



Radio – The fight back begins

A presentation by Oliver & Ohlbaum Associates
The Radio Festival, Tuesday 30th June



Challenges

- The four strategic challenges
- The impact of the recession

Catalysts

- Digital tipping point
- Revised regulation
- Economic recovery

The Fight Back

- New consumer propositions
- Consolidation
- New business models

CURRENT CHALLENGES TO RADIO IN THE UK

Four strategic challenges



Commercial radio is facing up to four structural pressures threatening to gradually reduce profitability...

	DETAIL
1) MACRO SHIFT	<ul style="list-style-type: none">• From display to 'intention-based' ads• Within display towards the internet
2) RISING COMPETITIVE INTENSITY	<ul style="list-style-type: none">• Within commercial radio• From the BBC• From TV?
3) FRAGMENTATION	<ul style="list-style-type: none">• Fragmenting analogue audiences• Digital platform choice proliferation
4) DISINTERMEDIATION	<ul style="list-style-type: none">• The rise of new middlemen e.g. Google, Apple, Spotify, Tun3r• Direct access to talent for advertisers/listeners

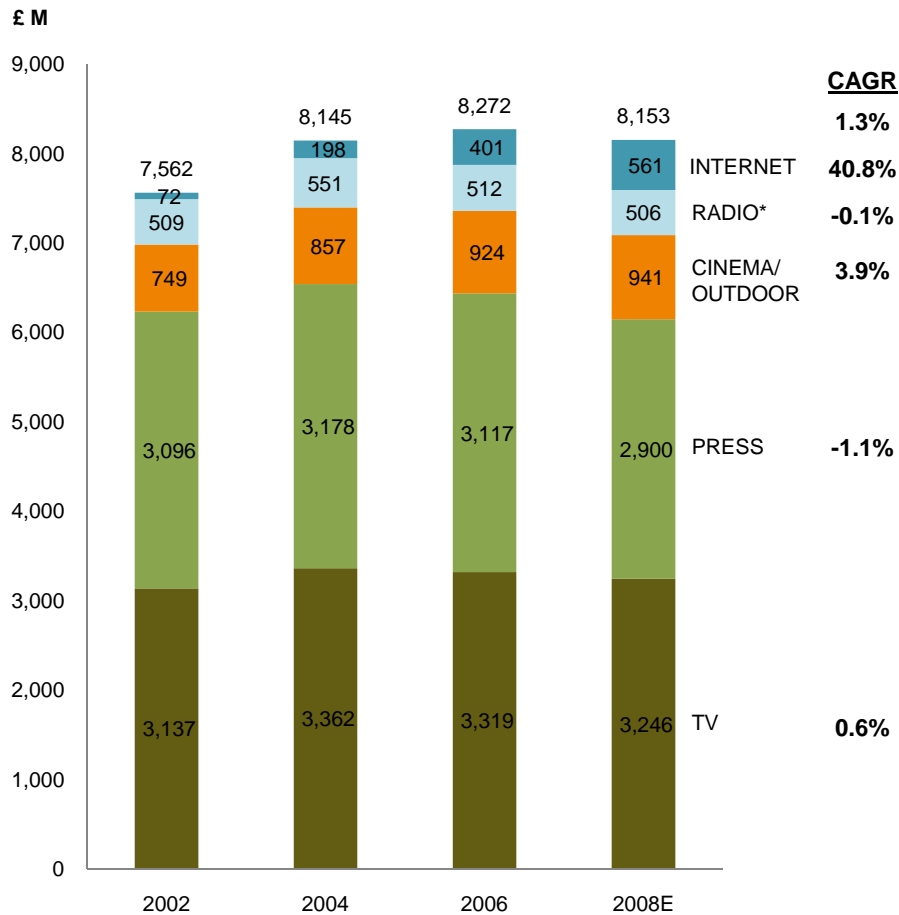
(1) MACRO AD SHIFT

Shift within display ads



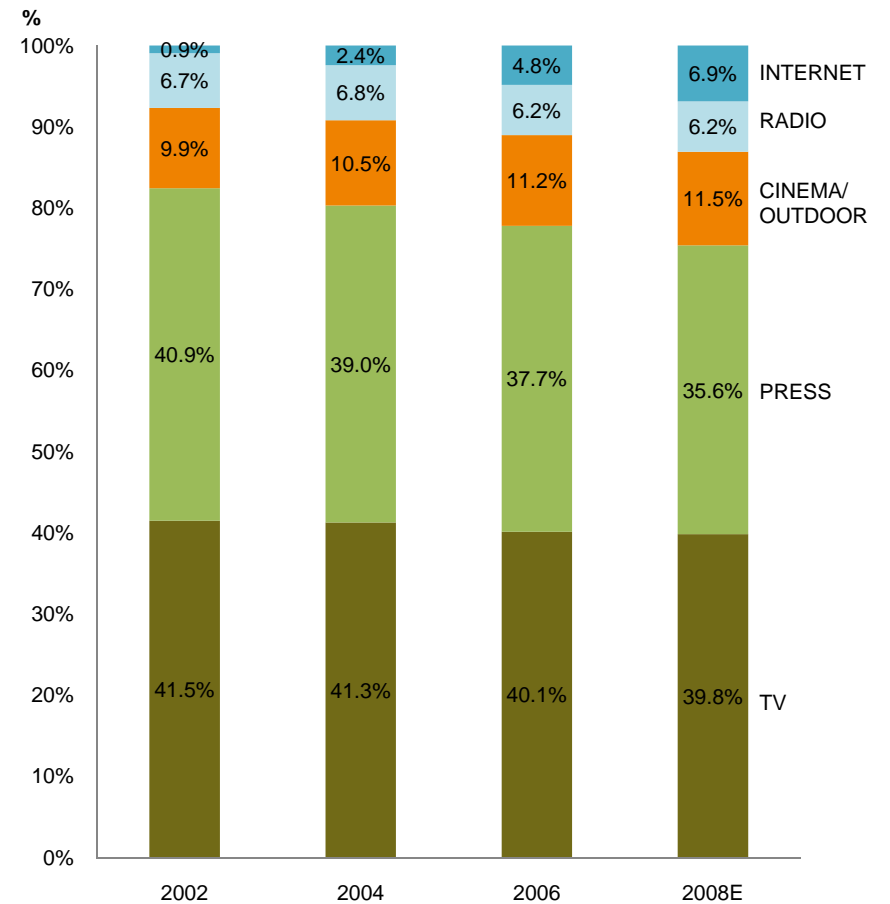
...total display advertising has grown at just over 1 per cent year on year since 2002 – a decline in real terms...

UK display net advertising revenue, selected years to 2008



...2008 estimates suggests the internet now accounts for a larger proportion of display advertising than radio...

Display advertising by medium, selected years to 2008



*Radio includes sponsorship revenue
Source: AA, RAB, O&O Analysis

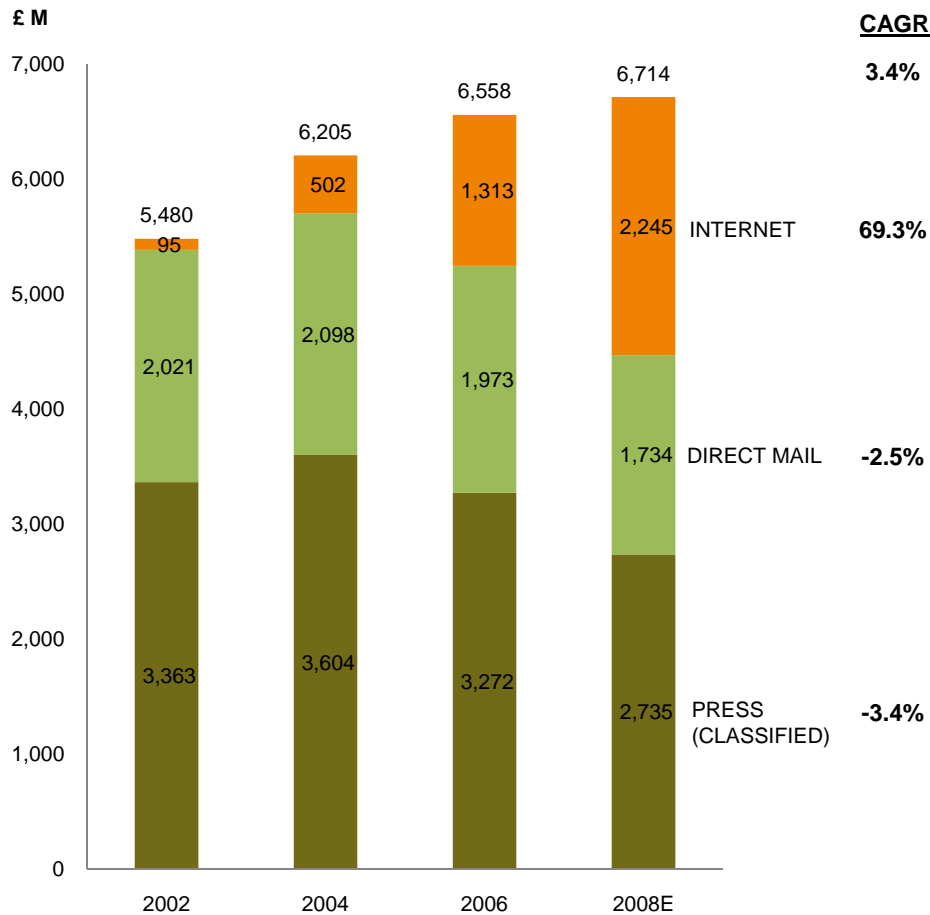
(1) MACRO AD SHIFT

Shift to 'intention-based' advertising



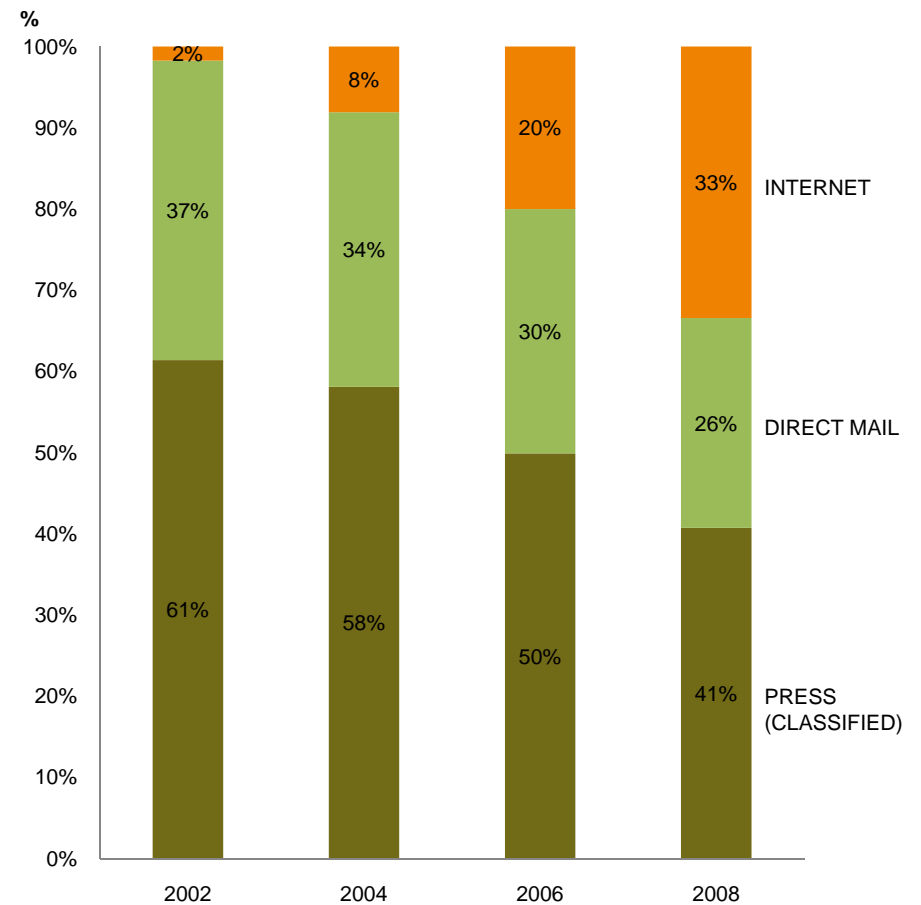
...Over 3 per cent annual growth in 'intention-based' advertising driven by spend online...

UK 'intention-based' net advertising revenue, selected years to 2008



...internet search and classified advertising now represents over a third of all 'intention-based' advertising...

UK 'Intention-based' advertising by medium, selected years to 2008



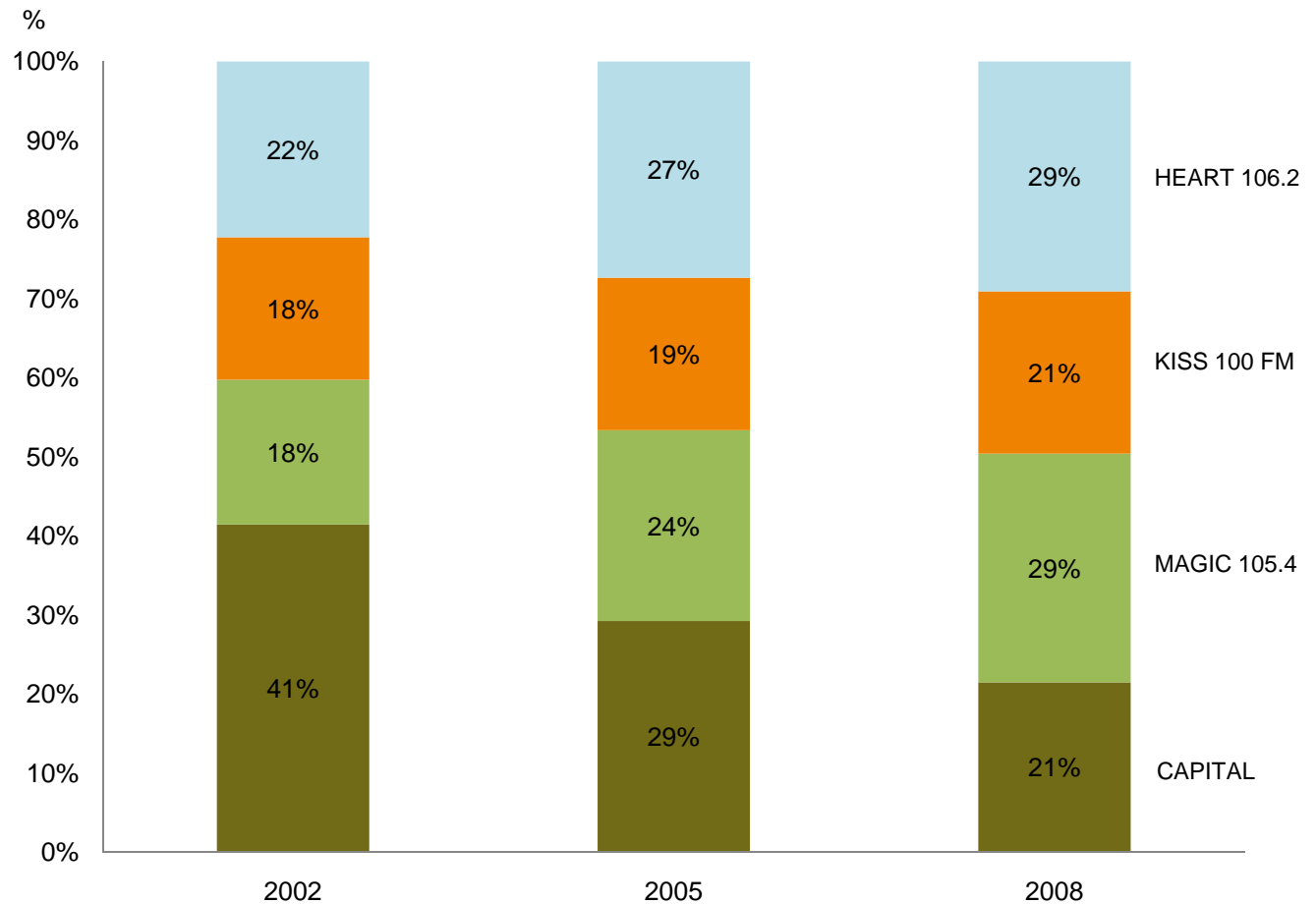
(2) RISING COMPETITIVE INTENSITY

Within commercial radio



Over the last few years there has been increased competition between commercial radio stations. This has been most pronounced in metropolitan areas...

Total listening share of top four London stations (proportion of aggregate share), 2002, 2005 & 2008



- Four-way competition for broad audience has replaced differentiated market
- Increased marketing and programme spend by these competing stations
- Less leverage with advertisers for each station

Source: Rajar, O&O Analysis

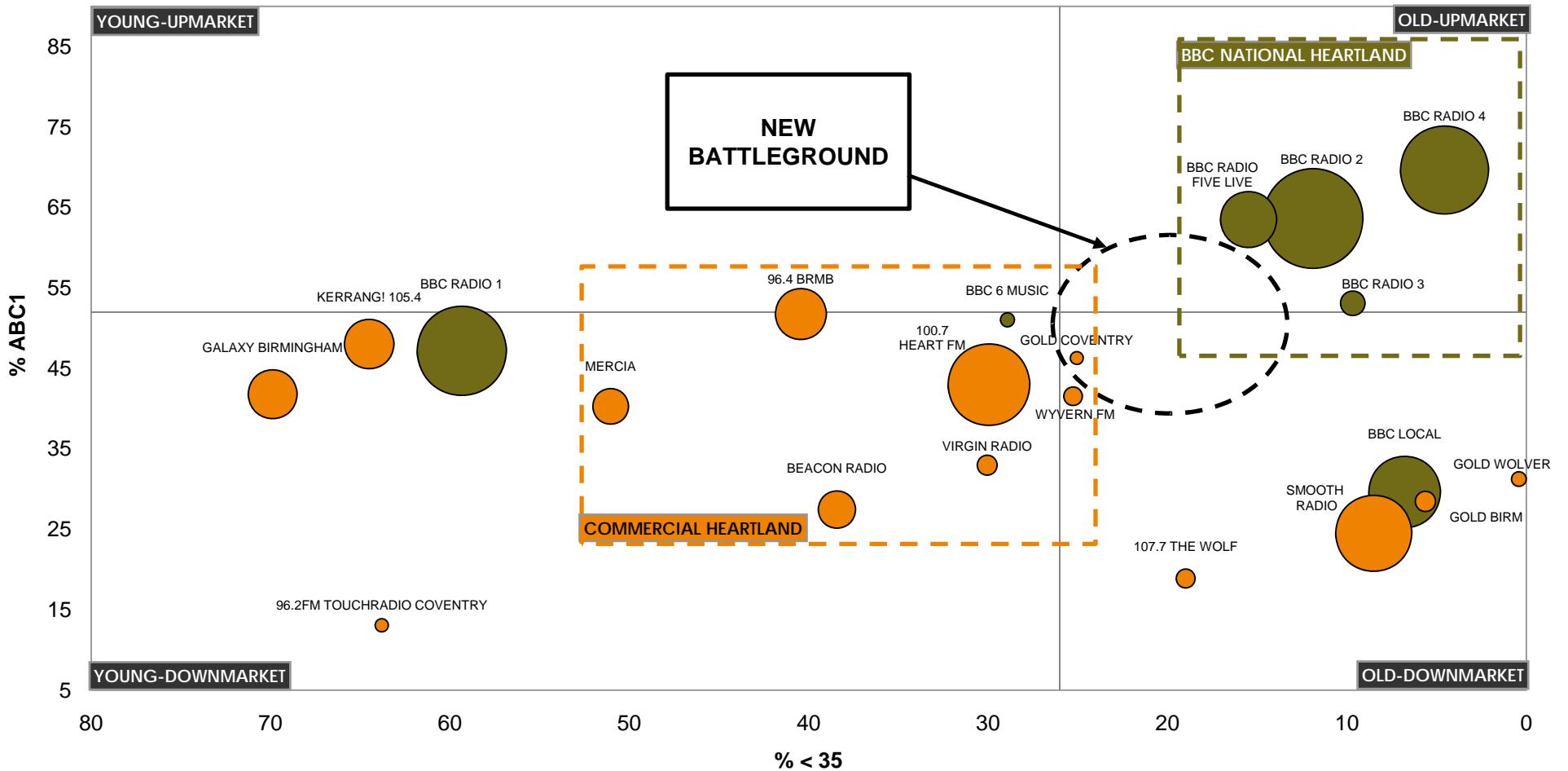
(2) RISING COMPETITIVE INTENSITY

From the BBC



...over the last few years the BBC has captured an increasing proportion of commercial radio's 15-44 heartland audience. There is a new battleground appearing between the BBC and commercial radio...

Station positioning in regional market – West Midlands



Source: Rajar, O&O Analysis

(2) RISING COMPETITIVE INTENSITY

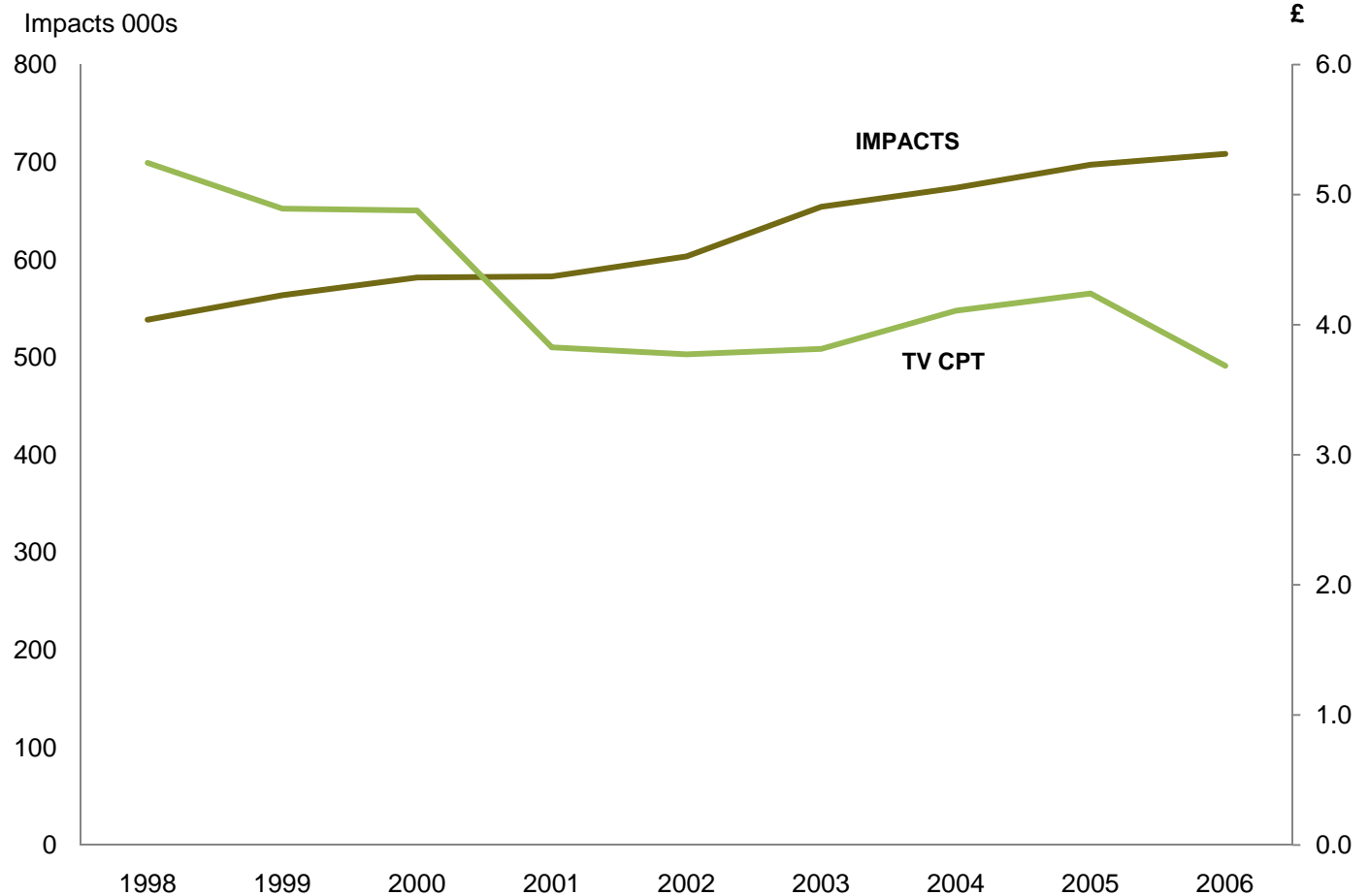
From TV?



...commercial radio revenue is also under threat from the growing number of low cost television outlets for advertisers...

- Multichannel viewing – growing number of impacts and commensurate fall in price of advertising on TV
- TV CPT fell 30 per cent between '98 & '06
- TV advertising now offers both 'reach' and cheap 'frequency'
- Becoming an 'economical alternative' to radio?

TV impacts versus CPT, 1998-2006



Source: Rajar, O&O Analysis

(3) FRAGMENTATION

Current radio advertisers want broad reach and frequency



Advertisers seeking broad demographics (at national and local level) account for c90% of all spend on radio...

ADVERTISER TYPE	AUDIENCE TARGETING	EST SIZE OF MARKET	PROPORTION OF OVERALL MARKET
TARGETED NATIONAL ADVERTISER	<ul style="list-style-type: none"> Narrow demographics and passion groups within 15 to 55 age groups High reach/frequency of narrow demographics 70% to 80% UK coverage Higher price for best demographics 	£60m	11%
BROAD NATIONAL ADVERTISER	<ul style="list-style-type: none"> Broader demographics across 20 to 45 age group – slight female skew High reach/frequency across broad demographic 80% to 90% UK coverage Highest price for highest reach in each local market 	£280m	56%
LOCAL ADVERTISER	<ul style="list-style-type: none"> Broader demographics 20 to 55 – slight female skew High reach/frequency across broad demographic Relevant coverage within market with limited wastage 	£165m	33%

MAIN MARKET



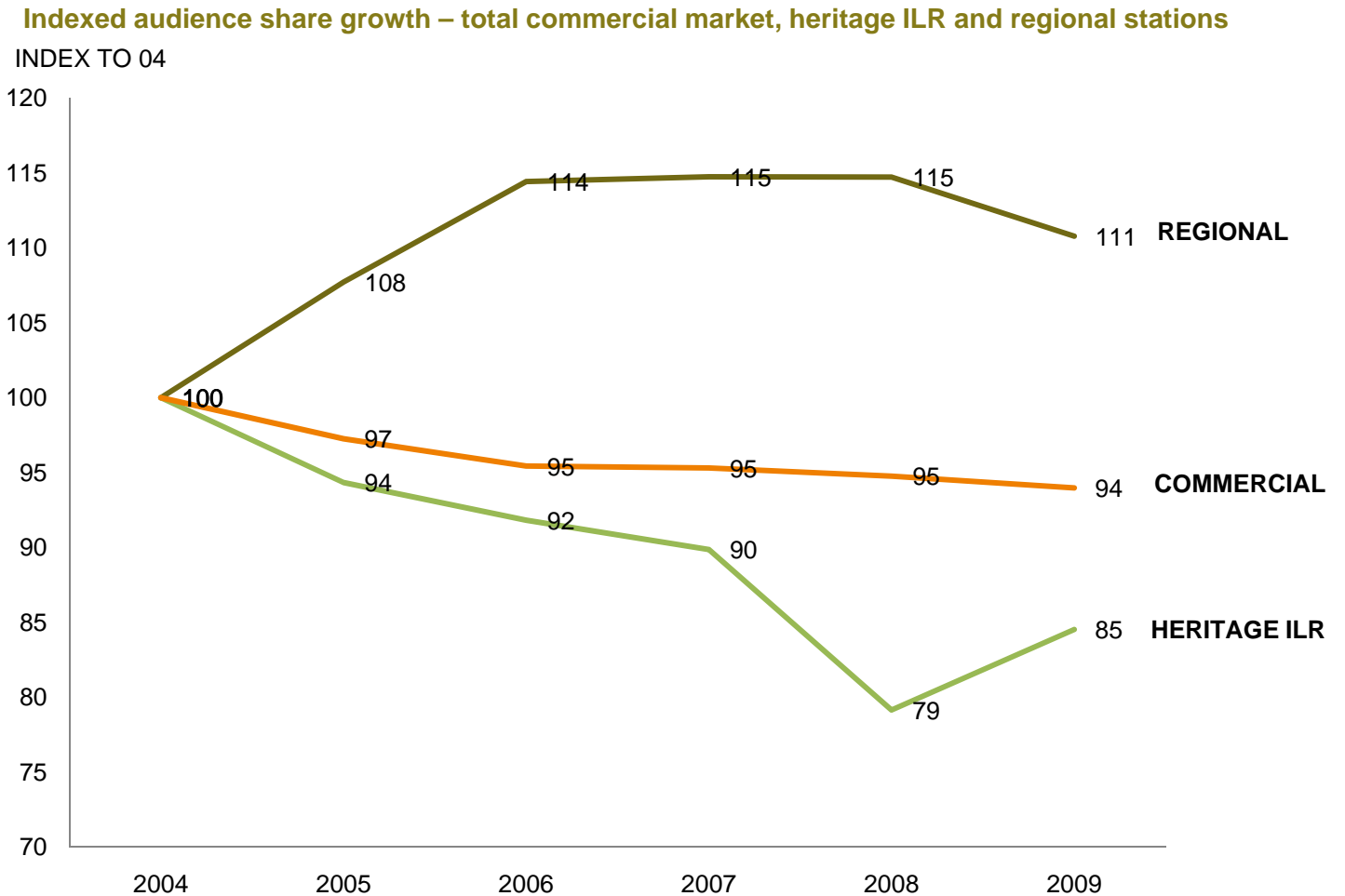
(3) FRAGMENTATION

Competition has fragmented the broad advertiser proposition



Within the traditional radio environment heritage ILR stations in particular are under pressure from audience migration to regional alternatives...

- Regional station's share of total listening has continued to rise despite a fall in overall listening to commercial radio...
- ...this has been at the expense of traditionally strong heritage ILR stations
- Analogue commercial radio audience now more fragmented



Source: Rajar, O&O Analysis (selected stations from major conurbations)

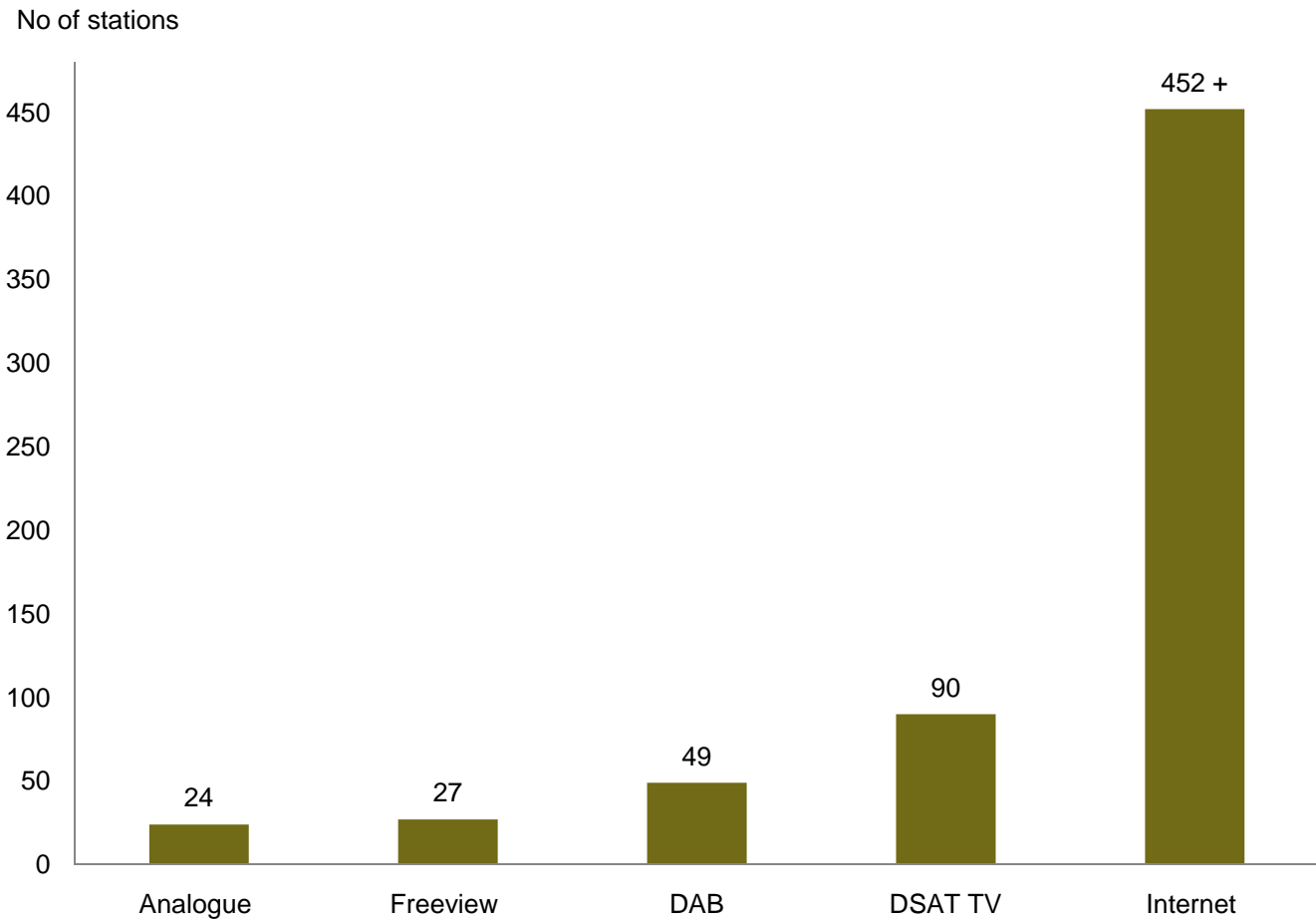
(3) FRAGMENTATION

New platforms are presenting more choice for the listener



Traditional analogue listening is under threat from new listening platforms offering a wider variety of stations...

No. of stations available on each major UK radio listening platform, London '08



- Over two thirds of households (with broadband) have access to over 450 stations
- Almost 90 per cent of households (with m/c TV) have access to a greater choice of stations
- Around a third of households with DAB set

Source: Rajar, Ofcom, Freeview, BSkyB, Radiofeeds.co.uk, Point topic, DRDB, O&O Analysis

(3) FRAGMENTATION

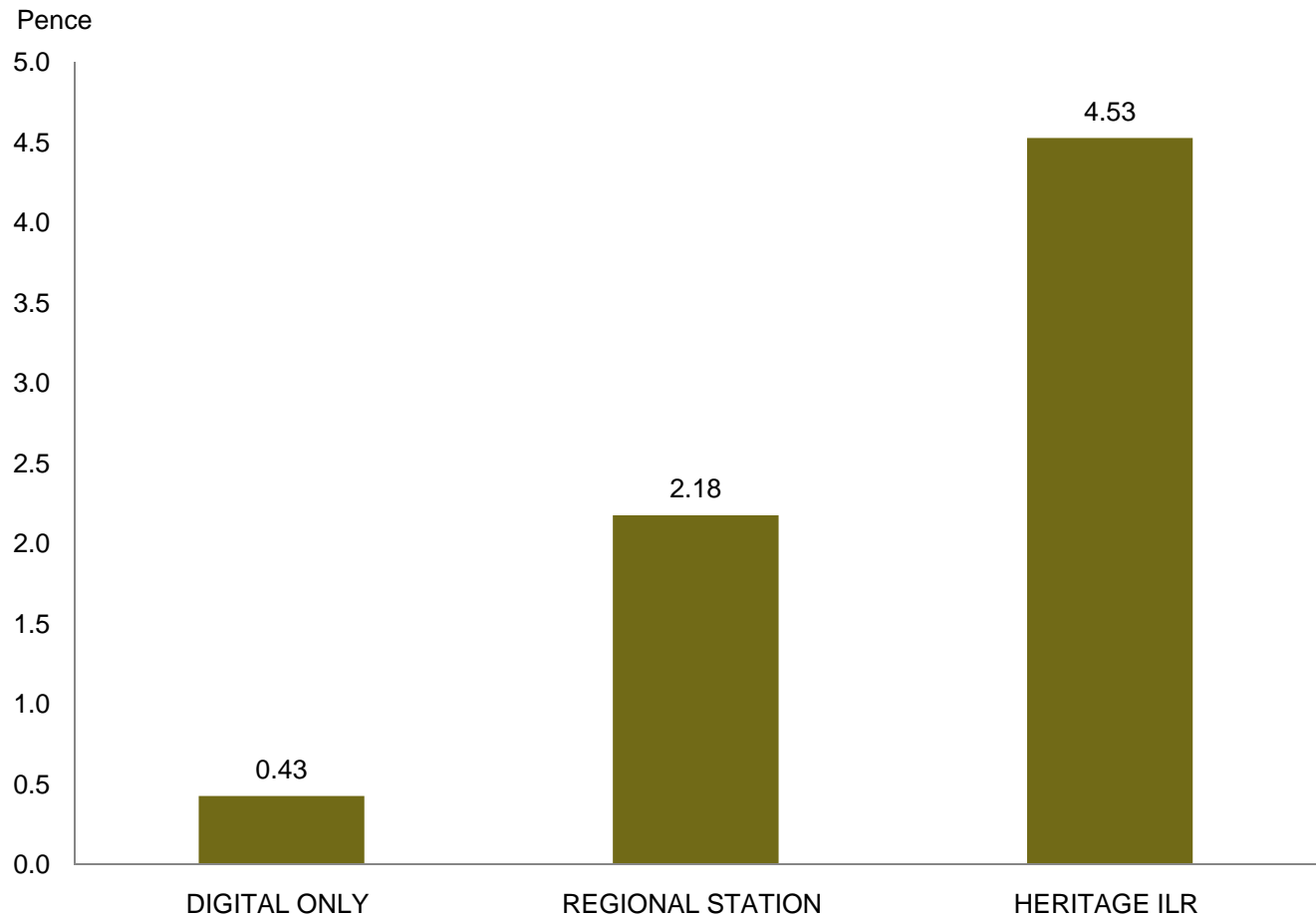
Fragmentation is reducing value to advertisers



Listening fragmentation (both platform and station led) has resulted in lower 'yields' for relatively new market entrants...

- Regional station's revenue per listener hour around half that of ILR counterparts
- Most ILRs benefit from share deals; being no.1 in local market; and low local wastage for local advertisers
- Digital yield very low given lack of reach, frequency and local content

Average revenue per listener hour (ad yield) for selected stations 07/08



Source: Nielsen, O&O Analysis (selected stations from major conurbations)

(4) DISINTERMEDIATION

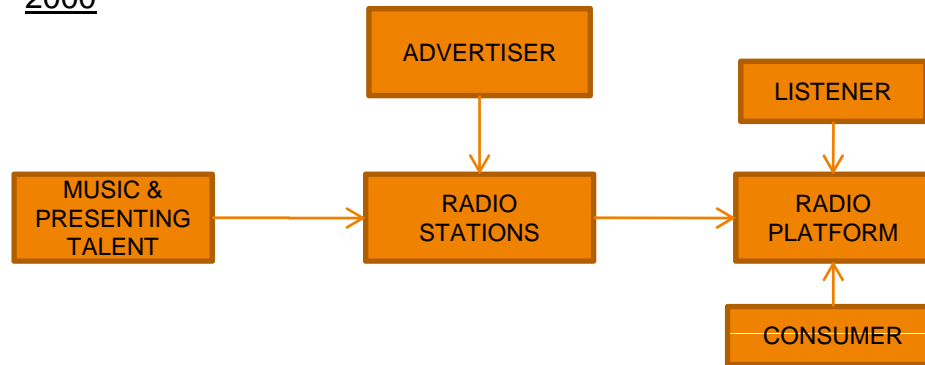
The threat to traditional radio model



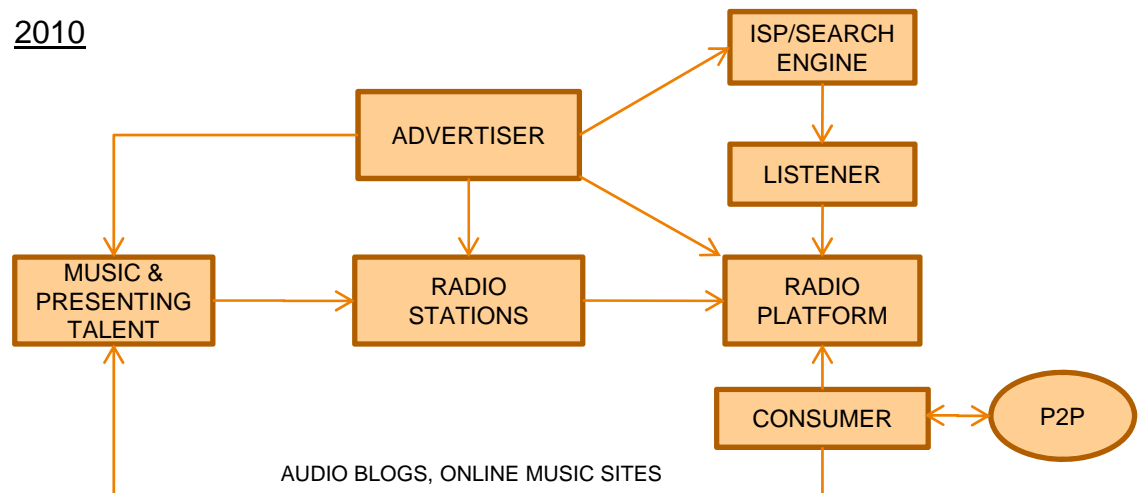
Advertisers may no longer have to rely on radio stations to connect with the audio consumer...

- Advertisers used to have only one route to radio listeners/consumers - and they paid a premium for the highest reach route
- ISP/Search engine aggregators (Google, Yahoo) take share of revenues from content sites
- Content aggregators (Spotify, iTunes, Apple, Tun3r) provide access to listeners
- Advertisers are also developing deals with music and presenting talent

2000



2010



THE IMPACT OF THE RECESSION

Previous four UK recessions as guides



The implicit assumption is that 2008 to 2010 will be similar to 1989 to 1991...although it can be argued that the squeeze on consumers will be greater than 1989 to 1991, and potentially more like the 1973 to 1976 downturn...

	REAL CONSUMER SPENDING DECLINE	CORPORATE PROFITABILITY DECLINE	REAL DECLINE IN DISPLAY ADS
1973 to 1976 Deleveraging recession with stagflation, rising oil prices and rigid cost base (union power)	(3.8%)	(-33.5%)	(22.7%)
1979 to 1981 New tighter monetary policy focused on inflation, but signal of shift to lower tax consumer economy (Washington Consensus)	(2.9%)	(9.7%)	+24.0%*
1989 to 1991 Tighter monetary policy to deal with rising inflation and assets but with more flexible cost base	(1.0%)	(16.5%)	(14.7%)
2000 to 2003 B2B recession after dotcom bubble bursts eased by loose monetary policy	+6.5%	(3.2%)	(7.7%)

* ITV's strike in 1979 pushed revenue into 1980/81 - mitigating the impact of recession

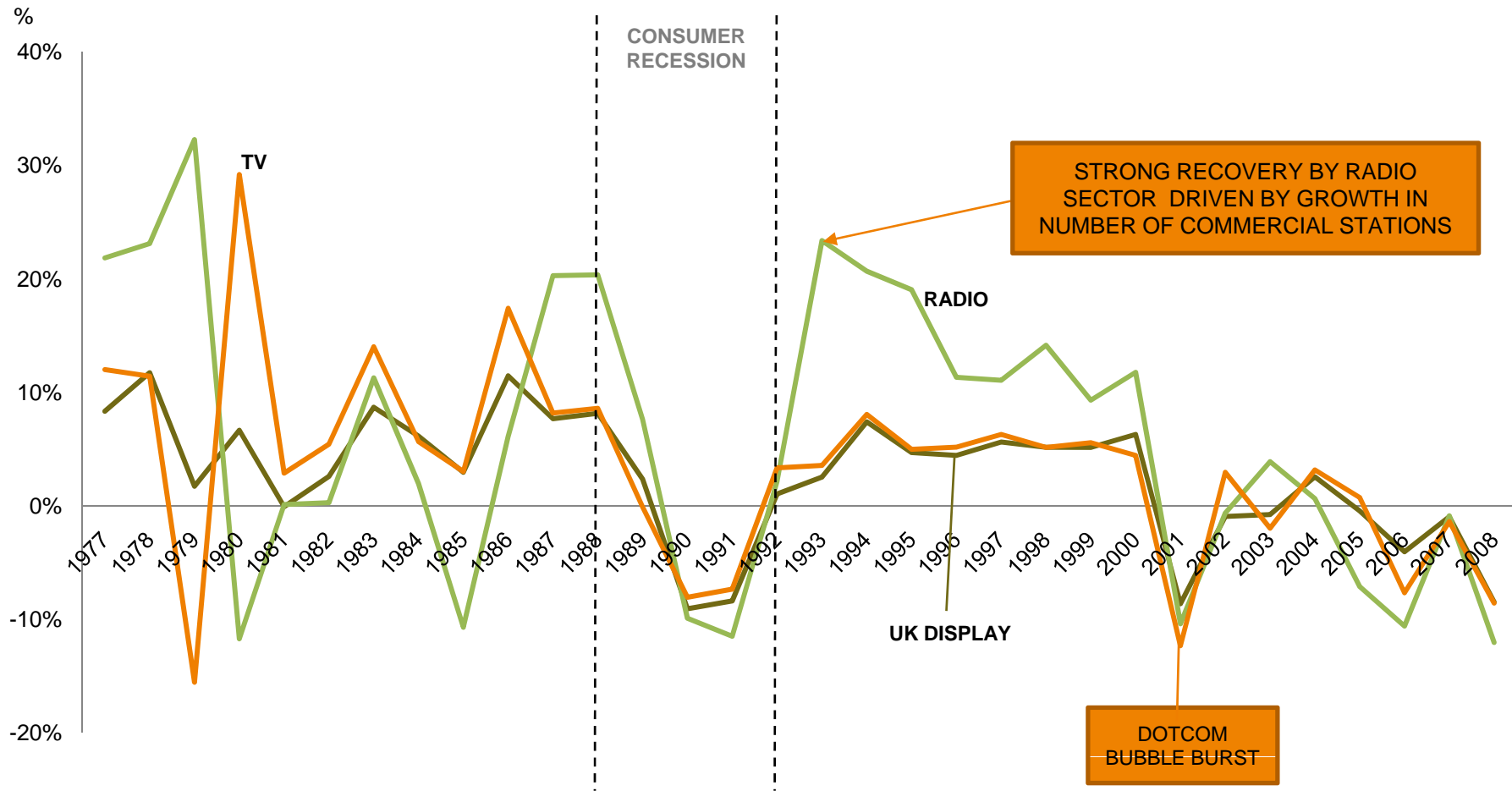
THE IMPACT OF THE RECESSION

Impact on radio industry



...during the last consumer recession radio revenues were hit harder than TV and overall UK display advertising sector...post recession recovery of radio was stronger than other display advertising media, driven by newly launched commercial stations...

Year on year growth rates in real terms, 1977-2008



Source: Rajar, O&O Analysis

THE IMPACT OF THE RECESSION

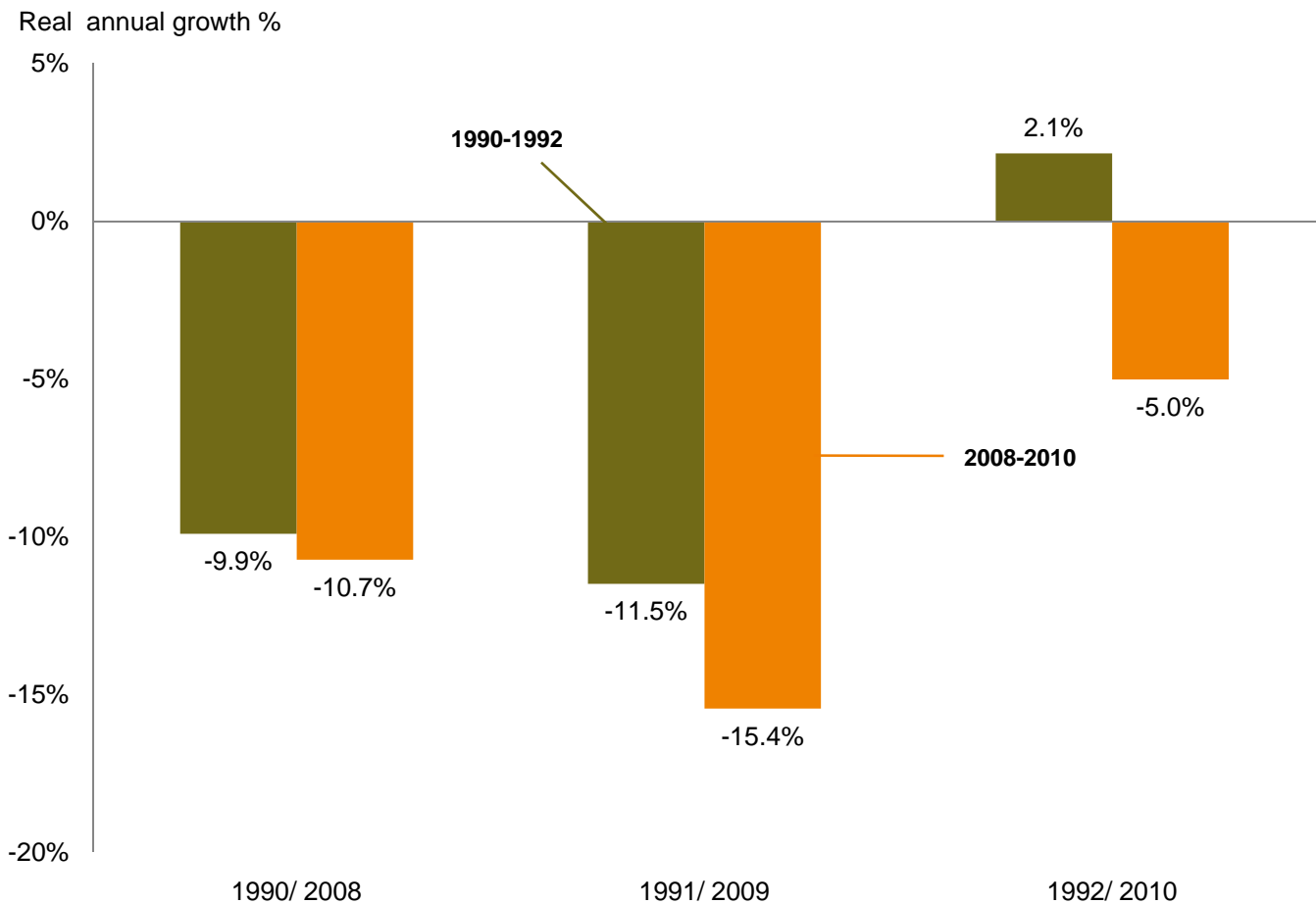
Impact on the radio industry



...rate of recovery from the current recession is unlikely to be as strong as in the early nineties...

- Decline in revenues likely to be greater than during last consumer recession
- Growth in number of commercial stations in 90s ensured market returned to growth in 1992
- Substitution to internet will reduce the strength of radio's recovery - unlikely to come until 2011

Radio annual growth rates, real terms – early 90s and current recession*



*Note: 2008-2010 revenues include sponsorship and inflation assumed to be 2% in '09 and '10
Source: AA, RAB, Oliver & Ohlbaum Trends

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The Fight Back

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DIGITAL TIPPING POINT

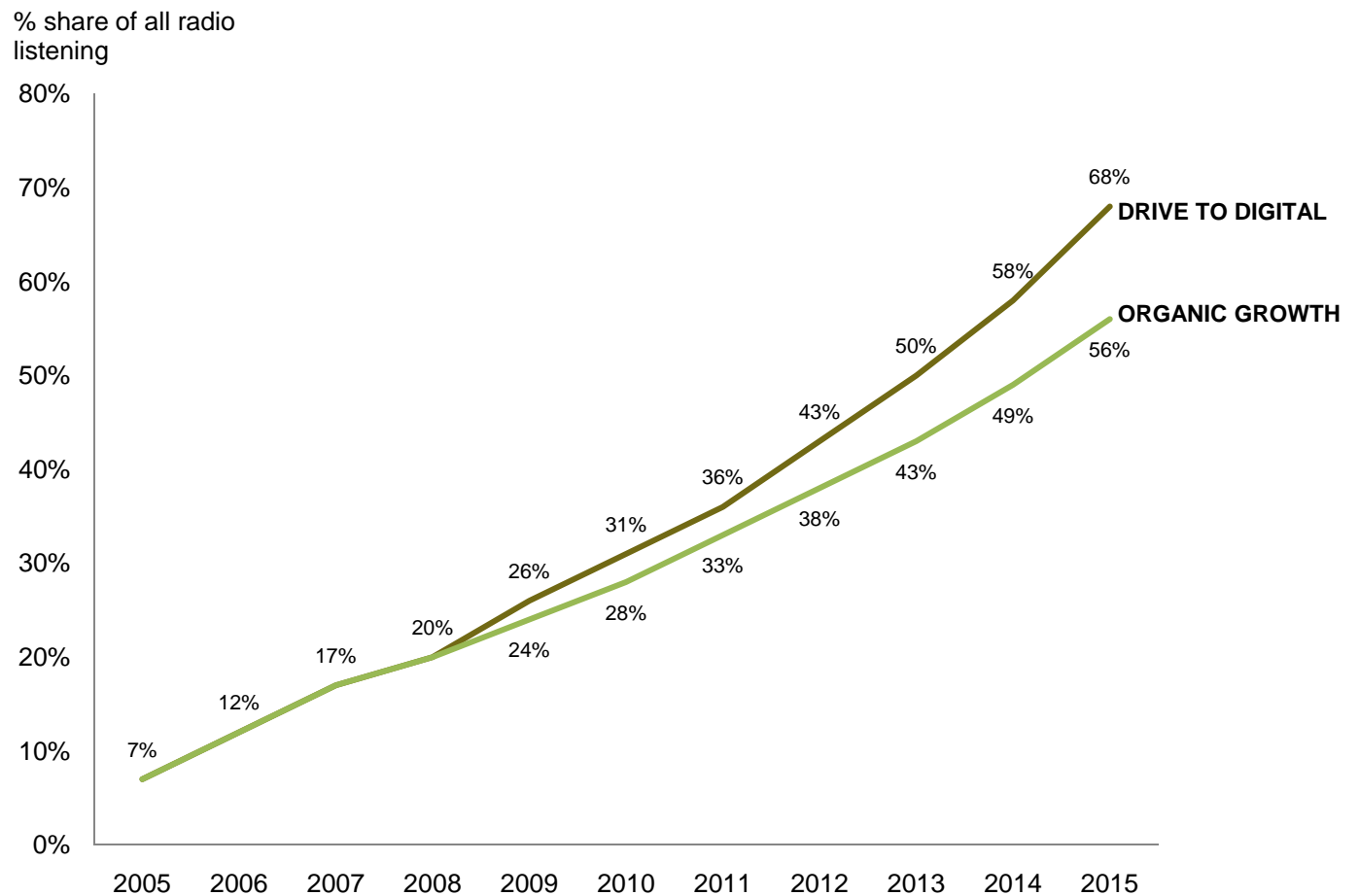
Is 2015 switch off likely?



The Digital Britain Report detailed the criteria that should be met before a likely DSO date can be set...

- Listening criteria of 50% met by 2013 if Digital Radio Upgrade timetable followed
- DSO to be announced at least 2 years in advance once criteria met suggesting 2015 switch off
- Is 2 year timeframe long enough?
- Could this be costly/contentious?
- End of dual transmission

Total digital share of listening, 2005-2015



Source: Digital Britain Report

REVISED REGULATION

Five potential revisions to regulation



Over the next few years there could be a number of favourable regulatory changes for the industry...

	POTENTIAL REVISION		DETAIL		IMPACT
1	LOWER TRANSMISSION COSTS?	→	<ul style="list-style-type: none">Contract price reductions a CC condition of Arqiva/NGW merger	→	<ul style="list-style-type: none">Cost base savings
2	NEW ROYALTY FEES?	→	<ul style="list-style-type: none">Royalty rates for commercial radio reviewed in light of changed music consumption	→	<ul style="list-style-type: none">Cost base savings?
3	NEW AD/PROMOTION RULES?	→	<ul style="list-style-type: none">Ofcom has launched review of broadcasting code	→	<ul style="list-style-type: none">Increased sponsorship and promotion opportunities (by end of 2009?)
4	CHANGE TO LOCAL CONTENT RULES?	→	<ul style="list-style-type: none">Myers report advises co-location and a better test for station localness	→	<ul style="list-style-type: none">Cost savings for co-locating stationsMore choice around local content
5	CHANGES TO RULES AROUND PROGRAMME NETWORKING?	→	<ul style="list-style-type: none">Relaxation of Ofcom programme guidance	→	<ul style="list-style-type: none">Programme networking in breakfast/drivetime? Likely?

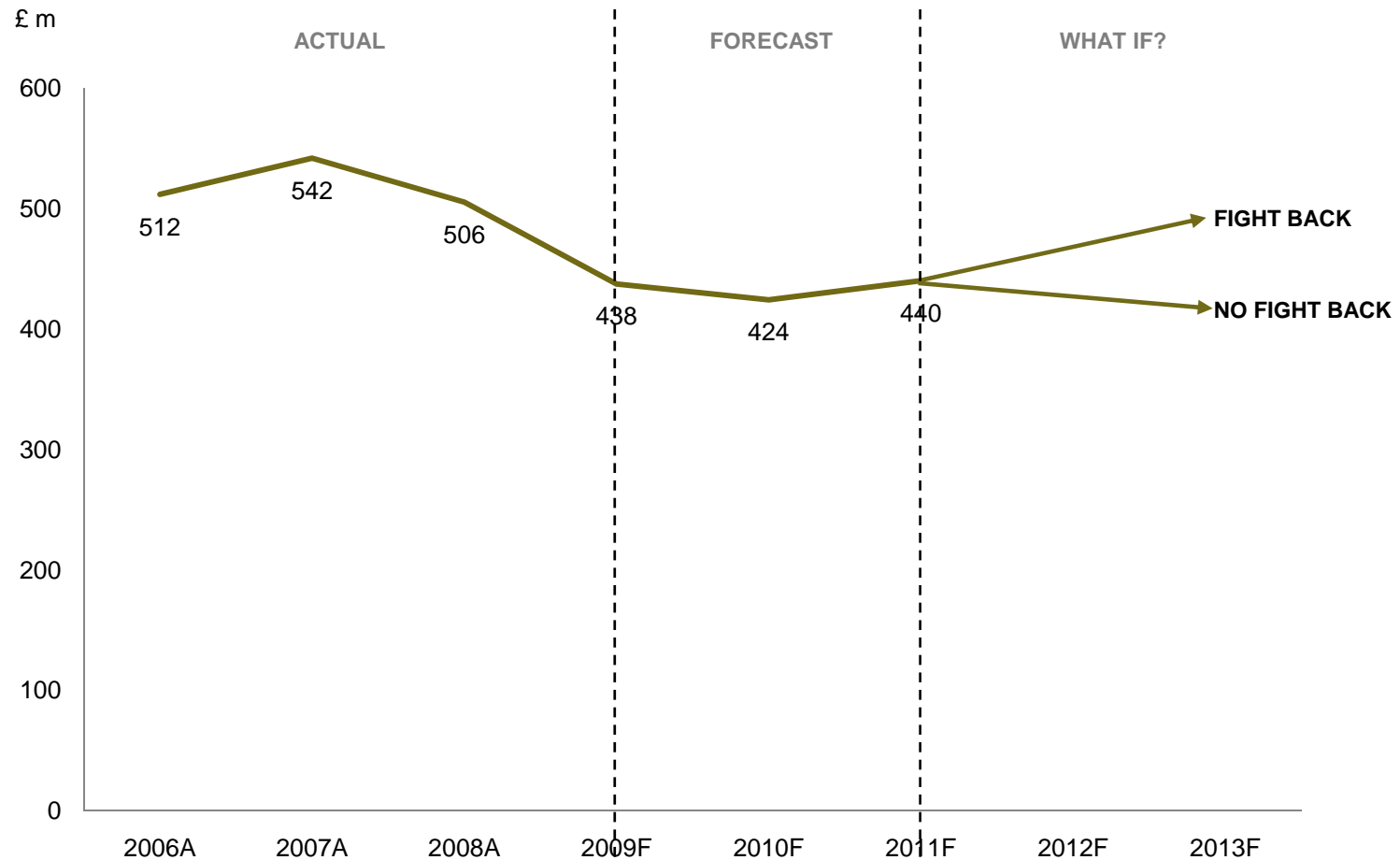
ECONOMIC RECOVERY

Growth will return...sooner than many have predicted



The market will recover with some marginal growth in 2010 and 2011. Any subsequent growth will be dependent on the radio sector restructuring and developing new business models...

Radio net advertising revenues, 2006-2013 (nominal terms)



- Already evidence of economic recovery in UK manufacturing sector
- Worst of recession effect felt in 2nd half of 2008 and 1st half of 2009
- Smaller decline in 2010 for advertising with flat S&P revenues
- Recovery in 2011 driven mainly by S&P growth
- Growth from 2011 dependent on commercial radio strategy

Source: Oliver & Ohlbaum Trends

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NEW CONSUMER PROPOSITIONS

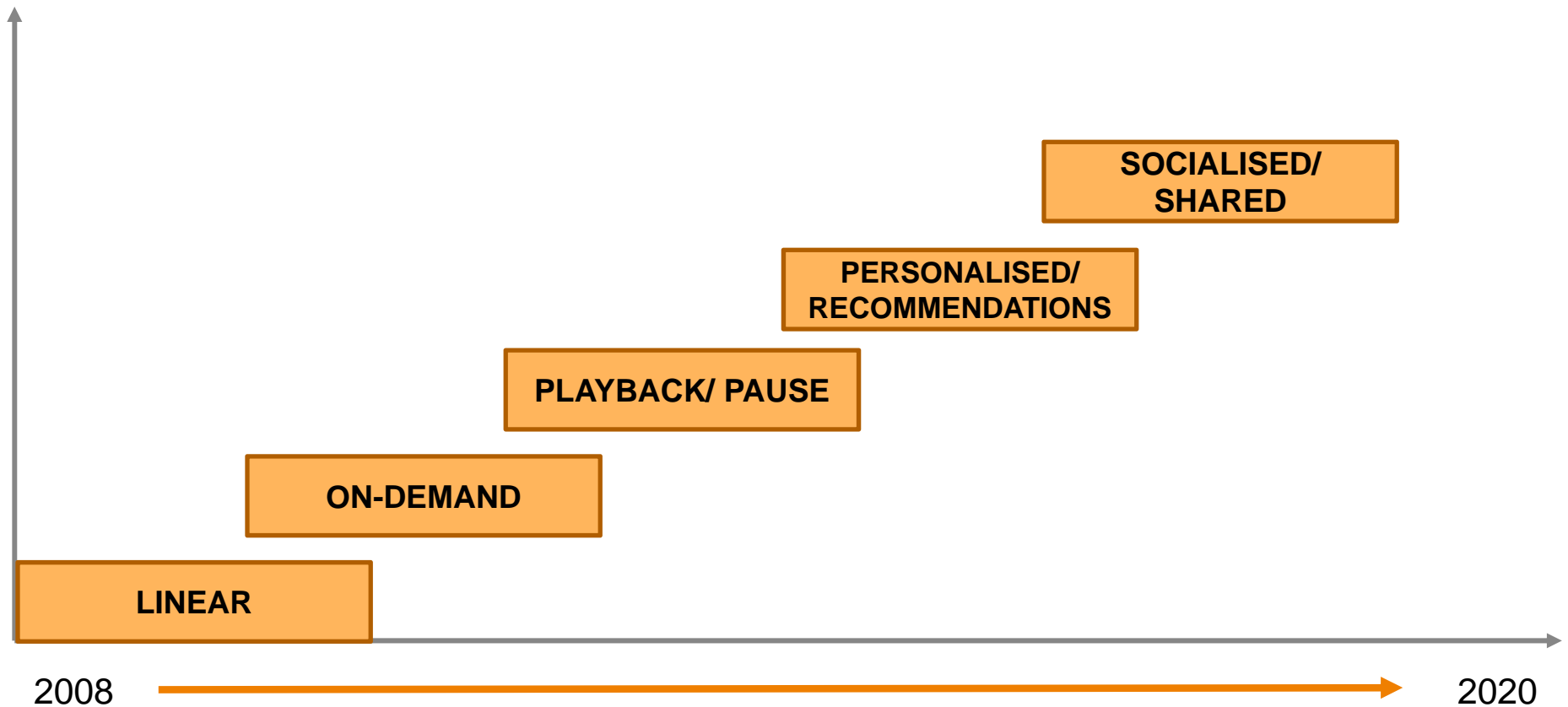
New opportunities on the web



The sector needs to adopt propositions that make the most out of broadband connectivity and new devices...

Radio online strategy to 2020

VALUE ADDED



Source: Oliver & Ohlbaum Trends

CONSOLIDATION

Mergers and station closures will lead to stronger spot advertiser proposition



Restructuring critical to ensuring commercial radio remains a key part of a marketer's portfolio of spend...

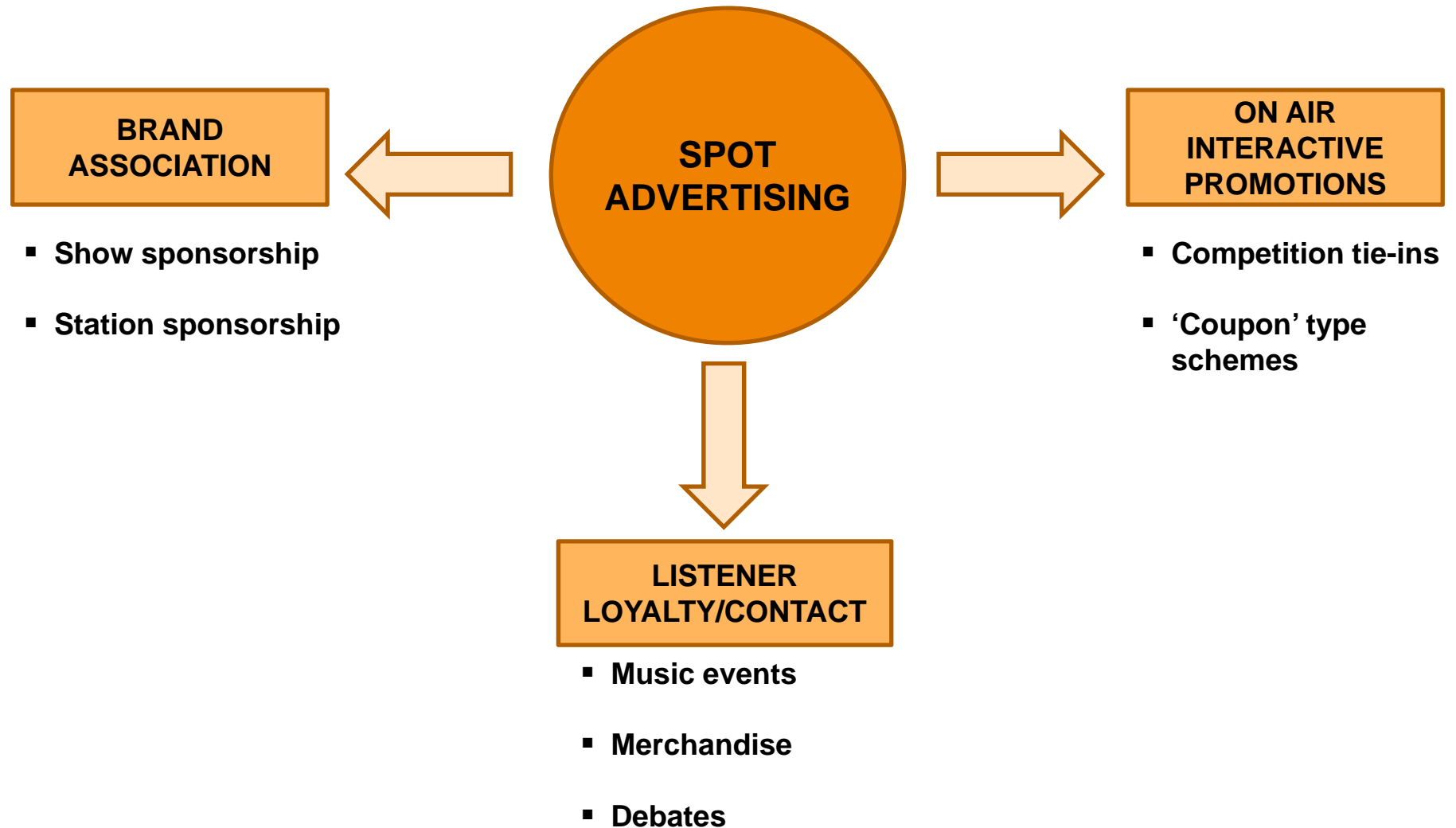
	NEW COMMERCIAL PROPOSITION - 2011	% OF ALL ADVERTISING	DETAIL
TARGETED NATIONAL ADVERTISER	<ul style="list-style-type: none"> • 5 to 10 targeted and branded national services 	20%	<ul style="list-style-type: none"> • Narrower age and gender focus OR • Passion group/ interest focus
BROAD NATIONAL ADVERTISER	<ul style="list-style-type: none"> • 3 to 5 broader quasi-national networks • Metropolitan ILR network 	50%	<ul style="list-style-type: none"> • Mainly networked shows • Household name presenting talent • National brands
LOCAL ADVERTISER	<ul style="list-style-type: none"> • Metropolitan ILR network • Ultra-local stations • Community stations • Local inserts on quasi-national networks 	30%	<ul style="list-style-type: none"> • Mainly local output

NEW BUSINESS MODELS

Breaking out of the spot ad model



Industry must drive revenue through means other than spot advertising...



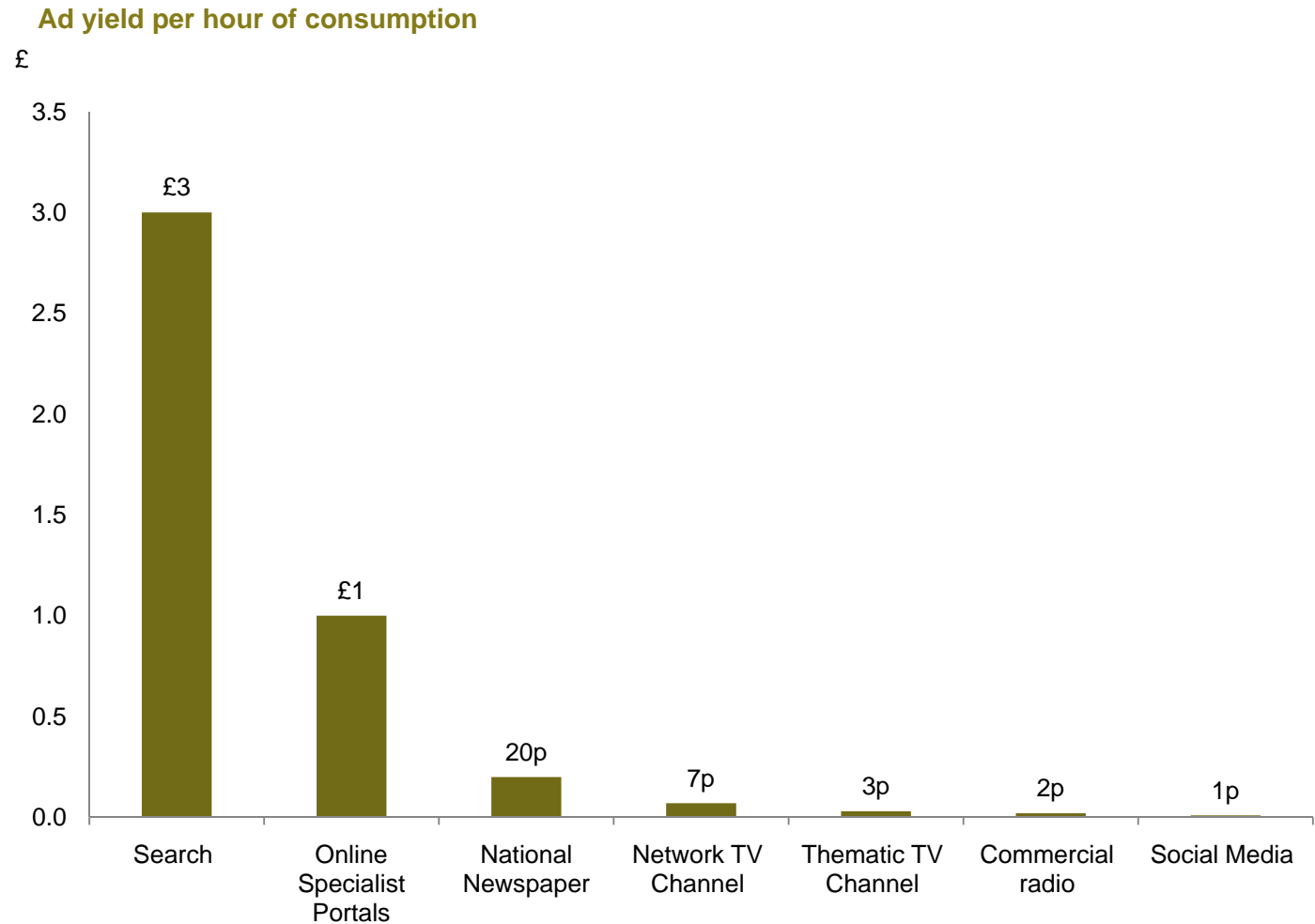
NEW BUSINESS MODELS

Ad targeting online – higher advertising yields?



The industry has an opportunity to increase its comparably low yields by improving the level of audience targeting online...

- Two distinct business models:
- Low yields:** high reach with little targeting e.g. TV, press and radio
- High yields:** lower reach with specific targeting e.g. Google, specialist websites
- Higher brand loyalty and more online listening should translate **into higher yields for radio**



Source: Oliver & Ohlbaum, Human Capital, company accounts

IN CONCLUSION



Sector faces a number of structural changes as well as a recession

- Shift of ad spend
- Competition intensity
- Fragmentation
- Disintermediation

But 2010 to 2012 likely to see three catalysts for change

- Re-regulation
- Push to digital
- Economic recovery

To take advantage of this the sector must

- Consolidate in a way that makes sense for listeners and advertisers
- Develop an enhanced proposition on broadband platform and new devices
- Look beyond the spot advertising model