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23rd February 2016

Dear Ed,

Radio deregulation

In your letter to me of 29 September 2015 you asked Ofcom to examine the scope to deregulate the licensing of commercial radio, in order to enable DCMS to consider consulting on options for legislation this year. I am writing to set out our conclusions.

You asked us to consider what options there are to reform the current regulatory requirements in three areas: music formats; local content, including news; and the local production of material. You asked us to examine the scope for deregulation wherever possible, and to consider how to create a level playing field for analogue and DAB (Digital Audio Broadcasting) radio services.

As you know, Ofcom's approach in this area has been broadly deregulatory over the last ten years, and given the evolution of the sector we think this is a sensible point to consider whether the statutory regime remains appropriate. The number of consumers listening to digital radio is continuing to climb steadily: 42% of all radio listening is now to digital services, and DAB is available in over half of all homes. However, the majority of commercial radio listening is still to analogue services, and analogue accounts for the majority of the industry's revenue. Consolidation and a focus on building national brands (for example, Kiss and Radio X) have enabled commercial radio to maintain growth, but online audio services are providing increasing competition, particularly among younger people (who spend 40% of their time using online streaming services such as Spotify, compared to just 9% of all adults). In addition, the BBC still accounts for the majority (53%) of all radio listening.

The options for deregulation that we set out below would require primary legislation to remove or amend existing statutory rules. In developing them, we have considered the current state of the commercial radio sector and trends in consumption of radio and audio more generally, as well as take-up of digital radio. A summary of our findings is set out in the accompanying annex, and the research that we have conducted will be published in full on our website alongside this letter and the annex.

Music formats

The current statutory framework requires that to promote choice for listeners, radio services must differ from other available stations in the music and speech that they broadcast. Ofcom delivers this by placing conditions in each station's licence about its output. This applies to

all local and national commercial radio stations, and across both analogue and digital services. We have already reduced the detail and number of requirements in local analogue service licences as far as we think is possible under the current law. Requirements for digital services are less detailed.

There has been a huge increase in the availability and the number of different sources of music since this statutory requirement was introduced, and we think that there is scope for significant deregulation here. This could be done at local or national levels, or at both. Taking each in turn:

- there are three national analogue commercial radio services. The law currently requires that one service must be non-pop music and another must be speech-based; there is no specific requirement on the third. One potential form of deregulation would be to remove these requirements. Doing so during the current licence period would need to be considered carefully since this would mean the current licence-holder for the non-pop music service - Classic FM - would be free to change the output of that service if they wished (especially given that it is broadcast on the technically-superior FM waveband). An important consideration from our analysis is that the audience for this service is currently less likely to access this type of content elsewhere, thus increasing the impact of any changes to its format or availability;
- if local analogue stations were free to play whatever music they wished, it is likely that they would choose to play mainstream popular music. We think the impact of removing regulation here on listeners would be relatively limited. Most local analogue services already play mainstream pop music, and this is generally popular with audiences. There are a small number of specialist services that do not currently play mainstream pop music, and these stations might decide to switch to a more mainstream output. To the extent that listeners are not able to access alternative sources of specialist output – for example through digital radio or streaming services – this could result in a loss of choice for those listeners, but the impact is likely to be very small;
- the availability of a large number of services on national and local digital radio offers an alternative source of choice for many listeners. The fact that there is already a large number of services on DAB suggests that there would continue to be a range of different output for listeners if digital format regulation were removed, although there may be some loss of particular specialist services if providers consider that they can generate more revenue from a more mainstream format. Again, for many listeners, specialist streaming services will provide an alternative.

If Government did choose to remove these requirements (and any relating to localness), the current system for awarding new analogue licences would need to be reformed. Currently, it operates on the basis of an assessment of the particular characteristics that a service would bring ('a beauty contest'). It would be necessary to consider what alternative competitive award process might be suitable, with one possibility being award under an auction process.

Local news and other local content

Section 314 of the Communications Act 2003 requires Ofcom to ensure that each local analogue station provides an appropriate level of local material. There is no parallel requirement for digital services. "Local material" includes both local news and other types of local content such as travel, weather and "what's on" information.

We have considered news separately from these other types of content, and carried out research on the role and public value of local news delivered by local commercial radio services in today's media landscape. As well as informing listeners, local journalism can promote community cohesion and encourage local democratic debate. Our research suggests that the provision of local news on commercial radio in particular is of value to consumers: local commercial radio reaches many more people than other sources of local news such as BBC Local Radio services and local newspapers¹; and listeners value the accessibility of regular local news bulletins which can be consumed "passively", rather than needing to be sought out. Local commercial radio also has a role in contributing to the plurality of local news sources.

However, local news is relatively expensive to produce, and impartiality rules prevent news being sponsored. In the UK, where local AM stations are no longer required to provide local news, and in other countries where similar requirements have been removed, the evidence shows that stations do not generally choose to provide local news.

Our analysis of the other types of local content including travel and weather suggests that this content would be likely to be provided on local radio if regulation were removed, since it is cheaper to provide than news, and can be sponsored. We also consider that if some stations were to cease providing these elements of local content in the event of deregulation, the impact on listeners would be limited because there are a large number of alternative sources for this information.

We therefore see a case for removing the requirements for most forms of local content. However, it is likely that complete deregulation would result in at least some local stations deciding not to provide local news. In light of the findings about the social importance of local news on local commercial radio, Government may consider it preferable to retain a requirement on all local stations to provide a minimum amount of local news.

Locally-made programming

If Government wishes to continue regulating for some local content to be carried by commercial radio stations, it will also need to consider whether to retain rules on where it is produced. Section 314 of the Communications Act 2003 requires that "a suitable proportion" of a local analogue commercial radio station's local material is locally-made.

In practice, this means that all local FM stations provide at least seven hours each day of locally-made programming. This requirement can help ensure that local content is relevant to the local area, as local newsrooms and locally-based presenters mean that stations can react promptly to breaking news and reflect back to listeners their local area. There is a parallel here with ITV, which is required to have studios in each region for which it provides regional news. However, in practical terms most types of local content could be produced in any location, and there is a question about whether, and to what extent, the location of production affects the local relevance of output.

Our research suggests that where programmes are made is of less concern to listeners than their quality and local relevance. If the requirement to make programming locally were removed, we think it likely that some stations would continue to provide locally-made programming as a point of commercial differentiation to attract listeners and advertisers. However, since locally-made programming is relatively costly to make because of the need to maintain separate studios and presenters, it seems likely that if regulation were removed some stations would choose to reduce or cease locally-made programming. In particular,

¹ For example, BBC Local Radio reaches only 16% of adults, whereas the BBC's national services reach 60% of adults and local commercial radio reaches 51%.

services that are part of a group or network are likely to have commercial incentives to consolidate studio facilities: half of all local analogue stations fall into this category. Against that, it might help to make some stations more economically viable because they would incur lower costs, and it may also be the case that the costs of maintaining separate studios and presenters could be spent instead on producing high quality, locally-relevant content.

Our analysis suggests that complete removal of the requirement for locally-made programming may cause concern amongst some stakeholders in parts of the UK, particularly in Scotland, Wales and Northern Ireland. It may be that the extent to which this is regarded as a significant issue differs between different areas and nations of the UK, so Government may wish to consider whether to retain some level of regulation of the place of production to reflect this.

Levels of regulation for analogue and digital services

You asked us to consider what regulation might apply to digital radio on local content and production. There are currently no localness requirements on digital radio. However, in practice around half of the services broadcasting on digital radio are simulcasts of existing local analogue services, so the local material carried on the analogue version of these services is also available on the digital version. The remainder of the stations on digital radio (which are not simulcasts) have generally chosen not to provide local content.

If any localness requirements – whether the current arrangements, or a reduced level – were extended to digital radio, the impact on these digital-only services would be to increase the level of regulation, with resulting cost implications for them (although the majority of these stations are provided by the major groups, which may be able to source local news for these stations from their other stations in the area).

In light of the fact that the majority of commercial radio listening is still to analogue services, and that listeners to local digital services can already access some local material through digital simulcasts, we think that there is not a strong case for additional regulation, i.e. for 'levelling up'. Government may wish to revisit the issue at a later date, potentially when digital becomes the majority platform for radio listening.

Community radio

Finally, you asked whether there is a need to retain a regulatory distinction between community radio and small-scale commercial radio if both types of service are going to be carried on the same digital multiplexes. If Government decides to pursue deregulation of commercial radio, our view is that there nevertheless may still be a case for continuing to regulate to secure the particular public policy objectives delivered by community radio. As you know, we are currently running a small-scale digital radio trial, and the outcome of this may also be helpful in informing decisions about community radio regulation.

I hope that you find this analysis helpful.

Yours sincerely,



Sharon White

Annex: Summary of findings

To inform our response, we have drawn on a variety of different sources:

- Ofcom's previous reviews of localness on radio (2009)¹ and music in radio formats (2015)², and experience of regulation since;
- Ofcom's ongoing quantitative research on listeners' consumption of, and attitudes toward, radio and other media published in our Communications Market report³;
- A new, qualitative research study on listener priorities for content on local commercial radio;
- Analysis and case studies on whether different elements of content would be likely to be provided in the absence of regulation;
- A study of local news delivery in a sample of local markets across the UK.

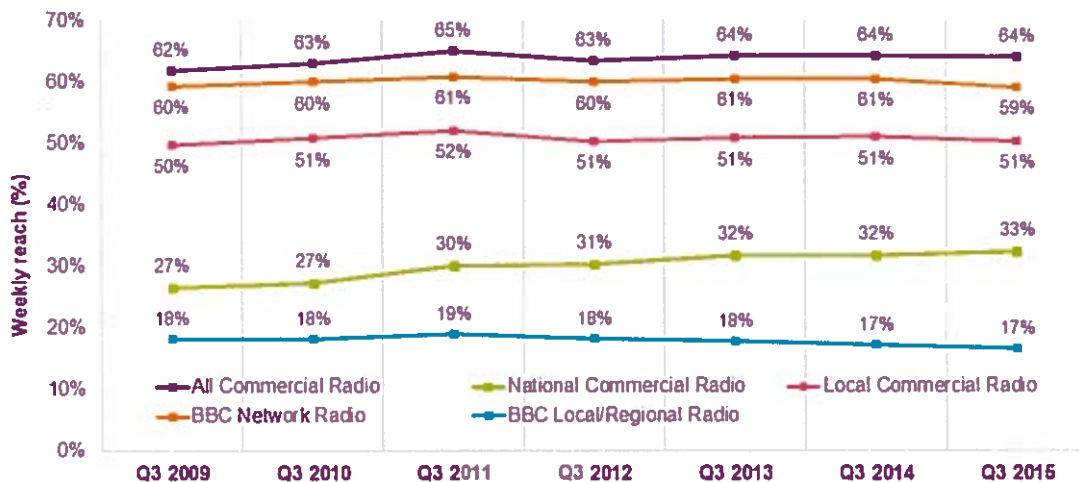
The summary of Ofcom's findings is set out in the following sections, corresponding to those in our letter.

Background and market developments

The commercial radio industry in the UK began in 1973 as a system of local analogue radio (broadcast on FM and AM) stations. The 1990s saw a large expansion in the number of local commercial stations. They also saw the introduction of three national commercial radio licences, one of which is on FM (currently Classic FM) and two on AM (currently TalkSport and Absolute Radio).

As a result, analogue commercial radio today is comprised of 291 local stations (between 2 to 8 in any single local area) and three national stations. The BBC has five national network stations and 43 local/regional stations. The average weekly reach of these different categories of service to UK adults is set out in the table below.

Reach of radio services by type of service, 2009 to 2015



Source: RAJAR, Ofcom analysis

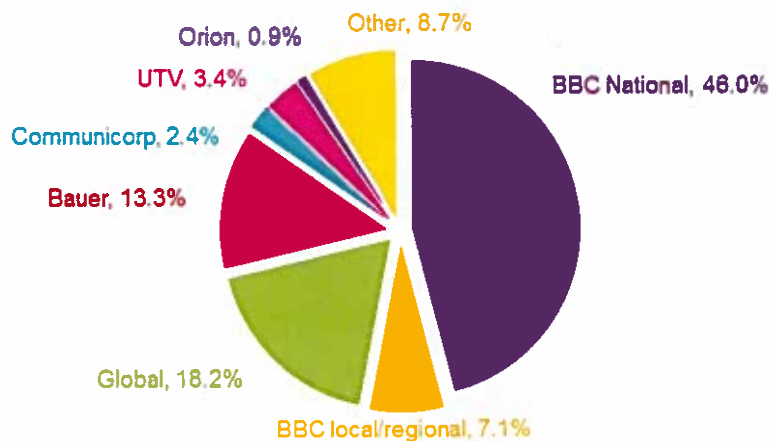
¹ 2009 review of Localness: <http://stakeholders.ofcom.org.uk/consultations/radio/>

² 2015 review of Music in radio formats <http://stakeholders.ofcom.org.uk/consultations/formats-review/>

³ Ofcom's Communications Market Reports: <http://stakeholders.ofcom.org.uk/market-data-research/market-data/communications-market-reports/cmr15/radio-audio/>

As shown in the table below, the BBC accounts for the majority of radio listening measured by share of listening hours. The commercial radio sectors' three largest groups (Global, Bauer and UTV) operate half the commercial stations and account for two-thirds of commercial radio listening.

Share of radio audience by station owner, 2015



Source: RAJAR. Base: National Total Survey Area

The majority of listening is still via analogue radio services and these account for the majority of commercial revenue. Commercial radio revenue grew at a compound annual growth rate (CAGR) of 2.1% over the five years to 2014 to reach £483m per annum.⁴

Digital radio development

In the 1990s commercial digital radio multiplexes were licensed at both national and local levels. This allowed for up to 15 national commercial services and for up to 15 local services in each of 50 local areas (more in London). A second national commercial radio multiplex will launch in March 2016 providing at least 15 new national commercial radio services.

DAB radios are now widely available: over 50% of households have a DAB set, 75% of new cars come with DAB as standard, and 15% (5m) of all cars on the road have a DAB radio.⁵ Total digital share of radio listening has increased to 42%.⁶

⁴ Further detail is set out in section 3.1.2 of the 2015 CMR
http://stakeholders.ofcom.org.uk/binaries/research/cmr/cmr15/UK_3.pdf

⁵ <https://www.gov.uk/government/speeches/digital-ministers-address-to-the-worlddab-assembly>

⁶ DAB penetration and total digital listening as reported by RAJAR Q4 2015
http://www.rajar.co.uk/content.php?page=listen_market_trends

DAB radio take-up, and total digital and analogue share of radio listening



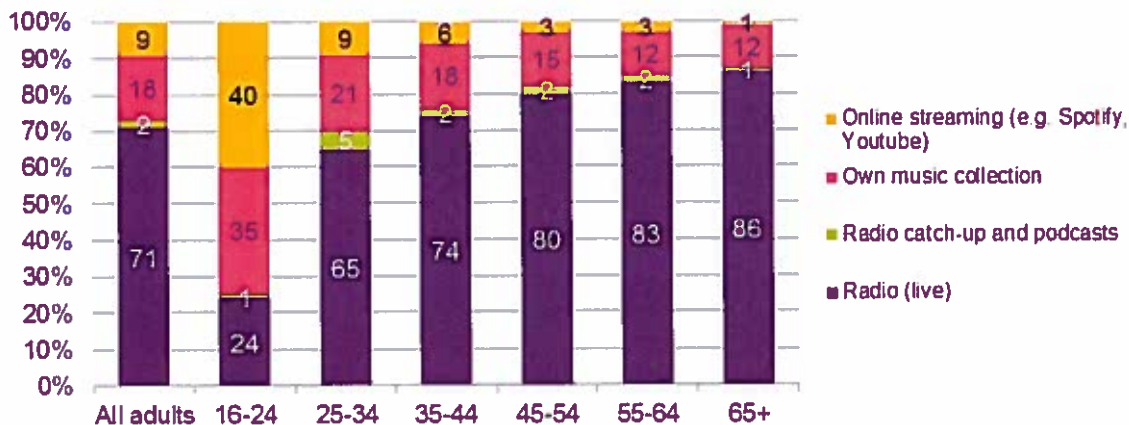
Source: RAJAR, Ofcom Digital Radio reports

As well as DAB, there are now thousands of radio services available online alongside on-demand audio services. Ofcom's research suggests online audio services are now used regularly by 30% of the UK population.

However, total consumption of audio is still concentrated on the traditional media of broadcast radio (accounting for 71% of listening) and own music collections (18% of listening). The use of online streaming services represents only 9% of the listening time for the average adult, but this varies greatly by demographic group, with online streaming representing 40% of 16-24 year-old's consumption (more than broadcast radio), but only 3% for those aged 45-54.⁷

Share of listening hours by source, by age group

Proportion of listening time (%)



Source: Ofcom Digital Day 7-Day Diary, Q1 2014

⁷ Further details on use and share of listening by different platform is published in section 3.1.3 of Ofcom's CMR 2015 http://stakeholders.ofcom.org.uk/binaries/research/cmr/cmr15/UK_3.pdf

Requirements for music formats

As explained in the letter, radio services are currently required under the statutory scheme to differentiate themselves from others in terms of the music and speech that they broadcast.

The current requirements are that one national analogue commercial radio station provides non-pop music (currently Classic FM) and that another provides a speech-based service (currently TalkSport). It is possible that, if these requirements were removed, the licence holders for these services might consider they could increase their revenues by changing to more mainstream output. We consider that the commercial rationale for such a change may be greater for the national FM service. The incentives for a change are likely to be weaker for a service on AM due to its inferior technical audio quality, and the increasingly fewer number of AM receivers in the market.

Such a change may reduce the choice of services for analogue-only listeners. If, for example, Classic FM ceased to be provided on FM but continued on DAB, half of the station's audience (2.25m) currently listen on analogue only and therefore would need to switch to DAB, and around half of these would need to buy a new radio (as 50% of people do not yet have DAB).

As set out in the letter, there is also a requirement to secure a diversity of local commercial analogue stations. Responses to Ofcom's 2015 music in radio formats review, and our international case studies⁸, suggest that if music formats were removed, the vast majority of local services would play a mix of broad music (across genres) and mainstream popular music. The impact of this on the majority of listeners would be relatively limited. This is because 77% of analogue local stations already have a format requiring them to play mainstream popular music⁹ and qualitative research suggests listeners expect local stations to play music catering to the general tastes of the local area (which they associate with a mix of younger and older popular music rather than coverage of more niche music genres). This suggests that most local stations would choose to continue to play, and most listeners would choose to listen to, mainstream popular music.

However, a number of local stations do not currently play mainstream popular music: 23% have formats requiring a specialist genre of music (rock, dance, easy-listening) or music for a particular ethnic audience. It is possible that some of these specialist music services may choose to play more mainstream music of wider commercial appeal. Further diversity of music is provided by DAB stations and online streaming services, and in our research some listeners said they used these sources already where they had more niche music interests. However, if listeners are not able to (or choose not to) access alternative sources of specialist output, or if there were to be a loss of choice in DAB services, this may result in a loss of choice for those listeners.

As explained in the letter, there is currently a regulatory requirement for range and diversity on DAB multiplexes. Our analysis suggests that the availability of a large number of services on national DAB will continue to offer an additional source of radio services for those listeners who have access to DAB radio. The BBC operates 11 national services on DAB.

⁸ From international case studies, regulation for music diversity has been reduced or removed in Norway, Sweden and Denmark, where the majority of stations play mainstream popular music.

⁹ Further detail is set out in Ofcom's 2015 review of Music in radio formats <http://stakeholders.ofcom.org.uk/consultations/formats-review/>

From March 2016 there will be at least 24 national DAB commercial services available to most households. This includes seven mainstream popular music, seven specialist music (from jazz to rock), three religious, two Asian and five speech-based. A further five DAB+ services will also be available for those with DAB+ radios.

Removal of the requirements for range and diversity is unlikely to lead to changes in the services which are already broadcasting mainstream popular music. It may lead to a loss of specialist services which, compared to mainstream services, tend to attract relatively small audiences and as such lower commercial revenues. However, given there are more services available on national DAB, we consider that overall there are greater incentives for differentiation of services, and the impact of the loss of any one specialist service on range and diversity would be limited.

Requirements for local material: local news and other local content

Local material includes local news and other types of local content such as travel, weather and “what’s on” information. We have considered the research and evidence available on these different elements of local material.

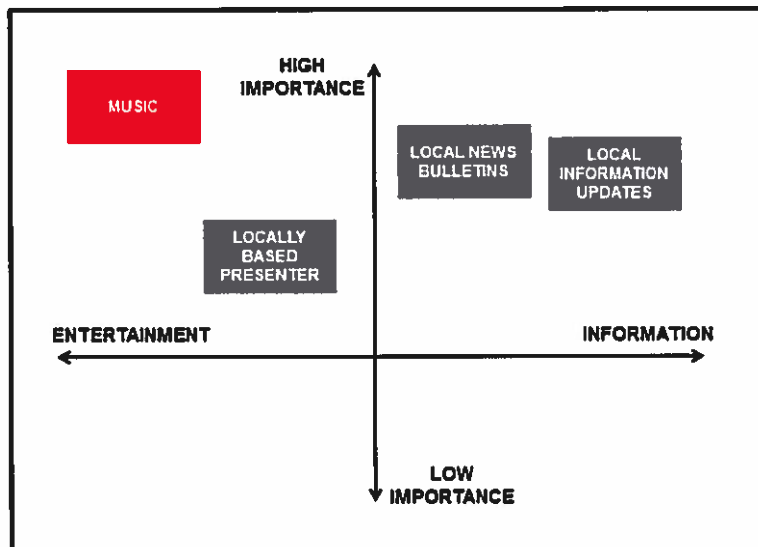
Our research suggests that local material on commercial radio remains valued by listeners. Quantitative research suggests that 45% of local commercial radio listeners particularly value local news on it, and 35% value it for local travel and weather information. Only 20% of local commercial radio listeners particularly value local presenters.¹⁰

Qualitative research also suggests that, after music, local news is the element of local radio services that listeners value most. The provision of other local information (e.g. travel and weather) on radio remains valued by listeners, though they consider provision on local radio slightly less important than local news. Other elements of local material linked to having locally based presenters, such as call-ins or competitions, were considered to be mainly entertainment and of less relative importance.¹¹

¹⁰ Ofcom's Third Public Service Broadcasting Review:
http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/psb-review/psb3/Annex_5_-_Radio_analysis.pdf

¹¹ Further details are set out in the qualitative research report *Local Commercial Radio Content* prepared for Ofcom by Kantar Media: <http://stakeholders.ofcom.org.uk/market-data-research/other/radio-research/>

Relative importance of different elements of content on local commercial radio



Source: Local Commercial Radio Content report, Kantar Media

Our research suggests that there are particular characteristics relating to the provision of local news on commercial radio which are of wider public value. These are:

- **Reach.** Commercial local radio remains a very effective way of reaching large numbers of people with local news. 27m adults (51% of the UK population) listen to local commercial radio each week. Local commercial radio listeners are typically younger, of lower socio-demographic classification (C2DE) and more ethnically diverse than listeners to other radio services, and a quarter of them (7m adults) do not listen to any other type of radio service. Local commercial radio's reach is significantly higher than other local media such as BBC local radio (17%), local newspapers (23%), local TV (available to less than half the UK, with a maximum reach where available of around 10%)¹² and hyperlocal websites (Ofcom research suggests that the reach of such websites is less than 10%)¹³. Listeners in the Nations also use local radio to access news about their Nation (26% in Scotland, 23% in Wales, 33% in Northern Ireland) more than for local news.
- **Accessibility.** Radio news is more accessible than other sources of news, such as press or online, where content must be sought out. In qualitative research respondents particularly noted the value of regular bulletins of breaking news throughout the day and that with radio they consume local news "effortlessly" or "passively" which they may not otherwise come across.
- **Plurality.** Our research suggests that commercial radio also contributes to a plurality of local news sources across the UK. Ofcom's main measure of plurality is the "share

¹² Based on Ofcom's *News Consumption in the UK 2015*:

<http://stakeholders.ofcom.org.uk/market-data-research/other/tv-research/news-2015/>

¹³ Internet Citizens Research

<http://stakeholders.ofcom.org.uk/market-data-research/other/telecoms-research/internet-citizens-15>

of news references” that each media represents.¹⁴ In 2015 the total share of references delivered by radio was 17%, predominantly through the national BBC services, with commercial radio representing 5% total share of references. Commercial radios’ contribution to news provision may be particularly important in Wales, where local daily newspapers only account for 1% share of news references (compared to 3% in England) and radio accounts for 20%, including a contribution from local commercial radio of 5%.

As set out in the letter, our analysis suggests that, absent regulation, at least some local radio services would decide to reduce or remove provision of local news. We base this view on analysis of trends in provision in the market:

- Since 2009, there have been nearly 80 changes of control of local stations: in seven of these cases involving acquisition by larger holding companies Ofcom was concerned they would not continue the level of local news delivery and varied the licence to maintain this. Separately, where requirements for providing local news have been removed on local AM stations, most stations no longer provide any at all.
- Our sample of current local news output suggests that most stations carry hourly news bulletins of around two minutes throughout daytime hours (6am to 7pm), adding to 20 to 30 minutes per day. However, the proportion of local news stories in these bulletins varied widely, from 10% to 50% of total stories between different stations. On most stations, the majority of stories in the bulletins were national or UK-wide stories rather than about the local area or region.

We also note that local news is relatively expensive to produce and represents a relatively high proportion of an average station’s programming costs. It is hard to monetise local news directly, as sponsorship of news is not allowed in order to protect impartiality.

By contrast, our analysis suggests other types of local information (e.g. local travel, weather) would be likely to be commercially provided on local radio and other sources. These are relatively inexpensive to source and provide, and are often monetised directly via sponsorship, which typically represents around a fifth of revenues to local stations. We note that this type of local information is also provided by a number of sources online at low or zero cost, with many offering greater localisation and customisation.

Requirements for locally made programming

As explained in the letter, locally made programming is currently required for most local analogue commercial radio services.

Our research suggests that locally made programming is of relatively lower value for listeners than other aspects of localness. In qualitative research, while many participants thought that local presenters were desirable, it was significantly more important that presenters were entertaining and/ or well-informed, and local material accurate and relevant, rather than simply being produced in their local area.

Our analysis also suggests that a requirement to provide locally made programming does not necessarily secure programming of local relevance. For example, in France and Canada, local stations are required to broadcast 3 hours or 6 hours per day of locally-made content:

¹⁴ Share of references is a bespoke cross media-metric which is derived from Ofcom’s consumer research. Respondents are asked which sources of news they use, and the frequency with which they use each source. The total number of references is then summed, and the references to each title or provider are aggregated and expressed as a share of the total.

despite this requirement, where specific types of content such as local news are not also required, they are not delivered consistently across the market.

As set out in the letter, absent regulation, we think it is likely that some local services would continue to provide locally made programming. Some services operating independently have suggested that locally made programmes and presenters are a key point of differentiation that attract their particular listeners and local advertisers (who represent a high proportion of their revenues).

However, the requirement for locally made material is a relatively high cost because of the need to maintain separate studios and presenters when programmes can now technically, and often more efficiently, be made centrally. Locally made programming is typically the highest single content cost for local stations as a proportion of their costs.

As a result, services that are part of a group or network (around half of stations) are likely to have commercial incentives to reduce, consolidate or remove local production. Following the 2009 Localness review, where Ofcom reduced the requirements for locally-made programming, changes made by services suggest that half of local radio stations – predominantly those in larger networks under single brands – would be likely to reduce local production. Many stations – particularly AM stations - have already moved to centralise production of local material (including local news production) and programming.

We also note that internationally, in countries where regulation to secure locally made programming on radio has been reduced, delivery by local commercial services has generally fallen to a minimal level or zero. This has happened, for example, following deregulation in Denmark and Norway.