio.
- The BBC provides the majority of national and local/regional speech based output, probably spending over nine times as much as commercial radio on this form of programming. The BBC's commitment to new drama and comedy, and magazine, features and documentary programmes is unique in the UK radio market.

#### **THE LIKELY DIRECT RADIO MARKET REVENUE AND COST IMPACT OF EACH CORE BBC RADIO SERVICE TO 2014**

- By 2014, the BBC's five national analogue networks – also simulcast in digital – and its local/national regional services are likely to be taking about 40 per cent of the listening audience.
- The estimated impact of each service on the advertising revenue of the commercial market in 2014 in today's prices – based on a very approximate market elasticity estimate of -2 that only has limited applicability to large scale structural changes - ranges from £5m (Radio 3) through £22m (Radio Five Live) to about £38m (BBC English Local Radio).
- In each case, the hypothetical cessation of a specific BBC service is likely to see some audience leave radio listening altogether and an even higher proportion migrate to remaining BBC services. The listening that does transfer to the commercial sector will only be attractive demographically in some specific cases, and will put downward pressure on the overall price of commercial airtime.
- Reduced cost inflation pressures on the commercial sector from the cessation of BBC services is likely to be limited with even the likely reduction in sports rights

prices partially contingent on how many rival commercial networks or quasi-national networks step into the market. It might also raise the cost of music rights to the commercial sector, or leave the music industry seriously out of pocket.

- The increased revenue to the commercial sector from the withdrawal of BBC services is likely to be spread across several different services and formats within the commercial radio portfolio, and is, therefore, unlikely to transform the economics of any one existing commercial service.

#### **THE IMPACT ON THE OVERALL COMPETITIVE MARKET EQUILIBRIUM**

- While it is possible the commercial portfolio as a whole might shift more towards speech radio and the over 50s if BBC services were withdrawn, and especially if vacated BBC frequency was made available to commercial radio, such services would be very unlikely to be able to match the rich speech and live music commitment of BBC radio. They would still be likely to seek to focus on narrowly segmented parts of the audience rather than aiming to establish broad networks providing for a range of tastes and interests.
- Even if BBC frequencies were allocated to the commercial sector and tough output regulation were applied to try and get the new commercial services to replicate what the BBC had done, it would be very unlikely to produce the depth and breadth of BBC service, would also involve extremely detailed and intrusive regulation on commercial operators, and in most cases would require on-going public subsidy to sustain it.
- While the current strengths of the BBC with the over 50 audience might be said to make it more difficult for the commercial sector to break into this market, the lack of interest from advertisers in this age group until now has probably been a more important factor. In any event, the commercial sector is increasingly likely to target this market with the advent of digital.

#### **OTHER MARKET BROADER ECONOMIC IMPACTS**

- BBC radio makes a significant contribution to the promotion of the successful UK music industry, through its coverage of new and established UK artists, new UK tracks and live music events where it covers half the music festivals in the UK. BBC radio also commissions almost as many new plays per year as the entire UK theatre sector, and is a major developer of new comedy writing talent that often goes on to success in TV and film.
- Through its 5 orchestras and one group of singers, the BBC Proms and its 60 new classical music commissions per year, the BBC is the leading sponsor of live classical music in the UK.

## THE OVERALL SCORECARD

- While the closure of services such as Radio 1, Radio 2, Radio 4 and English Local Radio might transfer a reasonable amount of revenue to the commercial sector<sup>20</sup> – which would most likely be spread across a number of commercial stations and only a proportion of which would be reinvested in programming – all four services do still offer something distinctive to the radio listener and broader market place. With Radio Five Live, National Radio and Radio 3 the increase in commercial revenue would be much less, and again something distinctive would be lost.

### EXHIBIT A

THE 'SCORECARD' BY SERVICE

	INDICATIVE NEGATIVE ANNUAL AVERAGE REVENUE IMPACT* (2006 TO 2014)	COST INFLATION	DISTINCTIVENESS	BROAD IMPACT ON COMMERCIAL PORTFOLIO	BROADER ECONOMIC IMPACT ON OTHER MARKETS
RADIO 1	c£30m	<ul style="list-style-type: none"> <li>• May actually reduce commercial payouts to rights holders</li> <li>• Some increase in presenter costs</li> </ul>	<ul style="list-style-type: none"> <li>• Range of tastes and interests</li> <li>• Wide playlist and live music</li> <li>• News and social action</li> <li>• UK music 'hub'</li> </ul>	<ul style="list-style-type: none"> <li>• May reduce number of segmented commercial services for under 30s</li> </ul>	<ul style="list-style-type: none"> <li>• Major UK music industry sponsor</li> </ul>
RADIO 2	c£32m	<ul style="list-style-type: none"> <li>• May actually reduce commercial payout to rights holders</li> <li>• Some increase in presenter costs</li> </ul>	<ul style="list-style-type: none"> <li>• Range of tastes and interests</li> <li>• Wide playlist and live music</li> <li>• Docs and news</li> <li>• Inter-generational meeting point</li> </ul>	<ul style="list-style-type: none"> <li>• May squeeze commercial 35 to 50 portfolio</li> </ul>	<ul style="list-style-type: none"> <li>• UK music industry sponsor</li> </ul>
RADIO 3	c£3.7m	-	<ul style="list-style-type: none"> <li>• Home of UK arts, culture and performing arts</li> <li>• Major sponsors of classical music</li> </ul>	<ul style="list-style-type: none"> <li>• Small Impact spread over many services</li> </ul>	<ul style="list-style-type: none"> <li>• Arts and classical music developer</li> </ul>
RADIO 4	c£27m	-	<ul style="list-style-type: none"> <li>• New drama and comedy</li> <li>• In-depth journalism</li> <li>• Documentaries</li> <li>• Range and breadth</li> </ul>	<ul style="list-style-type: none"> <li>• Small impact spread over many services</li> </ul>	<ul style="list-style-type: none"> <li>• New writing</li> <li>• Investigative journalism</li> </ul>
RADIO FIVE LIVE	c£18m	<ul style="list-style-type: none"> <li>• Some in sports rights but depends on number of competing commercial services</li> </ul>	<ul style="list-style-type: none"> <li>• In-depth rolling news</li> <li>• Breadth of sport coverage and journalism</li> </ul>	<ul style="list-style-type: none"> <li>• May squeeze commercial speech service</li> </ul>	<ul style="list-style-type: none"> <li>• Sport sponsor</li> </ul>
ENGLISH LOCAL RADIO	c£32m	<ul style="list-style-type: none"> <li>• Some in local journalism</li> </ul>	<ul style="list-style-type: none"> <li>• Home of local journalism</li> <li>• Catchment areas</li> </ul>	<ul style="list-style-type: none"> <li>• Some reduction in number of local commercial services in larger markets</li> </ul>	
NATIONAL REGIONAL SERVICE	c£6m	<ul style="list-style-type: none"> <li>• Some in national events and journalism</li> </ul>	<ul style="list-style-type: none"> <li>• National journalism</li> <li>• Focal point of national culture, events and debate</li> </ul>	<ul style="list-style-type: none"> <li>• Some increase in speech radio content on music services – metropolitan only</li> </ul>	<ul style="list-style-type: none"> <li>• National journalism pool</li> <li>• National arts and culture sponsor</li> </ul>

\*This indicative impact is based on an estimated historic survey based elasticity estimate of -2 which applied to small changes in price and volume – this may not be applicable to large scale changes.

<sup>20</sup> Exactly how much is difficult to discern given the limited applicability of the -2 elasticity estimate to large scale changes in commercial audience share.

## **1. BBC Service Performance and Distinctiveness and the Overall Implications of Commercial Market Developments to 2014**

Before considering the likely impact of individual BBC services on listeners and the commercial radio market by contemplating the effect of withdrawing each service, it is worth assessing the overall performance and distinctiveness of BBC services today and the overall likely implications of the analysis in Part A for distinctiveness going forward.

### **a. Current Performance and Distinctiveness**

The current BBC portfolio complements the commercial radio offering in a number of ways. These include the significant investment in more expensive speech and live music programming, the overall broad reach of BBC services across the whole UK population and the unique role in providing choice and variety to listeners likely to remain in some part underserved by the commercial market – the over 50s and those in rural areas and more remote small towns. BBC services also have no intrusive advertising breaks, and each service covers a broader range of tastes and interests than comparable commercial services targeting similar demographics.

#### ***A Significant Investment in New Radio Programming, Especially Speech Programming***

The analysis in Part A suggested that commercial radio invests about £155m out of its £560m in programming (excluding royalties and rights fees). By contrast the BBC invests about £320m of its £480m apportioned licence fee revenue into programming.

Within speech programming the contrast is even more stark, with commercial radio investing an estimated £40 million versus the BBC's £200m. The BBC employs over 3,000 local journalists and newsroom support staff in the UK across its local TV and radio services.

#### ***Coverage of a wide socio-demographic range across the portfolio***

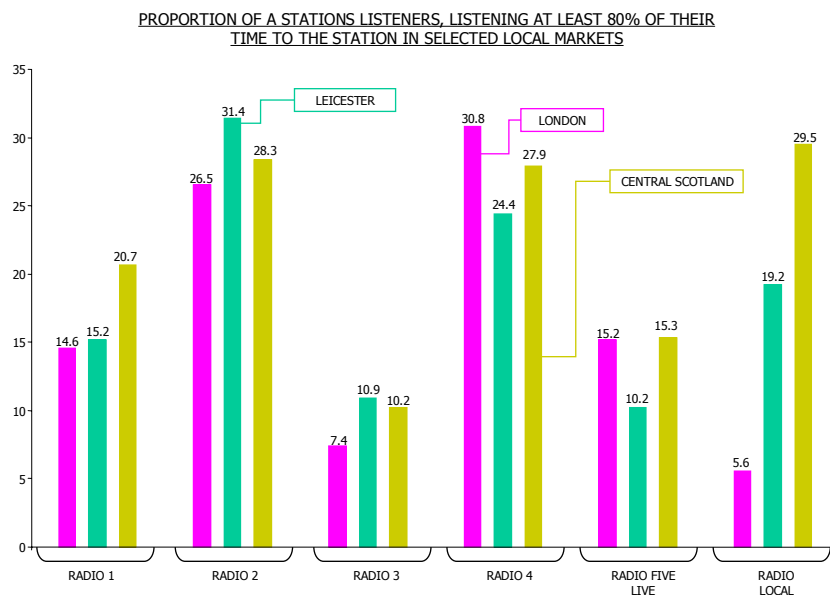
The BBC portfolio covers listeners aged 10 to 80, is broadly balanced between male and female listening and - through its music services, local services and Radio 5 Live - reaches a significant proportion of C2DE's.

Although there are significant overlaps between BBC audiences in individual local markets – most notably between BBC local radio and Radio 2, and Radio 4 and all other BBC services, there is also a significant amount of solus listening (listeners that only listen to a given BBC service) or almost solus listening (listeners spending 80 per cent of their time with a specific station). Solus or almost solus listeners to Radio 4 and Radio 2 tend to account for between 25 per cent and 30 per cent of all listeners to those stations in most local markets <sup>21</sup> (See Exhibit 15).

---

<sup>21</sup> Solus listeners means listeners to a station that listen to no other station – BBC or commercial – in a given week. Similarly, almost solus listener means listeners to a stations that spend less than 20 per cent of their listening time listening to any other station – BBC or commercial - in a given week.

## EXHIBIT 15



This suggests that some BBC services currently play a role in bringing certain listeners into radio from other media and competing activities.

### ***A Broad Coverage of Tastes and Interests within Each Network, Complementing the Commercial Sectors More Segmented Approach.***

Where a BBC service targets a relatively narrow demographic – such as with Radio 1 – the BBC tends to offer a broader range of music types and cater for a broader range of tastes and interests within that demographic than commercial rivals.

Where a BBC service targets a broad range of demographics - such as with Radio 2 or Radio Five Live – it tends to address both the different tastes and interests of the various demographics and offers output that brings them together.

Lastly, even within those BBC services where the output itself is very different from anything the commercial market provides – such as Radio 4, Local Radio and parts of Radio 3 – the range on offer is still broad and diverse.

While the commercial sector is tending to concentrate increasingly on what makes listeners distinct and then super serving their needs, the BBC seems more focused on providing each listener with a range of experiences. These two approaches complement each other – probably giving listeners the best of both worlds.

### ***Extra Choice in Smaller and Rural Markets***

For the 17 per cent of the UK population in radio markets with a choice of five or less analogue commercial radio services (versus the national average of 8 to 9) the BBC offers formats and choices that the commercial market simply does not cover. Many of these

markets only have a “heritage” ILR station targeting 20 to 40 year olds, and a Gold or easy listening service targeting 35 to 50 year olds.

In such markets the BBC offers something to the under 25s through Radio 1 and brings a variety of music and speech services for all those over 40. These rural markets are also likely to have more limited DAB choice than the rest of the UK, implying that the BBC will still be providing these listeners with significant additional choice in 2014.

### ***Radio without Adverts - in The Absence of Subscription Radio***

Spot advertising on radio can be more intrusive than on television. With no viable economic model for pay radio yet, the BBC offers those listeners who want an advert free experience the means to achieve it. The availability of advert free radio might well boost overall radio listening in the UK, attracting people who might otherwise avoid commercial radio altogether.

### ***Promotion of UK talent and Creative Endeavour***

Significant investment in live music, commissioned plays, sketch shows and poetry, new works of classical music plus the commitment to wide music play lists with significant air play for UK artists all currently differentiate the BBC from the commercial sector.

Commercial radio in the UK currently neither has the economic resources to provide much of this output nor the commercial incentives to introduce such output – i.e. incremental costs are greater than incremental revenue.

## **b. The Implications of Market Developments to 2014**

### ***Share of the Core BBC Services Likely to Decline from 52 to 40 per cent by 2014, with Reach Declining More Slowly from 66 per cent to just below 60 per cent.***

With commercial radio having a much greater share of digital capacity, and the likely impact of new digital BBC services on some of the established networks, the combined audience share of the core services is likely to decline to just under 40 per cent in 2014, from the current level of 52 per cent.<sup>22</sup>

Digital listeners are, however, likely to listen to more stations per week than current analogue listener patterns, which should help keep core BBC service combined reach at about 60 per cent.

### ***Differential Vulnerability to Increasing Commercial Choice and Competition***

Reviewing the performance of the BBC services across seven local radio markets with different degrees of commercial choice and competition suggests that some are more vulnerable than others (see Exhibit 16). While Radio 1 and BBC Local/National radio<sup>23</sup> tend

---

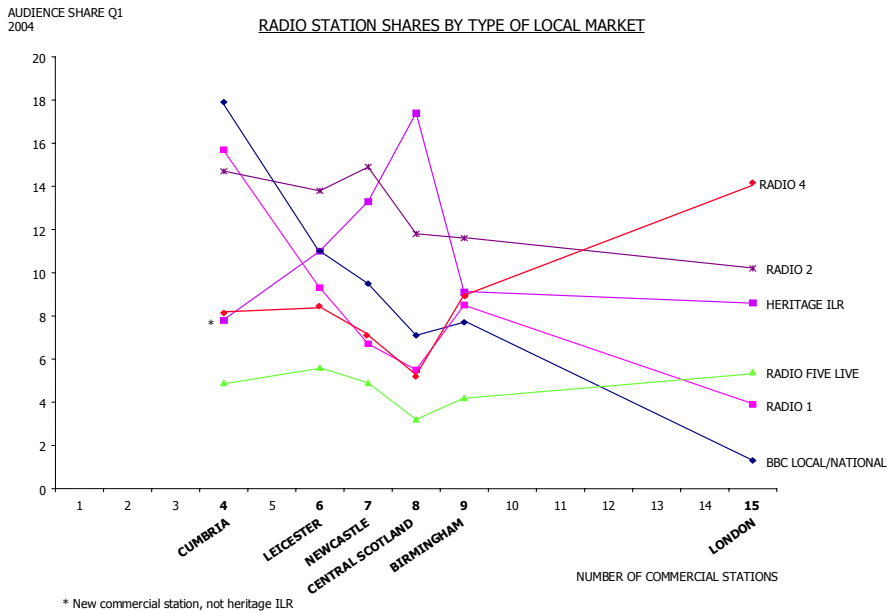
<sup>22</sup> BBC digital only services currently obtain about 0.7 per cent of all listening which could rise to 3 per cent by 2014 – so overall by 2014 the BBC core services would have 39.5 per cent, BBC digital services 3 per cent and all commercial services 57.5 per cent.

<sup>23</sup> Actually, the fall off in local/National BBC radio share with competition is not that great. The much lower share in London is due to the fact that London – uniquely in the UK – has a local speech, news and phone in service – LBC.

to lose out from higher levels of commercial competition currently, Radio Five Live's performance is hardly impacted at all, and Radio 2 suffers a modest decline.

Over the next 10 years, it is likely that Radio 1, Radio 2 and Radio Five Live will suffer the most significant audience erosion as the commercial sector widens its choice of music formats for the under 35s and extends the range of services it offers to the 35 to 50s.

**EXHIBIT 16**



**Some Areas of Differentiation May Decrease...**

With the commercial radio sector expanding the range of its service to cover the 10 to 50 age group with occasional outreach to the over 50s, the BBC's role in uniquely serving the underserved audience groups may reduce.

The commercial sector is also likely to increase its speech output, partly to attract the 35 to 50 audience.

**... But Some Will Increase**

However, despite a likely increase in speech/music mix commercial services, the BBC's commitment to speech radio – especially higher cost built speech radio – is still likely to be markedly different from the market place.

The increased segmentation of the commercial radio market, and the potential pressure on the old heritage ILR economic model is likely to leave the BBC's broadly based networks aimed at a wide range of tastes and interests even more differentiated from the commercial market place.

The BBC's commitment to local speech programming, local features programming and national news from a local perspective is likely to remain fairly unique in the UK market.

The BBC's commitment to new and live UK music is unlikely to be replicated by the commercial sector.

## **2. The Framework for Assessing the Contribution and Impact of BBC Services.**

### **a. The Service-by-Service Impact Analysis**

Each BBC service has been reviewed in turn using three broad criteria. First, how exactly does each BBC service currently differ from those offered by the commercial sector. Second, what might be the direct impact on the current commercial sector's advertising revenue and costs if the BBC service was to cease broadcasting – either in the short term in 2006 or in the longer term in 2014. Third, how might the whole commercial portfolio and equilibrium adjust if a BBC service ceased broadcasting.

In assessing the direct impact of a specific closure of a BBC service we have estimated the likely audience that might shift to the commercial sector as opposed to other BBC services or out of radio completely. We have based this estimate on the current level of solus listening to BBC services (i.e. the proportion in listeners who listen to no other radio services in a week) and the pattern of overlap with other BBC and commercial services among those listeners that do tune in to other services.

In assessing the likely impact of this shift in audience to the commercial sector on its advertising revenue we have used the rough advertising elasticity estimate of  $-2$  described in Part A, but then adjusted the resulting advertising revenue estimate to take account of the demographics of the shifting audience.

Given the likely scale of any shift in commercial audiences that might result from the closure of a BBC service, the past behavior of the UK radio advertising market probably only provides us with a very broad view of the likely impact on revenue. While we have used an elasticity of  $-2$  for the analysis in this section, given that this is only a rough estimate itself and that it probably only applies to small changes in commercial listening, the resulting numbers need to be interpreted as broadly directional only.

In assessing the impact on the general commercial market equilibrium we have tried to suggest what might happen in three circumstances. First, if the BBC frequency remained unused. Second, if the BBC frequency was reallocated as an analogue frequency to the commercial sector. Third, if the BBC frequency was allocated as a new digital multiplex perhaps offering about 8 new commercial digital services to the average UK listener. In each case we have given specific attention to the degree to which the commercial market might start to provide some of the more distinctive current output of the BBC.

In determining the likely commercial market response to a BBC closure it has been important to distinguish between the likely response of a purely commercial market and that of a heavily regulated yet commercially funded market.

The current pattern and structure of the UK's commercial radio markets is as a result of a managed licensing regime operated by the IBA, then the Radio Authority and now OFCOM. In deciding on the likely evolution of the commercial sector should the BBC analogue services be withdrawn in whole or in part, one has to decide what obligations, if

any, might be put on the commercial sector to replicate what the BBC does and, more importantly, how sustainable or enforceable those obligations might be.

#### **b. The Broad BBC Portfolio Impact**

In reviewing the broad impact of the whole BBC portfolio, we have not only set out how the combination of BBC services differs from the commercial offering, and what the overall impact on commercial revenue and costs might be, but we have also assessed the impact BBC core radio services have on broader cultural and creative activities in the UK and on the take up of digital radio.

### **3. CONTRIBUTION AND IMPACT BY SERVICE**

#### **a. Radio 1**

##### **i. Performance and Distinctiveness**

Radio 1 tries to cover a broader range of music tastes for the 15 to 24 audience with a greater emphasis on new UK and live music than its commercial counterparts, and with a significant amount of factual, news and social action programming aimed at its core audience. Its broad approach to the market has meant it has suffered in share terms more than reach as the commercial market chooses to concentrate on super serving narrower sub-segments of the listening market.

##### ***A Declining Share but Maintaining High Reach Among 15 to 24 year olds***

Radio 1 obtains a 7.5 per cent share of all listening in the UK and reaches about 10 million people or almost 20 per cent of the UK population. Share has fallen from about 10 per cent back in 1999 as the availability and number of commercial services focused at the under 30s has increased.

The impact of commercial radio choice on Radio 1 share can be seen by comparing its share across different local UK markets with different numbers of commercial stations. Share ranges from just 3.9 per cent in London to 15 per cent in Cumbria. (See Exhibit 16 again).

Radio 1's audience focus is on the 15 to 24 year old age group where the station achieves its highest share of age group listening across the UK at 20 per cent – down from 26 per cent in 1999. The station's reach to share ratio has increased over the last 5 years suggesting it still offers something to a large number of listeners in the target age group even if they are choosing to spend more time listening to other services. (See Exhibit 17).

## REACH SHARE RATIO OF UNDER 35 FOCUSED MUSIC SERVICES IN LONDON

	REACH	SHARE	RATIO
RADIO 1	12.9	3.9	3.3
CAPITAL FM	22.7	8.6	2.6
HEART FM	17.8	7.0	2.5
KISS	13.9	4.7	2.95
XFM	5.2	1.7	3.1

### ***Achieving Outreach to under 15s and over 25s, even in Very Competitive Markets.***

Even within the very competitive London market, with a number of relatively well funded commercial stations, Radio 1 tends to be relatively popular across the whole 15 to 30 age range while the commercial services either focus older – such as Capital FM and Heart – or on a narrower age group and/or gender group – as with Kiss, Choice and Xfm.

### ***Resisting the trend to Format Segmentation and Attempting to Appeal to a Wide Range of 15 to 24 Age Group Music Tastes***

In markets where there exist fairly focused dance/RnB stations such as Birmingham and Newcastle, Radio 1 tends to lose the younger female audience to these services. Where there exist both dance/RnB and indie/rock stations – such as with Kiss and Xfm in London – Radio 1 tends to be squeezed by both services but ends up with a broader gender mix than either rival service by trying to cover a range of music styles.

Among commercial radio stations concentrating on the 15 to 24 market across the UK, almost all focus on a specific music type at the expense of another. Only Beat FM in Central Scotland tries a similar strategy of covering a spread of 15 to 24 year old tastes due to the absence of a focused RnB/dance station or an indie rock station.

### ***A Playlist Concentrating on New UK and Live Music, Even During Daytime***

Unlike Beat FM - or indeed any other commercial service - Radio 1 provides large amounts of air play to new UK and live music – especially during daytime. Those commercial stations that do get near to Radio 1's commitment to new UK and live music – such as Xfm – play more of this music outside daytime and repeat the same tracks and artists more often.

### ***Providing a "Meeting Point" for New UK Music Movements and Talent***

Radio 1 is, therefore, the only service that achieves three objectives simultaneously : catering for a broad range of music tastes; giving a great deal of airplay to new UK and live music; and, spreading its airplay across a large number of tracks and artists in any one day.

Radio 1 therefore tends to act as a "meeting point" for different music tastes and new music trends. This contrasts with the commercial sector's current tendency to compartmentalize tastes and interests into readily identifiable formats and brands.

### ***Social Action and Targeted News for the Elusive 16 to 24 Age Group***

Radio 1 promotes a number of social action campaigns and supplies a tailored national news service all aimed at the generally hard to reach 16 to 24 age group.

## **ii. Indicative Direct Revenue and Cost Impact**

### **Audience Substitution**

Radio 1's current share of 7.5 per cent would be likely to fall to about 7 per cent by 2006 and 5 per cent by 2014 as digital brings the introduction of a likely new pop network and as dance/urban and indie/rock stations expanded across the UK as quasi national networks.

Radio 1's older audience is currently competed for by heritage ILR stations like Capital FM and Virgin. It faces competition for its male audience from the likes of Xfm, and for its younger and generally more female audience from stations such as Kiss and Galaxy. However, there is significant Radio 1 overlap with other BBC services, most notably Radio Five Live and to a lesser extent Radio 2 and Radio 4 at the older end. In addition, both 1Xtra and BBC 6 Music's audiences overlap with the current Radio 1 audience.

Of the 5 per cent share the network is likely to have by 2014, about 3.5 per cent would be likely to go to the commercial sector should it cease to exist with about 0.5 per cent likely to be lost to radio entirely as listeners sought out more new music through internet downloading activities while the remaining 1 per cent transferring to other BBC services - mostly 1Xtra, BBC 6 Music and Radio Five Live. With no new services introduced the commercial audience would likely split fairly equally among dance/urban, indie/rock, heritage ILR stations and any digital pop/dance station (such as the current Core service on Digital One).

In 2006, of the 7 per cent share taken by Radio 1, about 5.5 per cent would transfer to the commercial sector, with 0.5 per cent lost to radio, and 1 per cent transferring to other BBC services.

### **Revenue Impact**

With advertising revenue likely to be £600m in today's prices by 2006, and commercial share likely to have risen to 50 per cent, the transfer of 5.5 percentage points is likely to

represent a 11 per cent increase in impacts. If an elasticity of  $-2$  is used this would mean a price drop of 5.5 per cent and an overall revenue increase of 5.5 per cent, or £31.5m.<sup>24</sup>

With advertising revenue likely to be £1.2 billion in today's prices by 2014, and with total commercial share at about 57 per cent, a 3.5 percentage point transfer would represent a 6 per cent increase in commercial impacts, With an assumed overall elasticity of demand for advertising of  $-2$ , this would lead to 3 per cent increase in income – or £36m in today's prices by 2014.

However, the pattern of gain in share by the commercial sector might suggest slightly less than £31.5m in 2006 and £36m in 2014 is gained in revenue by the commercial sector. Although the demographics of the stations gaining the audience are likely to focus on the relatively valuable 15 to 35 audience, much of the audience will be divided into fairly targeted niche services of value to targeted national advertisers rather than local or broad national advertisers.

This might mean that the revenue gain is slightly less than proportionate, with perhaps a £28m gain in 2006 and a £32 million gain in 2014.

With no change in the commercial portfolio of analogue and digital services, Radio 1's listening share transferring to the commercial sector would probably be divided up between a series of younger audience niche services such as dance/RnB stations, indie/rock stations, pop stations and contemporary hits/adult contemporary stations. Some of the audience would also transfer to the heritage ILR stations.

This potential revenue gain of £32m would be likely to be spread across many formats and several stations within each format type.

### **Cost Inflation**

The withdrawal of Radio 1 would be unlikely to have a significant impact on the costs of the commercial sector. While there might be a little less competition for star name DJs, there is likely to be a fair amount of competition between the various quasi national networks focusing on the 15 to 34 year old market in any case.

There might, however, be increased pressure from the various rights trade bodies to increase the contributions made by the commercial sector should the BBC cease to be active in the market.

Radio 1 pays about £10m a year in music copyright payments. The extra advertising revenue transferring to the commercial sector is about £30 million a year over the period analysed. Commercial radio pays between 5 and 10 per cent of its advertising revenue to music copyright agencies – this would equate to £1.5m to £3m out of the extra revenue – leaving copyright holders out of pocket by at least £7m a year. This might well lead to calls for the proportion of commercial revenue going to music copyright to increase.

---

<sup>24</sup> Use of the  $-2$  elasticity is only very indicative, elasticity of larger scale changes envisaged here may well be different from that inferred from historic or current small scale changes in commercial listening hours.

### **iii. General Impact on the Commercial Market Equilibrium to 2014**

If Radio 1 were to cease broadcasting the market would be unlikely to respond by creating another Radio 1 type station with a broad coverage of music types, and a focus on male and female listeners with the 15 to 24 age group but with outreach to the late 20s.

Even if the analogue frequency was reallocated to a single commercial service, that service would have to be heavily regulated to produce the kind of output Radio 1 currently produces. The economic incentives of such a service would always be to narrow the range of programming, narrow the playlist, drop the social action items and documentary programmes.

With a single analogue frequency a commercial service would probably focus more on the heartland commercial audience of 25 to 35 year old listeners, and even if they were persuaded to focus on the 16 to 24 market, would certainly narrow the playlist and programme range.

If the frequency was not allocated to any new stations – digital or analogue – then the commercial market would be unlikely to change at all, each individually segmented service would pick up a proportion of Radio 1's audience. If the frequency was allocated to 8 new digital services, then the commercial market would be likely to segment even further, with each station probably having an even lower programme budget than previously. While revenue might increase by about £30m a year, the fact that this revenue was being shared by all existing commercial digital services plus another 8 new services, would be likely to reduce the average revenue gain per service to minimal levels.

This would be in stark contrast to Radio 1's current ability to provide large amounts of live UK and new music all within a service reaching a relatively large audience.

## **b. Radio 2**

### **i. Performance and Distinctiveness**

#### ***Recently Increasing Share Due in Part to Aging UK Population***

Radio 2 has grown its share of audience from 12 to 15 per cent over the last 5 years, while its overall reach has increased from 20 to 26 per cent.

All BBC services with a traditionally older audience profile have posted strong share performance over the last 5 years despite increased choice in the commercial sector. Radio 2 has probably benefited more than most from the disproportionate growth of the 40 to 55 age group over the last 10 years – a cohort who grew up with popular music in the late 60s and 70s - and the migration of Radio 1 listeners to Radio 2.

#### ***Strong Performance within the 35 to 45 age Group is Also Connected to Commercial Radio's Current Weaknesses in this Area***

However, even allowing for this general trend, the marked increase in share and reach with 35 to 45 year olds over the last 5 years – with share growing from 10 to 16 per cent and reach from 17 to 28 per cent – has been exceptional.

Commercial radio's traditional service for the 35 to 50 year age group– the Gold format – only has access to a medium wave analogue frequency while newer formats such as Jazz, Easy Listening and speech/adult contemporary mix, have only been introduced in a handful of analogue radio markets.

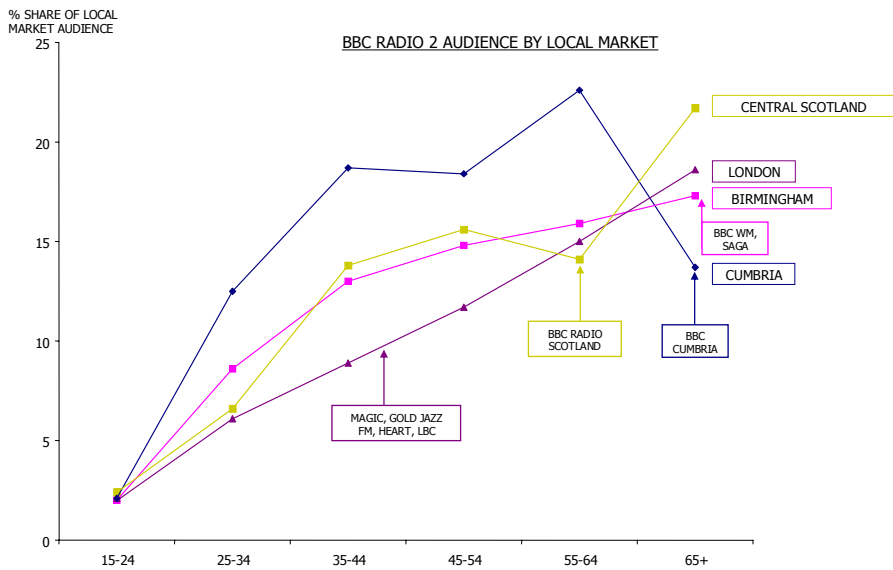
**The Station Tends to Lose Share Among the Under 50s in Markets with Stronger Commercial Easy Listening and Music/Speech Propositions**

Where there exist strong speech/music mix stations – such as Real Radio for example in South Wales and Central Scotland – Radio 2's audience share increase among the under 50s since 1999 has been less than the average 5 percentage point gain across the UK as a whole, especially with the female audience.

The Radio Authority only started to award licenses to mixed speech and music services – usually on a regional basis – in the more recent licensing rounds – and even then has not rolled them out in all major markets. Digital is likely to change this situation.

Furthermore, in markets where there are a wide range of commercial services focusing on easy listening music, speech and a speech/music mix, Radio 2 tends to lose share among the under 50s. In London, where listeners can access Magic, Capital Gold, Jazz FM and LBC, Radio 2's share of the 35 to 50 audience is about 5 percentage points lower than the national average. (See Exhibit 18).

**EXHIBIT 18**



**Wider Playlist and Greater Variety of Music Types Than Comparable Commercial Stations With A Commitment to Live Music**

Compared with commercial adult contemporary and easy listening stations aimed at the over 35s, Radio 2 plays more individual tracks and covers a broader range of musical

periods than these stations<sup>25</sup>. It also gives more airplay to a broader range of music types including those not currently covered well by the commercial market such as country/folk, gospel, traditional jazz etc.

Radio 2's commitment to live music and events – about 70 tracks a week, is far greater than any commercial radio station.

### ***Significant Proportions of Speech Output Both Within Music Programmes and As Standalone Documentaries***

Just over 40 per cent of Radio 2's output is speech with both speech items, political interviews and social action campaigns within music based programming formats and separate documentary (150 hours a year), comedy and religious strands.

While commercial stations such as Real Radio and Saga do also have over one third speech content, they do not have any built documentary or comedy speech programming and little political or social action content within their music programming.

### ***An Inter-generational Meeting Point with Music and Speech Appealing to Listeners from 35 to 75***

While those commercial stations targeting the over 40 market with a mix of speech/music tend to concentrate on a specific part of that market ( Real Radio 35 to 55, Saga FM from 50 to 65) only Radio 2 aims and succeeds in bringing a broad range of the over 40s to a single service.

This is reflected in the speech and music policy of the different stations with Real Radio focused on music from the 80s onwards, and Saga FM on music earlier than 1970.

With at least three digital stations planned to target the 35 to 55 year old Rock market, and 4 digital easy listening stations the commercial sector seems poised to segment the over 40 market in the same way they have previously segmented the under 35 market.

## **ii. Indicative Direct Revenue and Cost Impact**

### **Audience Substitution**

Radio 2's current share of 15.3 per cent is likely to decline to about 11 per cent by 2014. With the likely growth of quasi-national and national easy listening stations aimed at the 40 to 50 year old market through a combination of analogue and digital distribution and the likely growth of BBC 6 Music, a greater proportion of this share is likely to come from over 50 listening in the future as the network loses disproportionately among the under 50s.

Radio 2 has a significant number of solus and almost solus listeners at the moment. Even in London where there is a wide choice of easy listening stations and a local speech station, solus and almost solus listeners to Radio 2 account for 30 per cent of all listeners (see Exhibit 18.)

Radio 2 also enjoys significant overlap with Radio 4, Radio 5 Live and Local/National Regional radio across the UK (see Exhibit 19)

---

<sup>25</sup> Based on playlist research by Intelligent Media commissioned by the BBC.

**EXHIBIT 19**

AVERAGE OVERLAPS IN BBC SERVICES BY LOCAL MARKET SURVEYED (London, Birmingham, Central Scotland, Newcastle, Southampton, Leicester, Cumbria)

		SERVICE											
		RADIO 1		RADIO 2		RADIO 3		RADIO 4		RADIO FIVE LIVE		LOCAL/REGIONAL	
		HIGHEST	LOWEST	HIGHEST	LOWEST	HIGHEST	LOWEST	HIGHEST	LOWEST	HIGHEST	LOWEST	HIGHEST	LOWEST
OVERLAP WITH:	RADIO 1	-	-	33.6	12.3	30.1	6.0	20.8	8.2	34.9	15.9	20.6	13.8
	RADIO 2	31.6	18.5	-	-	60.8	28.3	46.3	29.3	44.8	26.2	39.9	24.9
	RADIO 3	4.7	3.4	12.2	4.8	-	-	23.8	14.3	11.1	2.7	15.1	2.4
	RADIO 4	15.7	7.4	37.3	19.6	74.1	50.6	-	-	35.3	19.8	38.9	17.7
	RADIO 5 LIVE	22.6	7.7	20.5	12.1	26.6	7.0	25.8	18.3	-	-	22.1	17.4
	LOCAL/REGIONAL RADIO	20.8	6.9	39.7	7.3	52.5	10.9	47.3	7.8	50.7	8.2	-	-

If Radio 2 were to cease broadcasting its audience would be likely to stay with the BBC for much of their speech requirements. Some of the solus listeners might also move away from radio towards TV viewing and other activities during the day. Of the 11 per cent share likely to be claimed by Radio 2 in 2014, only about 7 per cent is likely to transfer to the commercial sector.

**Revenue Impact**

A 7 per cent share transfer to the commercial sector, represents a 12 per cent increase in the number of commercial impacts in 2014 (commercial share would go from 57 per cent to 64 per cent). An increase in commercial impacts of 12 per cent would - other things being equal - convert into a 6 per cent increase in advertising revenue assuming a market elasticity of -2.<sup>26</sup> This would equate to £72m in 2014.

However, current analysis suggests that only Radio 2's under 45 audience would have a value to advertisers near to prevailing market rates, most of the audience over 45, and certainly almost all of the audience over 55, would sell at a significant discount to the market average price. Currently about 60 per cent of Radio 2's audience is over 45 and 40 per cent is over 55, and by 2014 this is likely to have increased due to greater competition for the 35 to 50 audience. By 2014, as much as 60 per cent of Radio 2's audience could be over 50.

While 40 per cent of the transferring Radio 2 audience to commercial radio may be sold at average market prices, 60 per cent of the audience is likely to be sold at an 80 per cent

<sup>26</sup> Again, it is worth noting that the -2 estimate is based on historic small scale changes in commercial audience share not the large scale changes envisaged here.

discount. Applied across all transferring listening hours the discount would be about 50 per cent implying that the extra value to the commercial sector would be about £36m in 2014.

If Radio 2 were closed down in 2006, then its share is likely to be about 14 per cent, of which about 9 per cent would transfer to the commercial sector. This would represent about an 18 per cent increase in commercial impacts (commercial share going from 50 per cent to 59 per cent).

This would convert to a 9 per cent increase in advertising revenue for the commercial sector, or £54m at today's prices. However, a 50 per cent discount is likely to apply to the demographics transferring (although Radio 2 will have retained more listeners under 45 by 2006 compared with 2014, the discount for listeners over 55 is likely to be higher than in 2014, by which time we have assumed advertisers will be slightly more keen on the over 55 audience than today).

Therefore, the likely transfer of value to the commercial sector is likely to be £27m.

This £27m is likely to be shared by a number of commercial services focusing on the 35 to 50 market, as well as local and national digital services aimed at the over 50s.

### **Cost Inflation**

The withdrawal of Radio 2 would be unlikely to have a significant impact on the costs of the commercial sector. While there might be a little less competition for star name DJs, there is likely to be a fair amount of competition between the various quasi national networks focusing on the 35 to 50 year old market in the future.

Again, as with Radio 1 above, there might be increased pressure from the various rights trade bodies to increase the contributions made by the commercial sector should the BBC cease to be active in the market. Again Radio 2 pays about £10m a year to music rights bodies while the transfer of revenue would only translate to £3m of payments from the commercial sector at most.

### **iii. General Impact Upon the Commercial Market Equilibrium to 2014**

If Radio 2 were to cease broadcasting the commercial market would be very unlikely to produce a service with such a wide target age group audience, variety of music types and tastes and with factual and documentary programming. Overall the market might increase its provision of services for the 35 to 50 age group - with a greater role for speech/mix services, and it also might produce a strong service - but based on a fairly narrow playlist - for the over 50s.

The allocation of the analogue frequency to a rival required to target a similar audience would probably result in a service which either targets the 35 to 50 market, or the over 50s market – but not both. While the service might have a relatively high proportion of speech its playlist would be narrower, coverage of live music would be minimal, the social action and political element of speech output would reduce and the presence of documentaries would also be minimal.

With no frequency transfer, the commercial market might shift its portfolio more towards a speech/music mix for the 35 to 50 market – as far as their licenses allowed them, but would also seek to segment that audience into different music tastes of gender preferences.

With frequency allocated to 8 new digital services, this would fragment revenue more than it tended to increase total revenue. While the overall shift in portfolio towards speech/music mix for the 35 to 50 age group might be greater – as new services might have greater flexibility to target this market than existing ones - overall revenue would be more fragmented, leaving each service with a lower programme budget.

This would be in marked contrast to Radio 2's ability to reach a wide range of age groups – including the over 50s - with a range of different live and recorded music together with significant amounts of news, documentary and debate.

## **c. Radio 3**

### **i. Performance and Distinctiveness**

#### ***Steady Audience Share and Reach, with An Old and ABC1 Audience Getting Slightly Older and More ABC1.***

Radio 3's share has been steady at about 1.2 per cent over the last five years with a reach of about 4.3 per cent. 70 per cent of the network's listening hours are among the over 55s, while 75 per cent of listening hours are from ABC1s. Over the last 5 years its audience has become slightly older and more ABC1.

#### ***A Wide Range of Classical Music mixed with Jazz and World Music – With a Significant Commitment to Live Performance and New Works***

Radio 3's classical music covers pieces right up to the present day, together with significant amounts of new and cutting edge Jazz and World Music. Its music repertoire is more modern, more challenging and more varied than Classic FM, with a greater commitment to covering live performance and a unique commitment to commissioning new works.

#### ***Trying to Enhance the Understanding and Involvement with Classical Music, and Exposure to the Arts and Cutting Edge Dramatic Performance.***

The network commissions a number of music based documentaries as well as series covering art, poetry and performing arts. Its remit within dramatic works is to cover some of the more challenging classical pieces as well as modern and new work.

### **ii. Indicative Direct Revenue and Cost Impact**

#### **Audience Substitution**

Radio 3's audience share is likely to remain at the 1.3 to 1.4 per cent level over the next 10 years if there are no dramatic schedule changes. The network has a relative low number of solus listeners but very high levels of overlap with Radio 4 and Radio 2. The major commercial services listened to by the current audience are Classic FM, Jazz and Saga.

If the network closed down, about 10 per cent of listeners would be likely to reduce their radio listening significantly, but of the remaining 90 per cent about half might migrate to other BBC services, leaving about 0.6 per cent share migrating to the commercial sector.

### **Revenue Impact**

0.6 per cent of share equates to 1.2 per cent of commercial impacts in 2006 and about 1 per cent in 2014. At average market prices this is likely to entail a transfer of £2.8m in 2006 rising to £6m in 2014. But the socio-demographic profile of Radio 3's audience probably suggests a discount of 20 per cent on the market price – with only Radio 3's under 45 audience and its AB audience over 50 really being of value to advertisers.

The main beneficiaries of this share and revenue transfer are likely to be services such as Classic FM, Saga/Primetime and Jazz FM.

### **Cost Inflation**

The withdrawal of Radio 3 is unlikely to have any cost inflation reduction benefits to commercial radio. While Classic FM might secure access to any live event more cheaply, there would be fewer orchestras and events in the UK with the BBC withdrawing from the market. This might eventually reduce the overall supply of events, pushing Classic FM's costs up again.

Again, copyright agencies might want a greater contribution from Classic FM if Radio 3 withdrew from the market, although in this case given that Classic FM might be the only classical music service, it would be more likely that the music rights owners would end up out of pocket.

### **iii. General Impact Upon the Commercial Market Equilibrium to 2014**

The commercial portfolio is unlikely to adjust in reaction to the closure of Radio 3, and would certainly not adjust to come up with a replacement for Radio 3 – even if heavily regulated to do so. Any commercial version of Radio 3 would have to be subsidized heavily, and even then would be likely to reduce the highest cost and/or least cost effective of Radio 3's obligations.

If Radio 3's frequency were allocated to the commercial sector for any use – then it would be likely to produce a station more akin to those mentioned above in the Radio 1 and Radio 2 sections – but this time competing for the still existing Radio 1 and Radio 2 audience.

If Radio 3's frequency were turned into 8 digital services, then it would simply expand the number of services focused on the under 30 or 35 to 50 music or music/speech market.

## **d. Radio 4**

### **i. Performance and Distinctiveness**

#### ***Solid Audience Share Performance Over Last 5 Years***

Radio 4 has managed to maintain an 11 per cent share over the last 5 years, with fluctuations being linked to major news events such as the war in Iraq. Radio 4's share is highest in London and the South East, outside of London and the South East in England share tends to reduce slightly with the amount of competition, while in the National regions share tends to be lower as the relevant National service tends to pick up some of Radio 4's audience demographic.

#### ***An In-depth News And Analysis Service***

News and current affairs accounts for 45 per cent of all Radio 4 output. Radio 4 covers UK and international news and parliamentary affairs with both the reporting of breaking news and in-depth analysis, commentary and interviews.

#### ***Investigative Journalism and Magazine Programming***

Radio 4 is the main supplier of investigative journalism on the radio with strands such as *File on Four* and *You and Yours*. The network also provides regular magazine programmes such as *Women's Hour* covering a wide range of contemporary issues with interviews, discussions and reports. Strands such as *Feedback*, *the Moral Maze*, *Any Questions* and *the Commission* are there to encourage debate and discussion on major issues.

#### ***Dealing With Popular Culture, Science and Religion***

Strands such as *Front Row*, *Back Row* and the *Saturday Review* give extensive coverage and access to the worlds of culture, arts and entertainment, while specialist factual strands exist for science and religion.

#### ***A Commitment to Drama and Comedy***

Radio 4 provides 2000 hours of drama and readings a year, adapting 70 books a year for reading – covering well known and lesser known works – and commissioning over 300 new plays a year. The network also broadcasts over 500 hours of comedy, satire, quiz shows and sitcoms a year. While *Oneword* in the commercial sector has broadcast readings and archive comedy, Radio 4's commitment to new works is unmatched in commercial radio.

### **ii. Indicative Direct Revenue and Cost Impact**

#### **Audience Substitution**

Radio 4's current audience share is 11 per cent, tending to perform more strongly in London and the South East – gaining 14 per cent of all listening – and less well in the National regions where the BBC's national services often gain share within Radio 4's heartland demographics.

Radio 4 is likely to lose relatively little audience by 2014, with some listening migrating to the BBC's new digital service BBC 7 and to the World Service in digital homes. With an ageing and more educated population over the next decade, the network may well still account for 10 per cent of all listening by 2014 although there is a risk that it will lose more of its younger audience to Radio Five Live. Radio 4 is unlikely to lose any share by 2006, leaving it with an 11 per cent share in that year.

Between 25 and 30 per cent of Radio 4's listeners across various local markets are solus or near solus listeners, and it has significant overlaps with BBC local/national radio, Radio 2 and Radio Five Live.

Should Radio 4 cease broadcasting, a significant proportion of its audience is likely to move either to other services such as Radio Five Live or Radio 2, or to reduce their overall radio listening given that no other radio station produces the kind of non news programming produced by Radio 4.

Of the 10 per cent share in 2014, only about 3 per cent would be likely to transfer to the commercial sector. A very similar amount of share would be likely to transfer in 2006.

### **Revenue Impact**

An 8 per cent increase in commercial impacts in 2006, would equate to a 4 per cent increase in commercial revenue – which would be worth £24m with no discounts or premiums. By 2014, a 7 per cent increase in commercial impacts would cause a 3.5 per cent increase in revenue – about £42m.

About 60 per cent of Radio 4's audience is over 55. However, about 80 per cent of the audience is ABC1, and about 40 per cent is AB social group. Perhaps most importantly about 10 per cent of the audience are under 45 ABs while about 36 per cent of the audience are older C1C2DEs. While Radio 4's older non AB audience is likely to sell at a significant discount to market rates, its under 45 AB audience is likely to sell at a significant premium.

If we assume that the younger AB's sell at a 100 per cent premium, the older C1C2DEs sell at an 80 per cent discount, and the rest of the audience sell at market rates, then the blended average rate would be about 80 per cent of the market rate. This would yield £19m of revenue in 2006 and £34m in 2014.<sup>27</sup>

### **Cost Inflation**

The only possible benefit to costs of the commercial sector if Radio 4 ceased would be if the archive then became available to third parties at low prices. However, as no new archive would be created this effect would be short lived and in any event the main determinant of archive costs is clearing the rights with the artists and writers involved.

One might argue that the significant reduction in news resources resulting from the withdrawal of Radio 4 might reduce the costs of news wire services and journalists to the commercial sector, but Radio 4 is probably not in the same labour market as commercial radio for journalists. The BBC's withdrawal from the news wire market might therefore actually push costs to other users up.

---

<sup>27</sup> Again the -2 estimated elasticity might well not apply to such large scale changes in commercial audiences.

### **iii. General Impact Upon the Commercial Market Equilibrium to 2014**

The impact of the closure of Radio 4 on the market would be similar in kind to Radio 3, with the release of its frequency having more impact than the direct cessation of the service. The cessation of the service might encourage some of the speech/music mix stations to increase their output speech output – even their news and current affairs – but little more than this.

If the frequency was reallocated as 8 digital services it might be more likely that not that a news and current affairs network would be one of them. If the analogue frequency was reallocated, then commercial operators would probably opt for a speech/music mix service with perhaps a greater emphasis on news and current affairs than otherwise might be the case.

If the analogue frequency was reallocated with a stipulation that it must be a speech service aimed at the over 35 ABC1 audience, then it would probably be a news and current affairs networks with occasional readings and magazine shows – but with no documentaries, investigative journalism, new drama shows of drama adaptations, or new comedy.

#### **e. Radio Five Live**

##### **i. Performance and Distinctiveness**

###### ***Steady Audience Share Equally Dependent on News and Sport and Skewed Male 35 to 55***

Radio Five's share has remained at between 4.5 and 5 per cent share over the last 5 years fluctuating between these levels due to individual sporting events and the incidence of major news stories.

The audience skews male and is centered on the 35 to 55 age group. The audience is more ABC1 than the population in general although much less so than Radio 4.

News and current affairs makes up about 70 per cent of the schedule and accounts for 50 per cent of the listening. Sport makes up about 30 per cent of the schedule and accounts for the other half of listening, with live sporting events gaining about twice the normal share of listening when broadcast – about 9 per cent.

The younger audience tends to be brought in by the sport but often also samples the news and current affairs programming.

###### ***A Rolling News Service with Depth and Breadth of Coverage with Feedback and Investigative Reporting***

Radio Five Live provides a rolling news services drawing on specialist correspondents, regional correspondents from around the UK and the BBC's international network or reporters.

The station also has phone in and discussion programmes similar in format to commercial rivals with some investigative strands.

## ***An Extensive Coverage of the National Sporting Calendar, Bringing Exposure to Minor Sports***

Radio Five Live covers most of the major UK sporting events – except cricket which is on Radio 4 Long Wave – and Formula 1 which is on TalkSport (although the practice sessions are on Radio Five Live).

The station also covers a large number of minority sports with both live coverage and news and scores.

## **ii. Indicative Direct Revenue and Cost Impact**

### **Audience Substitution**

Radio Five Live's current audience share is about 5 per cent, with around half its audience coming from news and current affairs, which accounts for about 70 per cent of its output, and about half its audience coming from live sports coverage and sports magazine and phone-in programmes, but which accounts for just 30 per cent of its output.

The 2.5 per cent share that goes to news and current affairs programming is likely to only erode by about 0.5 per cent over the next 10 years, as the commercial sector is unlikely to launch a specialist 24 national hour news and current affairs service with DAB coverage (i.e. a bulletin based service like the now defunct ITN service might re-appear on digital TV distribution systems).

The audience for the sports service might erode more substantially, as it is likely that either TalkSport, or a quasi-national speech and music station will bid and win a selection of sports rights over the next 10 years. This share might drop to 1.5 per cent, yielding a total Five Live share of 3.5 per cent by 2014.

Loss of share to 2006 will, however, be minimal.

If Five Live was to close down in 2006, while its coverage of minority sports and more minor events in major sports are unlikely to be wanted by commercial radio, some of the major events would transfer, and so would a significant proportion of the audience to these events – although some listeners would also migrate to TV and new media coverage, especially as commercial radio would probably end up paying less for the audio rights which might encourage sports owners to keep certain sports off the radio so as to drive pay TV and new media interest.

Overall, about 2 per cent of its 2.5 per cent sports coverage share would migrate to commercial radio. But only about 0.5 per cent of its 2.5 per cent news and current affairs audience would migrate to commercial radio – most would go to Radio 4, Radio 2 or BBC local radio. This would mean just 2.5 per cent share – or half the current audience would go to commercial radio.

By 2014, about 2 per cent of its total 3.5 per cent share would probably migrate to commercial radio.

## Revenue Impact

The 2.5 per cent share points transferring to commercial radio in 2006 would represent a 5 per cent increase in commercial impacts or a 2.5 per cent increase in commercial revenue – i.e. £15m in 2006 in today's prices.<sup>28</sup>

The 2 per cent share transfer in 2014 would equate to 3.8 per cent share of impacts and a 1.9 per cent share of revenue – or about £22m in 2014 in 2004 prices.

Although, the Radio Five Live audience is mostly 35 to 55, its male, quite up market focus would probably enable it to be sold at normal commercial market rates – without a discount – leaving actual revenue gain in 2006 at £15m and in 2014 at £22m.

The increased commercial revenue would be spread among a number of speech/music, adult contemporary and easy listening stations, but the largest shares would probably transfer to TalkSport and LBC – especially if these networks were to cover many of the sports events currently covered by Radio Five Live.

TalkSport in particular might be set to gain about half the revenue.

## Cost Inflation

The withdrawal of Radio Five Live from the sports rights market might reduce costs – although at the moment, TalkSport and commercial local radio services that cover sports such as Century – tend not to go head to head with Radio Five Live which limits the impact on their cost base of any withdrawal.

If more local, regional or quasi- national stations were to see Radio Five Live's withdrawal from the market as an opportunity in sport the cost inflation gains could be minimal. In fact, if the commercial rivals were to engage in a significant amount of head to head competition for specific sports some might rise in price.

## iii. General Impact Upon the Commercial Market Equilibrium to 2014

The withdrawal of Radio Five Live, with no reallocated frequency, would probably encourage more speech on the 35 to 50 age group music services – including sports coverage – and a slight movement upmarket by TalkSport but with a similar mix of programming as now.

If the analogue frequency was allocated to a new service with any remit – it would be likely to produce another speech/music station. If it was allocated on condition that output were similar to Radio Five Live, then it would be likely to increase sport, phone in and rolling news coverage and to become more of a direct head to head competitor with TalkSport.

If the frequency was allocated as 8 new digital networks there might be a slightly increased tendency for one of those networks to be a news and sport network, but again more like TalkSport than the current Radio Five Live.

---

<sup>28</sup> The -2 estimated elasticity might well not apply to such large scale changes.

## **f. English Local Radio**

### **i. Performance and Distinctiveness**

#### ***A Robust Share Performance in the face of Increased Competition***

English local radio has maintained a 10 to 11 per cent share over the last 5 years despite further expansion in commercial local and regional radio. Share varies considerably by market and depends a great deal on the nature of the local radio market. While share in London is just 2 per cent given London's 15 local commercial stations and its own commercial speech station, share in Cumbria – with only one fairly recently established local radio station - is 18 per cent.

#### ***Providing Local News and National News From A Local Perspective while Commercial Radio Concentrates on Local Identity Rather than Local News***

For the most part local commercial radio concentrates on forming a local identity, with local promotions and sponsorship of events. Most commercial radio limits its local news reporting to short bulletins, travel, weather and what's on information - and occasional issue based phone-ins, while its national news service –sourced through IRN - is delivered from a national rather than local perspective.

English local radio share has held up fairly well even in markets with new regional speech/music mix stations which give more coverage to local news and issues – such as Century radio in East Midlands, North West and North East, aimed at the 30 to 45 market, or in areas where Saga FM exists such as the West Midlands.

Although such services do have regional news and phone in programmes, the large areas they cover – which in turn yields the volume of audience impacts and revenue they need to cover the higher costs of speech radio – means that they may fail to cover truly local and community issues either from a local or national perspective.

All breakfast shows across the BBC English Radio Network are speech based. During the rest of the day about 60 per cent of all airtime is speech. The typical coverage areas of English local radio stations – about 1 million people on average – means that outside of London and they are the only providers of truly local speech based radio.

The average programme spend per hour of an English local radio station of about £300 to £400 per hour is far greater than the average commercial radio station of about £125 per hour.

#### ***Promotion of Local Talent and Events***

Local radio in England also provides extensive coverage of local events, local musical and performing talent and relevant sports matches and tournaments. While local commercial radio reports local events and campaigns and often covers local Premiership and Championship football matches, BBC English local radio tends to cover more events live and devotes more airtime to these events as well as covering a wider range of local sports and events.

### ***A Focal Point for the Community – Especially the Over 50s***

In many areas – especially outside the major urban areas – English local radio provides a focal point of the local community, especially those over 50 who are largely excluded from local commercial radio.

### ***A Different Role in Major Metropolitan Markets***

In major urban markets – especially in London – where the commercial market caters more for the tastes of the over 50s, English local radio has adapted its role to focus on other underserved groups. In London, London Live focuses on providing an intelligent speech to service to the 30s and 40s, with coverage of ethnic communities in the capital.

## **ii. Indicative Direct Revenue and Cost Impact**

### **Audience Substitution**

Currently English Local radio accounts for about 8.5 per cent of all listening – i.e. about 10 per cent amongst 85 per cent of the UK's listeners. This is unlikely to be eroded by 2006, but is likely to reduce by 2014 to about 7.5 per cent. While growth in easy listening and speech/music mix stations might take some audience away as it has done in more competitive markets to date, they are unlikely to attract BBC local radio's core audience.

At the same time, the potential erosion of heritage ILR radio's ability to sustain their current commitment to programming on local issues and news is likely to gain BBC local radio some listeners – at least for part of the day. Commercial radio is unlikely to deliver specialist local speech stations like LBC in London – which has a significant impact on BBC Radio London – in any other markets. While the growth in speech/music mix stations with digital might bring some more speech competition, this will be regionally rather than locally focused, and will be aimed at primarily a younger market than the core BBC local radio audience in England.

BBC local radio enjoys a high proportion of solus listeners and a high degree of overlap with other BBC services – especially outside the major urban markets.

If the BBC local radio in England were to close, a proportion of its listening might be lost to radio – with its listeners seeking local news from the internet, TV or newspapers. Some listening would also end up with other BBC services – although they might prove a poor substitute for the local news and information being sought by transferring listeners.

Overall about 6 per cent of the local radio audience in 2006 might transfer to commercial radio in 2006 and about 5.5 per cent in 2014.

### **Revenue Impact**

A 6 per cent transfer in listening in 2006 would represent a 12 per cent increase in commercial impacts, which would cause a 6 per cent fall in price and, therefore, a net 6 per cent increase in revenue. This would be the equivalent of £36m in today's prices. The audience transferring would be mostly over 50, but at the same time it might help heritage ILR and local easy listening stations maintain or even grow their overall local market reach

which might benefit local advertising revenues. The overall discount might be lower than that for Radio 2, perhaps about 30 per cent. This would yield a net revenue transfer of £26m.

In 2014, the commercial impact increase would be 9 per cent (5.5 per cent divided by 57 per cent), and the revenue increase – with no discounts – would be 4.5 per cent, or £54m. With a 30 per cent discount this would be about £38m<sup>29</sup>.

### **Cost Inflation**

There might be some reduction in the salaries demanded by local broadcast journalists, but the commercial sector's use of such journalists is limited, and it is just as likely that former BBC journalists would pursue other careers rather than applying for jobs in commercial radio.

## **iii. General Impact Upon the Commercial Market Equilibrium to 2014**

The cessation of English local radio – and no reallocation of its frequencies – might initially cause existing local heritage ILR commercial radio stations to increase their speech and local news content marginally so as to capture some more of the under 50 audience – they might do this on their Gold service rather than their FM service.

A re-allocation of frequency to a national analogue service or set of digital services, might have a similar effect to the above, while a reallocation to new local services would be likely to squeeze the budgets of all local services.

The reallocation of local analogue frequency with no stipulation on use is most likely to produce a local speech/music service with some local news and events, or niche music service. The allocation of analogue frequency locally with a stipulation to be mostly local speech would result in 48 commercial local stations focused on basic local news, national news bulletins and phone ins – and even these would be unlikely to survive as independent stations – instead requiring some networking across the UK.

## **g. National Radio Services for Scotland, Wales and Northern Ireland**

### **i. Performance and Distinctiveness**

#### ***Share Holding Up Reasonably Well Over the Last 5 Years***

The National services in English have held their share fairly well over the last 5 years. Radio Ulster and Foyle in Northern Ireland achieve the highest share at over 26 per cent while Radio Wales achieves a 9.2 per cent share and Radio Scotland a 7.6 per cent share. Radio Scotland tends to focus on a slightly different demographic than the others by effectively offering a national alternative to Radio 4 in Scotland and attracting ABC1s between 40 and 60.

---

<sup>29</sup> Once again it is worth noting that the -2 estimate is based on historic small scale changes in commercial audience share not the large scale changes envisaged here.

Over the last 5 years Radio Ulster/Foyle has actually increased share slightly, Radio Wales had remained steady and Radio Scotland has lost a percentage point.

Radio Cymru – the Welsh language service, has lost some share over the last 5 years – declining from 5.4 per cent to 4.4, while Radio nan Gaideal – the Gaelic language service in Scotland – obtains on a very small share given the very low number of Gaelic speakers in Scotland.

### ***Share in Scotland and Wales Under Some Pressure from the Arrival of Real Radio***

Radio Scotland's loss of share and Radio Wales loss of some share among younger women have been due in large part to the arrival of Real Radio in the central belt of Scotland and the South Wales area. These services – owned by the Guardian Media Group – offer a mix of speech and adult contemporary music, targeting the 30 to 50 market segment.

However, for the most part these services have taken share from the incumbent commercial services, and they only cater for the metropolitan areas of Scotland and Wales while the BBC services have remit to cover issues and interests of the whole nation.

### ***A Broader Remit Than English Local Radio***

The National services have a broader remit than English local radio. They are expected to give extensive coverage to the devolved assemblies and the issues these assemblies decide. Each station also offers programming designed to analyze national issues and provide the focal point for the national debate.

### ***Reflecting Developing Distinct Cultures, Traditions and Language***

Above all these services offer programming covering the national cultural and music tradition, with large number of relayed live events, live music output and local drama and comedy.

## **ii. Indicative Direct Revenue and Cost Impact**

### **Audience Substitution**

Radio Scotland currently gains a 7.6 percent share in Scotland, while Radio Wales and Radio Cymru obtain a combined share of 13.5 per cent in Wales. Radio Ulster and Radio Foyle gain a 25 per cent share in Northern Ireland.

The shares of Radio Scotland and Wales have suffered slightly from the introduction of the Real Radio speech and music mix stations in Central Scotland and South Wales, and they might be expected to lose more share in the coming years with the increased number of easy listening stations on digital.

Overall, the three services share of all listening in the UK is likely to fall from 1.8 per cent in 2013 to 1.5 per cent in 2014.

Like English local radio, the services have significant overlap with other BBC services but compared to England they tend to have more solus listeners.

If the services ceased to be available, a significant proportion of the audience would probably migrate to local and regional commercial services aimed at the 35 to 50 age group. About 1.3 per cent share might transfer in 2006 and 1.1 per cent in 2014.

### **Revenue Impact**

This share of listening transfer equates to a 2.6 per cent increase in commercial impacts in 2006 and a 2 per cent increase in 2014. With an elasticity of -2 this yields a revenue increase for commercial radio in Scotland, Wales and Northern Ireland combined on £8m rising to £12m at average market rates.

However, advertising rates in the national regions are about 40 per cent lower than the national average leaving likely revenue transfer of £5m rising to £7m in today's prices<sup>30</sup>.

### **Cost Inflation**

There might be some less competition for the Nations' sports rights, and other national events – although this would clearly leave these sports and events worse off as well. There might also be the same impact on local journalist salaries, but the same caveat applies as with English local radio – the journalists are just as likely to seek other careers.

## **iii. General Impact Upon the Commercial Market Equilibrium to 2014**

The closure of national radio – English and local language services – with no reallocation of frequency would cause a shift in the local station portfolio – especially in the larger urban markets – towards some more speech and news output, but probably focused on the under 50 market.

The reallocation of an analogue frequency with a requirement to be local speech and news – with local language programming as well – would not produce the range and variety of the BBC's current services but would produce a concentration on metropolitan audiences, and a squeeze on the viability of services such as Real Radio.

The reallocation of the frequency to local digital services would be likely to further fragment the Nations' commercial radio markets.

---

<sup>30</sup> It should be considered however that the -2 estimated elasticity may be less applicable to changes of this scale.

### 3. THE BROAD IMPACT OF THE BBC'S OVERALL PORTFOLIO

#### a. Indicative Overall Direct Revenue and Cost Impact

The level of audience share either leaving radio altogether or migrating to other BBC services following the closure of a specific BBC service is summarized in Exhibit 20.

**EXHIBIT 20**

LIKELY AUDIENCE TRANSFERRING OUT OF RADIO OR TO OTHER BBC SERVICES IF INDIVIDUAL BBC SERVICES ARE CLOSED DOWN

	AUDIENCE SHARE BY 2014	SHARE POINTS TO OTHER MEDIA TRANSFERRING IN 2014 IF CLOSED DOWN	SHARE POINTS TRANSFERRING TO OTHER BBC SERVICES IN 2014 IF CLOSED DOWN	RATIONALE
RADIO 1	5.0%	0.5%	1%	<ul style="list-style-type: none"> <li>Some overlaps with Radio 2</li> <li>Transfer to 1Xtra and 6 Music</li> </ul>
RADIO 2	11.0%	1.5%	2.5%	<ul style="list-style-type: none"> <li>30% solus or near solus listening currently</li> <li>Significant overlap with Radio 4, Radio 5 Live and local/national - some Radio 1</li> </ul>
RADIO 3	1.3%	0.1%	0.6%	<ul style="list-style-type: none"> <li>Overlap with Radio 4 and Radio 2</li> <li>Solus listening 10%</li> <li>Unique Radio 3 output</li> </ul>
RADIO 4	10%	1.5%	5.5%	<ul style="list-style-type: none"> <li>25 to 30% solus listening</li> <li>Radio 5 Live and Radio 2 overlap</li> </ul>
RADIO FIVE LIVE	3.5%	0.2%	1.3%	<ul style="list-style-type: none"> <li>Overlap with Radio 4 and Radio 2</li> <li>10% to 15% solus listening</li> </ul>
ENGLISH LOCAL RADIO	7.5%	0.5%	1.5%	<ul style="list-style-type: none"> <li>Other forms of local news developing</li> <li>Overlaps with Radio 2 and Radio 5 Live</li> </ul>
NATIONAL RADIO	1.5%	0.1%	0.3%	<ul style="list-style-type: none"> <li>ABC1 audiences of Radio Scotland likely to transfer to other BBC services</li> </ul>

Overall, the combined individual direct revenue impacts of all the analogue services could be an extra £151m a year averaged over the 2006 to 2014 period for commercial radio if the -2 elasticity estimate was used. However, as has been noted already, use of this elasticity for large scale changes in commercial audience may not provide a very accurate estimate.

The positive revenue impact on the commercial sector of switching all BBC services off at the same time might clearly be larger than this £150m as there are no remaining BBC services for people to switch to. On the other hand, such an enormous change in the commercial audience would almost certainly make the -2 elasticity completely irrelevant implying that the combined impact might actually be less than £150m as the commercial market struggled to absorb such a large scale change.

In addition, total radio listening would be likely to reduce if many types of output previously supplied by the BBC were not replicated by the commercial sector.

Exhibit 21 summarises the indicative revenue impacts.

**EXHIBIT 21**

**INDICATIVE DIRECT REVENUE IMPACT ON COMMERCIAL RADIO OF WITHDRAWING SPECIFIC BBC SERVICES**

	AUDIENCE SHARE IN:		LIKELY AUDIENCE SHARE TRANSFER TO COMMERCIAL RADIO IF SERVICE CEASES		INCREASE IN COMMERCIAL IMPACTS		INCREASE IN COMMERCIAL REVENUE (NO DISCOUNT OR PREMIUM)		INCREASE IN COMMERCIAL REVENUE (APPLYING LIKELY DISCOUNT OR PREMIUM)	
	2006	2014	2006	2014	2006	2014	2006	2014	2006	2014
RADIO 1	7.0%	5.0%	5.5%	3.5%	11%	6%	£31.5m	£36m	c£28m	c£32m
RADIO 2	14.0%	11.0%	10.0%	7.0%	18%	12%	£54m	£72m	c£27m	c£36m
RADIO 3	1.3%	1.3%	0.6%	0.6%	1.2%	1.0%	£2.8m	£6.0m	c£2.3m	c£5.0m
RADIO 4	11%	10%	4.0%	4.0%	8%	7%	£24m	£42m	c£19m	c£34m
RADIO FIVE LIVE	5%	3.5%	2.5%	2.0%	5.0%	3.7%	£15m	£22m	c£15m	c£22m
ENGLISH LOCAL RADIO	8.5%	7.5%	6.0%	5.5%	12%	9%	£36m	£54m	c£26m	c£38m
NATIONAL REGIONAL RADIO	1.8%	1.5%	1.3%	1.1%	2.6%	2.0%	£8m	£12m	c£5m	c£7m

Note: This indicative impact is based on an estimated historic survey based elasticity estimate of -2 which applied to small changes in price and volume. This may not be applicable to large scale changes.

**b. General Impact Upon the Commercial Market Equilibrium to 2014**

How far the commercial portfolio would adjust to the absence of all the BBC's core services by providing a greater range and depth of service is difficult to judge. Almost certainly, the commercial market by itself would be unlikely to provide the live music of Radio 3, Radio 2 and Radio 1 in similar volumes, or the continuous local speech service of BBC local radio, nor the built drama, comedy and magazine programming of Radio 4.

Even if regulators tried to mandate such output as a condition of releasing extra spectrum to the commercial market, much of the BBC's output would simply be uneconomic to produce and therefore any such regulatory requirements would be unsustainable.

For those elements of the BBC's output which might still be relatively expensive or cost ineffective, but still sustainable – such as probably in depth national news, a wide range of sporting events, a wide and varied playlist of recent, adult contemporary and easy listening music, or social action campaigns – rules would probably have to be both detailed and applied rigorously if they were to affect commercial radio output.

**c. The Overall Impact on the Radio Market and Listeners**

The overall impact on the listener would be likely to be:

- a narrower range of output in each area;
- an almost complete absence of the highest cost type of output such as new drama and comedy;

speech radio limited largely to news, sport and phone-ins

an absence of any broadly based networks trying to engage with a range of interests and cross fertilizing different tastes from different communities and groups

a reduction in the total amount of spending on new programming ( with the commercial unlikely to make up even half of the current programme spending of the BBC – which is £345m a year).

## d. The Impact on Broader Cultural and Creative Activities

While BBC radio services might have a direct impact on the commercial radio sector, they also has an indirect, and largely positive impact on a number of broader cultural and creative markets such as music, new writing, performing and writing talent development and local journalism. These would probably be lost if BBC services were closed down.

## i. UK Music Creation and Performance

Analysis of relevant government and commercial body statistics by O&O suggest that music and the performing arts in the UK is a £5.7 billion sector (excluding the actual broadcasting of such activity), with about a £400m contribution from public funds. (See Exhibit 22 below).

### EXHIBIT 22

#### PERFORMANCE AND CULTURE – MUSIC AND THE PERFORMING ARTS

		GOVERNMENT FUNDING	CORPORATE/DONORS	CONSUMER	TOTAL	
MUSIC CONSUMPTION	CLASSICAL MUSIC	LIVE	£76m	£19m (sponsorship)	£160m	£410m
		RECORDED	-	£25m (royalties)	£130m	
	MUSICALS	LIVE	-	£35m (sponsorship)	£192m	£312m
		RECORDED	-	£15m (royalties)	£70m	
	POPULAR/CHART MUSIC	LIVE	-	£115m (performance) £15m (sponsorship)	£447m	£2,877m
		RECORDED	-	£480m (royalties)	£1,920m	
	OTHER MUSIC	LIVE	£9m	£4m (performance) £3m (royalties)	£47m	£346m
		RECORDED	-	£3m (royalties)	£280m	
	MUSICAL EDUCATION		£24m	-	£293m	£317m
	MUSICAL INSTRUMENTS		-	-	£760m	£760m
OTHER		£111m (51 local)	-	-	£111m	
TOTAL MUSIC		£219m	£682m	£4,299m	£5,200m	
THEATRE/DRAMA/LIVE COMEDY		£132m (£62m national) (+£70m local)	£30m	£131m	£293m	
DANCE/BALLET		£55m (£25 national) (+£30 local)	£10m	£21m	£86m	
TOTAL		£406m	£722m	£4,451m	£5,579m	

The UK music industry (recorded, performance and composition) is one of the UK's success stories – it is worth about £5.2 billion and makes about a £400m a year trade surplus. While

the UK consumer represents 8 per cent of total demand for global music, the UK's music industry takes an 11 per share of the global market in music.

UK music accounts for 50 per cent of UK music sales – a higher proportion for indigenous music than any other major European country, and UK music consistently takes the highest non US share of the USA market. While comparative success in the USA could be expected given the language and cultural affinity, the same factors should apply to UK imports of US material. The fact that the UK music industry still accounts for half the domestic market despite the scale and strength of the US market is a testament to the strength of the UK industry.

Live popular music is gaining in strength in the UK with 70,000 concerts/gigs and 25 festivals per year – attracting total visitor numbers on the region of 20 million. There are about 50 professional symphony orchestras spread across the UK, giving over 4,000 performances per year.

The BBC makes a significant contribution to the UK music industry. UK music makes up over half of Radio 1's daytime playlist – and 40 per cent of that is of new UK music. Both Radio 1 and Radio 2 play a wide range of tracks and more new music than their commercial counterparts.

Radio 1's *Onemusic* strand provides information and support to aspiring singers and bands, airing demo tapes and helping them gain access to record labels and backing.

The BBC runs 5 orchestras and 1 choral group across the UK, providing about £16m of subsidy to maintain the orchestras for live performances and special recordings. 50 per cent of all music played on Radio 3 is live music, and the station commissions new work from about 60 composers a year. BBC musicians tour schools to support music education and the BBC runs a New Generation Artists Scheme playing new music alongside established pieces.

Over the last 5 years the BBC has commissioned work from 250 different composers covering Chamber, Orchestral, Jazz, Choral and World music and spending about £450,000 a year on new commissions. Last year, 15 per cent of new works were from composers under 35 years old.

The Proms is the UK's largest classical music festival, with 250,000 tickets sold a year plus another 40,000 sold for Proms in the Park. Radio 3 plays 74 Prom concerts and 700,000 listeners tune in per week to Radio 3 to listen to the Proms. The Proms probably plays a leading role in encouraging classical music sales in the UK, with recordings of the Proms leading the iTunes download chart in September 2004.

## **ii. New Writing, Talent and Journalism**

There are about 16,000 theatrical performances in the UK every year. However, only about 430 new plays are commissioned by the theatre in each year in the UK. BBC Radio commissions about 350 new plays by established and new writers every year as well as 300 hours of original comedy every year.

BBC radio's investment in written drama and comedy has created a number of formats that have transferred to TV – Channel 4 as well as the BBC – such as *Dead Ringers*, *Little Britain* and the *The News Quiz* (Have I Got News for You).

Many of these formats have been developed by independent TV producers.

About 10 per cent of the BBC's built programming output is made by independent producers – a sector that the BBC has developed from scratch over the last few years. 75 per cent of people working in the independent radio sector have been trained at the BBC.

The BBC employs over 3,000 journalists in its local radio and TV divisions and is the largest single employer of local and regional journalists in the UK, and the only major force in regional/local journalism providing a comprehensive alternative to the increasingly concentrated local press.

#### **d. The Impact on Digital Take Up**

At one very general level, having a strong portfolio of analogue services could be seen as preventing digital take up. If the analogue radio sector did not have the core BBC services, listeners might be keener to take up digital radio that offered them more choice, if not the depth and breadth offered by the BBC. However, it is just as likely that with no BBC analogue services, radio would be a less healthy medium overall, and consumers would spend more time on other media and simply be less interested in digital radio.

More relevant perhaps to this analysis is the clear impact that cross promotion of digital radio on the BBC's core services has had in take up, and in particular in encouraging migration to digital by older parts of the population who tend to be rather slow in taking up new technology across other media. Most current DAB households are heavy consumers of BBC core services and older than the core commercial radio audience.

Perhaps even more importantly, BBC core radio services have played a vital role in introducing the UK population to internet radio streaming.

### **5. The Overall Scorecard**

Set out in Exhibit 23 below is an overall scorecard for each BBC core radio service. It summarizes:

- the indicative revenue impact of each service based on the very approximate -2 elasticity of demand for radio advertising and the size and demographics of any audience that might shift to the commercial sector;

- the main areas in which the absence of the BBC service might reduce or increase cost inflation for the rest of the sector;

- the main elements of distinctiveness within each service;

- the likely response of the commercial portfolio to the absence of the BBC service (without heavy direct regulation of commercial output); and,

- the broader economic contribution of each service that would be lost if the service closed.

As has already been suggested, it is impossible to estimate with any degree of accuracy the effect on the UK radio market of the withdrawal of the whole of the BBC's analogue radio portfolio. Spot elasticity calculations cannot provide any sort of effective guide to the revenue impact of such a radical change which would fundamentally reshape the market. In addition, the indicative revenue impact which has been calculated for each network is based on the transfer of some audiences to other BBC services. The behaviour of these audiences in a market in which there were no other BBC analogue services is difficult to predict and would depend on the degree of regulatory intervention to shape replacement services, and what emerged to fill the gap left by the BBC. The only thing that can be said with any degree of confidence is that a market without the BBC's core radio services would be entirely transformed, would probably prevent the production and broadcast of certain types of content, and would also transform the economics of a number of related cultural markets.

**EXHIBIT 23**

THE 'SCORECARD' BY SERVICE

	INDICATIVE NEGATIVE ANNUAL AVERAGE REVENUE IMPACT* (2006 TO 2014)	COST INFLATION	DISTINCTIVENESS	BROAD IMPACT ON COMMERCIAL PORTFOLIO	BROADER ECONOMIC IMPACT ON OTHER MARKETS
RADIO 1	c£30m	<ul style="list-style-type: none"> <li>• May actually reduce commercial payouts to rights holders</li> <li>• Some increase in presenter costs</li> </ul>	<ul style="list-style-type: none"> <li>• Range of tastes and interests</li> <li>• Wide playlist and live music</li> <li>• News and social action</li> <li>• UK music 'hub'</li> </ul>	<ul style="list-style-type: none"> <li>• May reduce number of segmented commercial services for under 30s</li> </ul>	<ul style="list-style-type: none"> <li>• Major UK music industry sponsor</li> </ul>
RADIO 2	c£32m	<ul style="list-style-type: none"> <li>• May actually reduce commercial payout to rights holders</li> <li>• Some increase in presenter costs</li> </ul>	<ul style="list-style-type: none"> <li>• Range of tastes and interests</li> <li>• Wide playlist and live music</li> <li>• Docs and news</li> <li>• Inter-generational meeting point</li> </ul>	<ul style="list-style-type: none"> <li>• May squeeze commercial 35 to 50 portfolio</li> </ul>	<ul style="list-style-type: none"> <li>• UK music industry sponsor</li> </ul>
RADIO 3	c£3.7m	-	<ul style="list-style-type: none"> <li>• Home of UK arts, culture and performing arts</li> <li>• Major sponsors of classical music</li> </ul>	<ul style="list-style-type: none"> <li>• Small Impact spread over many services</li> </ul>	<ul style="list-style-type: none"> <li>• Arts and classical music developer</li> </ul>
RADIO 4	c£27m	-	<ul style="list-style-type: none"> <li>• New drama and comedy</li> <li>• In-depth journalism</li> <li>• Documentaries</li> <li>• Range and breadth</li> </ul>	<ul style="list-style-type: none"> <li>• Small impact spread over many services</li> </ul>	<ul style="list-style-type: none"> <li>• New writing</li> <li>• Investigative journalism</li> </ul>
RADIO FIVE LIVE	c£18m	<ul style="list-style-type: none"> <li>• Some in sports rights but depends on number of competing commercial services</li> </ul>	<ul style="list-style-type: none"> <li>• In-depth rolling news</li> <li>• Breadth of sport coverage and journalism</li> </ul>	<ul style="list-style-type: none"> <li>• May squeeze commercial speech service</li> </ul>	<ul style="list-style-type: none"> <li>• Sport sponsor</li> </ul>
ENGLISH LOCAL RADIO	c£32m	<ul style="list-style-type: none"> <li>• Some in local journalism</li> </ul>	<ul style="list-style-type: none"> <li>• Home of local journalism</li> <li>• Catchment areas</li> </ul>	<ul style="list-style-type: none"> <li>• Some reduction in number of local commercial services in larger markets</li> </ul>	
NATIONAL REGIONAL SERVICE	c£6m	<ul style="list-style-type: none"> <li>• Some in national events and journalism</li> </ul>	<ul style="list-style-type: none"> <li>• National journalism</li> <li>• Focal point of national culture, events and debate</li> </ul>	<ul style="list-style-type: none"> <li>• Some increase in speech radio content on music services – metropolitan only</li> </ul>	<ul style="list-style-type: none"> <li>• National journalism pool</li> <li>• National arts and culture sponsor</li> </ul>

\*This indicative impact is based on an estimated historic survey based elasticity estimate of -2 which applied to small changes in price and volume – this may not be applicable to large scale changes.