

# ANNUAL MARKET REVIEW 2014

PRS market outlook 2015



by





# Annual market review 2014

## PRS market outlook 2015



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# EXECUTIVE SUMMARY

PhonepayPlus commissioned mobilesquared to conduct the 2014 PRS annual market review. The premium rate regulator asked mobilesquared to examine the market for premium rate services (PRS), take an in-depth look at its component parts and assess the prospects for PRS in the near future.

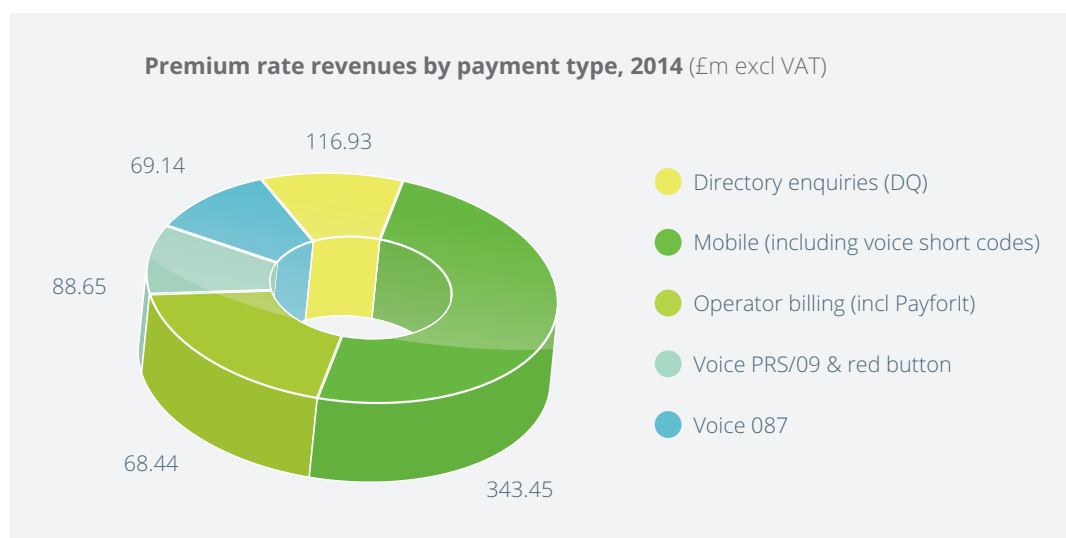
In 2014, the PRS market in the UK was worth £686.6 million (excluding VAT), including charity donations, which have zero-rated revenue shares<sup>1</sup>. Market revenues have fallen year-on-year 3.2%, down from £708.9 million (excluding VAT) in 2013.

With the PRS market in decline, mobile represented the two payment mechanics that experienced growth in 2014, with operator billing (including Payfort) up 86% on 2013 revenues, and mobile (including voice short codes) increasing 5%.

Operator billing (including Payfort) has shown meaningful growth as a nascent platform, yet still only accounted for 10% of total PRS revenues generated in 2014. Mobile, consisting of PSMS, charitable donations and voice short codes, accounted for 50% of PRS revenues in 2014. Add operator billing to the mobile category and it reveals that mobile has become the dominant payment channel for PRS, accounting for 60% of total PRS revenues in 2014, or £411.9 million (excluding VAT).

Voice-based PRS have been hit hardest with the 2013-2014 revenue decline, with voice PRS/09 (including red button) falling 26%, directory enquiries and Voice 087, both dropped 17%. Collectively, voice-based services experienced the greatest decline in revenues between 2013 and 2014, down 20% from £344.6 million to £274.7 million (both excluding VAT).

Fig 1: Premium rate revenues by payment type, 2014 (£m excl VAT)



Source: PRS market sizing for PhonepayPlus

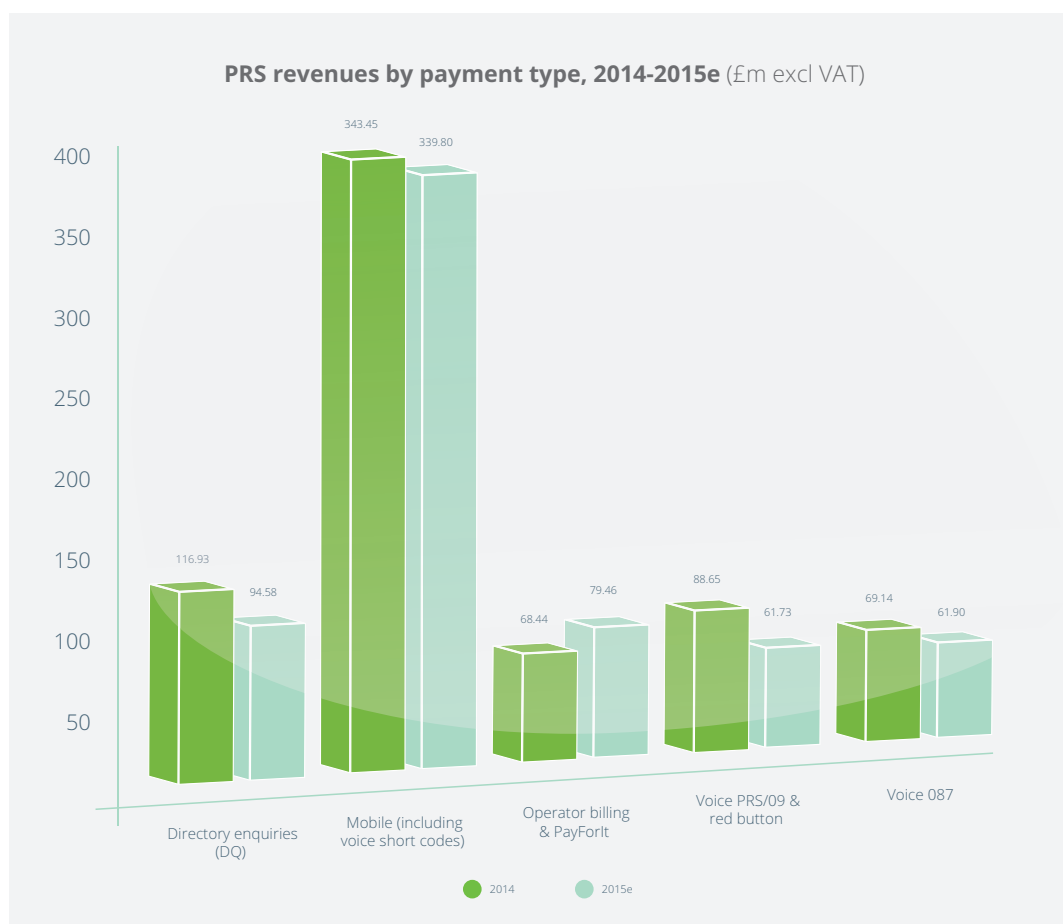
In 2015, the total PRS market is projected to be worth £637.5 million in 2015 (excluding VAT), representing a decline of 7.2% between 2014 and 2015.

<sup>1</sup> See Methodology

Mobile's dominance as a payment type for premium rate services – including PSMS, charitable donations, voice short codes, and operator billing – will increase from 2014 to 2015 and account for 66% of total PRS revenues. In 2015, mobile categorised services are expected to generate revenues of £419.3 million (excluding VAT).

Overall, mobile-based payments (including operator billing) are projected to increase 2% between 2014 and 2015, while voice-based payments are expected to fall 21%. Broken down by payment channel, voice PRS/09 will experience the largest decline in revenues (30%), while directory enquiries is projected to drop 19%.

Fig ii: PRS revenues by payment type, 2014-2015e (£m excl VAT)



Source: PRS market sizing for PhonepayPlus, industry research

If the PRS industry is to stage any kind of recovery in the coming years, it will do so on its triumvirate of growing services of charitable donations, games and gambling, otherwise known as the new “3Gs” of “giving, gaming and gambling”.

Charitable donations represented the standout success story of 2014 for PRS, contributing £115 million to the total market, with the total value of donations doubling over a two-year period. Giving, gambling and gaming (including games or apps charged to bill, and social gaming) combined, accounted for 40% of the total PRS market in the UK in 2014.

Across the service taxonomy, 14 of the 18 services are expected to experience a decline in revenues in 2015. Voice-based information services is projected to experience the biggest



year-on-year decline, 32%, followed by tarot and astrology (22%) and low-cost international or reverse-charge calling (20%).

Only the “3 Gs” of giving, gaming and gambling are expected to experience an increase in revenues in 2015, and they will account for 49% of the PRS market. Revenues for charitable donations and for gambling are predicted to each increase 8%, with gaming (including games or apps charged to bill and social gaming) revenues set to jump 11%.

Using year-on-year 2013-2014 percentage revenue change applied to each category's user base, a performance-based risk assessment has been created. In total four categories are projected to experience revenue growth between 2014-2015, three services can be classified as “no risk”, although music & video content is on the cusp of dropping into “low risk”, which has four services of which virtual gifts is also on the verge of dropping into the greater risk category. Directory enquiries and dating or flirting services have been classified as “medium risk”, with five categories in the “high risk” zone: adult, off-handset purchase (adult), tarot & astrology, low cost international & reverse calling, and voice-based information services.

Based on findings from the consumer survey, the UK was estimated to have had 19.3 million PRS users as of the start of 2014<sup>2</sup>, which accounted for 35% of the total population<sup>3</sup> aged 11 and over.

It is estimated that 087 customer services remained the most popular service among PRS users (with 8.8 million people using the service at least once in 2014), followed by broadcaster interaction (6.6 million people), charity donations (5.8 million people) and games or apps (4.8 million people). The average PRS category at the start of 2015 had 3.1 million users.

One of the Key Performance Indicators within telecommunications is average revenue per user (ARPU). Annualised ARPU for PRS was £35.60 (excl VAT) in 2014. This reveals that the average monthly spend by a PRS user was £2.97 (excl VAT).

The market is haemorrhaging users, with the number of expected PRS users to fall from 19.3 million in 2014 to 16.5 million at the start of 2015. Despite this, annualised ARPU looks set to increase 9%, to £38.64 (est., excl VAT).

By the start of January 2015, there were an estimated 2.8 million people fewer using premium-rate services than January 2014, with an average departure rate of 233,000 per month. Estimates of the number of PRS users exiting the industry per month indicate that 108,000 (46%) of those users will leave as a direct consequence of perceived non-compliant activity, while approximately 125,000 (54%) will leave because of a cost, service relevance and alternative content-related issue.

<sup>2</sup> This figure has been extrapolated from the screening-out process applied at the start of the consumer survey and applied to the total UK population. See Methodology for full details.

<sup>3</sup> Source: 64.1 million. Office for National Statistics, National Records of Scotland, Northern Ireland Statistics and Research Agency, 2013



Consumer perception of PRS pricing is generally inaccurate. However, cost-related issues were the principal reasons for PRS users to reduce their usage of PRS or stop using the services altogether. PRS pricing is not reflective of changing market dynamics, such as the impact of free alternative content on the internet, and changes in consumer expenditure via their mobile device. And this explains why a number of PRS categories have been classified as at risk.

Service providers within the PRS industry claim that compliance levels averaged 80% in 2014<sup>4</sup>, with industry-identified non-compliant activity still accounting for one-fifth. In 2014, the four most complained-about services – adult, competition, digital content and directory enquiries – accounted for almost two-thirds of complaints to the regulator<sup>5</sup>. The PRS sector (service providers and mobile operators) are targeting compliance levels of 85% in 2015.

PRS had a core of 7.9 million satisfied users in 2014 – which could rise to 10 million dependent on how the 2.1 million “don’t know” users swing. The satisfied users cited affordability, likability, an increase in disposable income, and more spare time, as the principal reasons for being satisfied with PRS.

While the 3 Gs represent the greatest service-type opportunity within the PRS industry, operator billing presents a nation-wide opportunity for companies (Level 1s) operating in the sector capable of processing payments. There are 10.8 million PRS users (56%) that would be interested in using their mobile device to pay for “other transactions” based on operator billing.

For operator billing to succeed, a standardised mobile operator approach is imperative, but aligned with this is the need for a united industry promoting the simplicity and consumer demand for operator billing. The industry believes the £500 million revenues generated via operator billing in 2019 is more than achievable.

<sup>4</sup> Source: Industry research

<sup>5</sup> This is not in itself an indicator of non-compliance.



# METHODOLOGY

mobilesquared were commissioned by PhonepayPlus to conduct the 2014 PRS annual market review, and to provide an outlook for 2015. The review aims to:

- accurately size the market for PRS and the sectors within it
- assess how consumers' engage with PRS
- assess year-on-year trends to date in the market, with an appraisal of the 2015 outlook for the various sectors

To do this, mobilesquared adopted a five-step approach to the research process based on quantitative and qualitative research models that fed a market modelling exercise.

## Consumer: Quantitative research

The quantitative research was based on an online survey to a nationally-representative sample in the UK aged between 11 and 65 years old. Parental permission was sought for participants aged 16 and under. Questions in relation to adult entertainment, dating and gambling did not go out to the under 18s. In total, 8,538 panellists started the survey, with 5,538 screened out for claiming to have not used at least one premium rate service over the previous 12 months, leaving 3,000 PRS panellists to complete the survey and share their PRS habits, expenditure, emerging trends, and future requirements.

The consumer survey went live on the afternoon of 19/12/2014 and closed on the evening of 07/01/2015.

Quantitative research demographic breakdown							
11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
180	90	300	450	450	510	390	630

The quantitative survey was conducted by Lightspeed GMI, part of Kantar.

## Consumer: Qualitative research

To sense-check findings from the quantitative research into consumer views, behaviour and their understanding of PRS, qualitative consumer research was conducted on the streets of Reading, Peterborough and Guildford, during March 2015. In total 116 people aged between 15 and 65+ took part in the research.

Qualitative research demographic breakdown						
15-17	18-24	25-34	35-44	45-54	55-64	65+
9	16	24	30	15	9	13

## Industry: Qualitative research

Qualitative industry research was based on in-depth interviews of businesses operating within the PRS space, and regulated by PhonepayPlus. The research also included companies operating outside of the PRS space to provide a more holistic overview of the telecommunication and content sectors, and PRS' role within that.

mobilesquared conducted 122 in-depth interviews to provide a complete overview of every





sector within the PRS market in the UK, covering the past and present. The interviews were based on a survey created with direct input from PhonepayPlus and industry trade body AIME.

As with the consumer survey, every effort was made to maintain the themes and questions included in previous rounds of the industry research survey to ensure continuity as specified by PhonepayPlus, although changes in market trends and market developments were taken into account.

In addition to the industry research, mobilesquared also interviewed app developers and mobile agencies to provide an “outside-in” perspective of how the developer community view the PRS industry and the in-app purchasing opportunity.

The interviews were used as background to provide market commentary throughout this report, and to provide data and input into the 2014 market modelling process and 2015 forecasting.

The research took place between 5th January 2015 and 31st March 2015.

## MARKET MODELLING

The market-modelling exercise took summary data (revenue, excluding VAT) from the network returns submitted to PhonepayPlus and combined this with survey data about stated use of different services by consumers. The subsequent model produced estimates of revenue for the 18 different categories of service as identified in the updated PRS taxonomy (see below). These figures were later sense-checked with members of the industry that had participated in the qualitative research, and adjustments were made to account for over- or under-reported use of services.

Data from the nationally-representative consumer survey when applied to latest UK population data<sup>6</sup> of residents aged 11 and over, was used to extrapolate a total PRS user base for the UK, applicable to the start of January 2014. This resulted in a PRS user base of 19.3 million people.

The total PRS user base was then broken down by service by calculating the weightings for over- and under-stated use that have been applied to the rest of the model. All references to PRS users or usage will be based on the consumer research findings, unless stated otherwise.

The network returns data does not contain estimates of the value of charitable donations by premium rate, so figures for charitable donations were introduced to the model on the basis of a robust figure derived from figures supplied by industry players working in that sector, and data from the consumer survey. This is a departure from the methodology in previous years, in which estimates of charitable donations by premium rate were calculated as a percentage of the rest of the market. Overall, market revenues and forecasts have been sense-checked by members of the PRS industry.

In the last three quarters of 2014, PhonepayPlus received, for the first time, network-returns data showing voice short-code revenue separately from mobile revenue from PSMS. This meant that revenue from voice short codes could be separated out from other mobile revenue.

<sup>6</sup> Source: 63.6 million. Office for National Statistics, National Records of Scotland, Northern Ireland Statistics and Research Agency, 2013



Because the voice short-code revenue for Q1 in 2014 was included as mobile revenue, this was estimated on the basis of its being equivalent to the average of the other quarters, and this figure was added to the voice short-code total for the year and subtracted from the revenue declared for mobile.

### Forecasting

Sector-by-sector forecasting of 2015 revenues has been undertaken for this report. The methodology employed in the forecasting was similar to that used for the 2014 model. Forecast annual revenues for each payment platform were derived by taking the annual totals from 2010-2014 and extrapolating to 2015 using least-squares regression. This data was then modelled within the same method as above, and sense-checking was applied according to industry forecasts for their sectors.



## Updated service taxonomy

To address the changing services in the market, the service taxonomy for the PRS industry has been updated and is based on the following:

2013 categories	2014-2015 categories
Called Directory Enquiries (number starting 118)	Directory enquiries (eg numbers starting 118)
Received paid text alerts, for example news or sports alerts, or texted information services like getting arrival times of the next bus or similar, where you can text in and get info	Voice-based information services (eg weather hotline, text alerts, etc.)
NO EQUIVALENT	Low cost international or reverse charge calling
Babe/porn type images and videos on your mobile	Adult content (eg video clips, chat, images)
Sex chat on the phone	Adult content (eg video clips, chat, images)
Entered a competition or quiz by text (costing more than a regular text)	Competitions or quizzes
POSTAL-BASED COMPETITIONS (09) MISSING FROM PREVIOUS SURVEYS	Competitions or quizzes
Voted on a reality TV show (like X-Factor or I'm A Celebrity, Get Me Out of Here) by calling a phone number. This could either be a number starting with 09, or a 5-digit 'voice shortcode' (e.g. 88990)	TV or radio show voting or interaction (e.g. X Factor voting)
Voted by text or texted in comments to a TV or radio show (costing more than a regular text)	TV or radio show voting or interaction (e.g. X Factor voting)
NO EQUIVALENT	Internet-based information services (books, magazines, newspapers)
Paid for something that's not on your phone by calling a premium phone line - for example pictures or services on the internet. This premium phone line could either be a number starting with 09, or a 5-digit 'voice shortcode' (e.g. 88990)	Off-handset purchases for adult-related content (e.g. DVD unlock)
Sent a text to pay for a non-mobile phone related product or service- for example WiFi for your laptop or for access to something you can see or use on your computer or on the TV	Off-handset purchases for services (e.g. temporary Wifi access)
Flirt, dating or chat services (non-sexual)	Dating or flirt chat service
Betting, lotteries, scratchcards or gambling	Betting or gambling (eg betting, lottery, scratch cards)
Bought a mobile game	Games or apps charged to my bill (not on social networking sites)
	Games on social networks
Used your mobile to buy a 'virtual' (digital) gift or tool - perhaps within a game, virtual world or a social network.	Virtual gifts in the social media space such as Facebook credits or SwapIts
Bought music or video for your mobile - downloaded or streamed	Music or video content
Tarot, Astrology, Psychic or fortune-telling services	Tarot or astrology
Bought a mobile ringtone, ringback tone, wallpaper or a similar digital "decoration" for your phone	Ringtones, ringback tones, wallpapers etc
Given money to charity using text	Charity donations
MISSING FROM 2013 SURVEY - CHARITABLE DONATIONS 09 NUMBERS	
NO EQUIVALENT	Customer service (eg advice, sales or support)
Called an 09 number to place a bid on something you saw advertised on TV	NO EQUIVALENT
Called an information service line, like car mechanic help, help with computers/software or race tipster line or other information, using an 09 number	NO EQUIVALENT

## Section 1

# MARKET OVERVIEW

- Revenues
- Payment type
- Forecasts



# PRS MARKET IN DECLINE

## Key stats

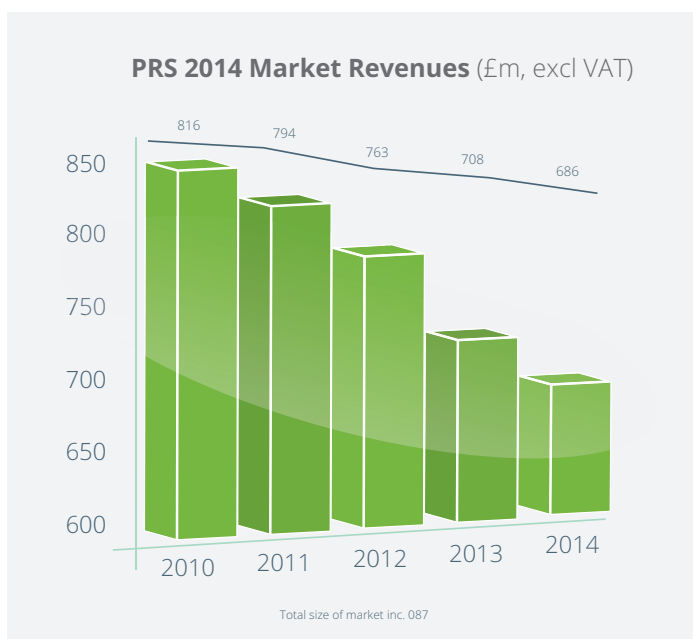
- PRS market worth £686.6 million (excluding VAT) in 2014,
- PRS market revenues fall 3% 2013-2014
- Operator billing grows 86% 2013-2014
- Voice-based services revenues down 20% 2013-2014
- The new 3 Gs: Giving, Gaming and Gambling

In 2014, the premium rate services (PRS) market in the UK was worth £686.6 million (excluding VAT), based on a market-modelling exercise using summary data (revenue, excluding VAT). This figure is derived from network returns submitted to PhonepayPlus, combined with consumer survey data about stated use of different services, and on charity donations, which have zero-rated revenue shares<sup>7</sup>.

This represents a year-on-year drop in market revenues of 3.2%, down from £708.9 million (excluding VAT) in 2013 (see Fig 1). There has been a slowdown in the decline in revenues between 2013 and 2014 compared to the 7.2% fall between 2012 and 2013.

Between 2010 and 2014, the PRS market has experienced successive year-on-year declines in revenues, during which time the market has contracted 16%.

Fig 1: PRS market revenues, 2010-14 (£m excl VAT)



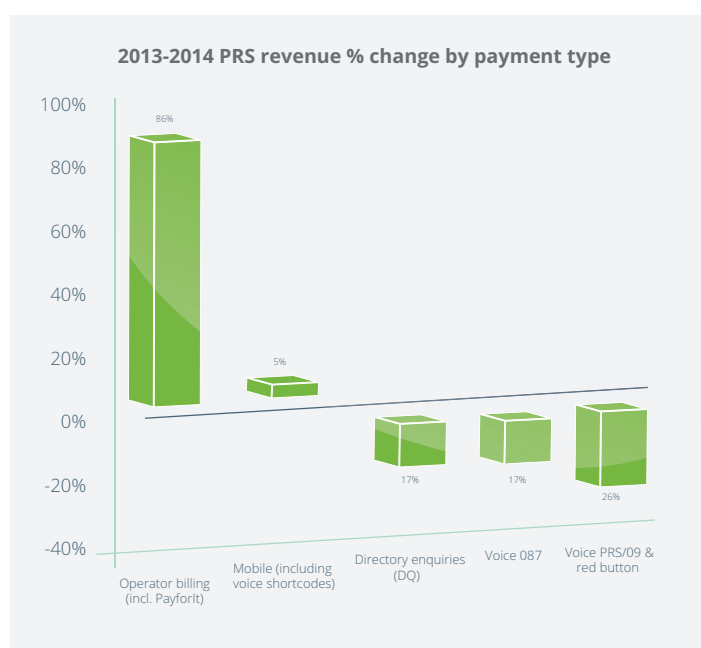
Source: PRS market sizing for PhonepayPlus

<sup>7</sup> See Methodology

### Revenues by payment type

With the PRS market in decline, mobile represented the two payment mechanics that experienced growth in 2014, with operator billing (including Payfort) up 86% on 2013 revenues (see Fig. 2), and mobile (including voice shortcodes) increasing 5%. This is in contrast to all of the other payment channels which experienced an annual decline between 2013 and 2014. Those channels hit hardest were voice PRS/09 and red button, which collectively fell 26%, followed by directory enquiries and Voice 087, each of which dropped 17%.

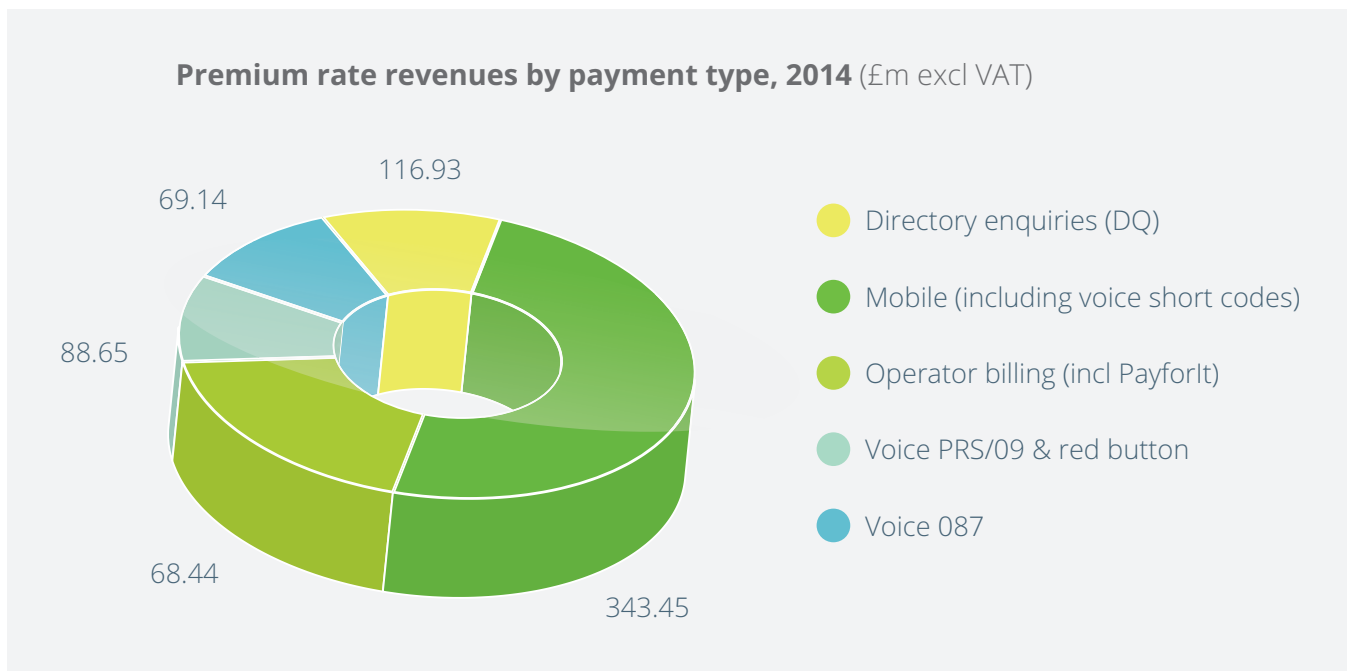
Fig 2: 2013-2014 PRS revenue % change by payment type



Source: PRS market sizing for PhonepayPlus

Operator billing (including Payfort) has shown meaningful growth as a nascent platform, yet still only accounted for 10% of total PRS revenues generated in 2014. Mobile, consisting primarily of PSMS, charitable donations and voice short codes, accounted for 50% of PRS revenues in 2014. Add operator billing to the mobile category and it reveals that mobile has become the dominant payment channel for PRS, accounting for 60% of total PRS revenues in 2014, or £411.9 million (excluding VAT). This represents an increase from 2013, when mobile (including operator billing, PSMS, voice short codes and charitable donations) accounted for 51% of total PRS revenues.

Fig 3: Premium rate revenues by payment channel, 2014 (£m excl VAT)



Source: PRS market sizing for PhonepayPlus

It is the voice-based services of directory enquiries (DQ), voice PRS, 09 and 087, which are experiencing the greatest decline in revenues between 2013 and 2014, down 20% from £344.6 million (excluding VAT) to £274.7 million (excluding VAT).

### Market size by sector – the new “3 Gs”

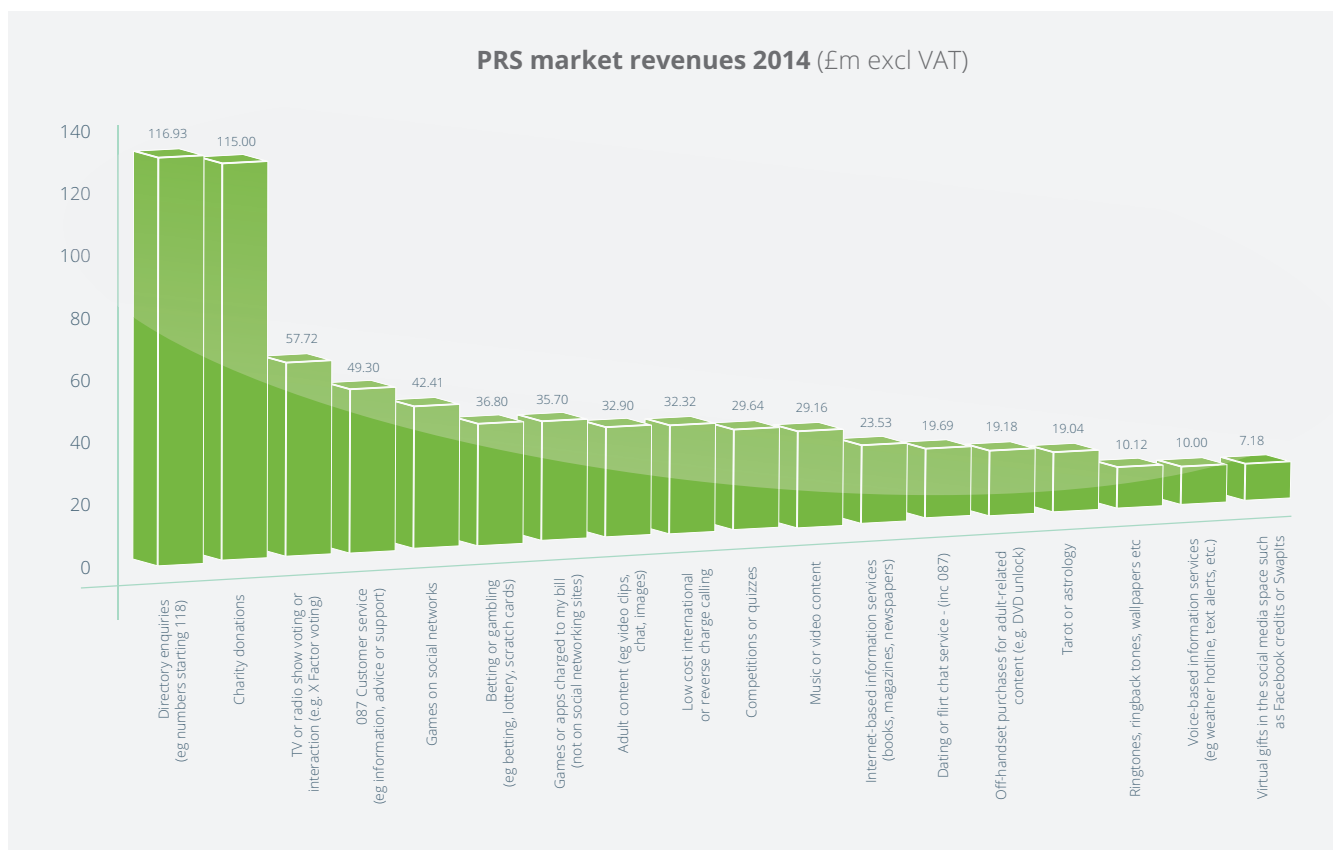
If the PRS industry is to stage any kind of recovery in the coming years, it will likely do so on its triumvirate of growing services of charitable donations, games and gambling. While the advent of 3G in 2003 heralded the emergence of the “3 Gs: girls, gaming and gambling”, this can now be updated with the “3 Gs” of “giving, gaming and gambling”.

Charitable donations represented the standout success story of 2014 for PRS, contributing £115 million to the total market, with the total value of donations doubling over a two-year period. Giving, gambling and gaming (including games or apps charged to bill, and social gaming) combined accounted for 40% of the total PRS market in the UK.

Directory enquiries marginally edged out charitable donations to maintain its position as the leading PRS revenue generator (£116.93 million, excl VAT) in 2014. Interaction with a broadcaster was the third largest PRS revenue generator, ahead of 087 customer service.

Even though voice-based services are under increasing pressure from falling revenues, directory enquiries (DQ) and 087 customer service were two of the top four premium-rate services in 2014.

Fig 4: PRS market revenues, 2014 (£m excl VAT)



Source: PRS market sizing for PhonepayPlus

### PRS market revenue forecasts, 2015

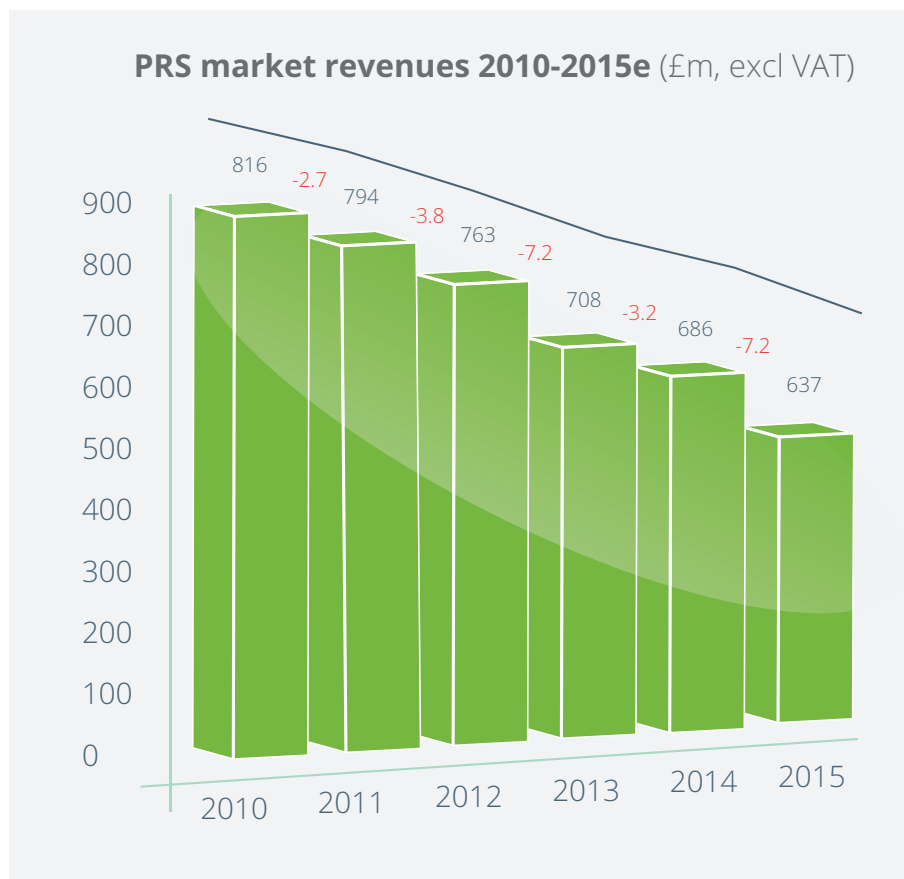
The total PRS market is projected to be worth £637.5 million in 2015 (est., excluding VAT), representing a decline of 7.2% between 2014 and 2015 (see Fig. 5). The 2015 PRS market forecasts have been derived from extensive industry research, applied to the market-modelling exercise conducted for 2014 market revenues using summary data (revenue, excluding VAT) from the network returns submitted to PhonepayPlus by network operators<sup>8</sup>.

The market estimation for 2015 also reveals that the PRS market will have contracted by 22% since 2010.

<sup>8</sup> See Methodology



Fig 5: PRS market revenues 2010-2015e

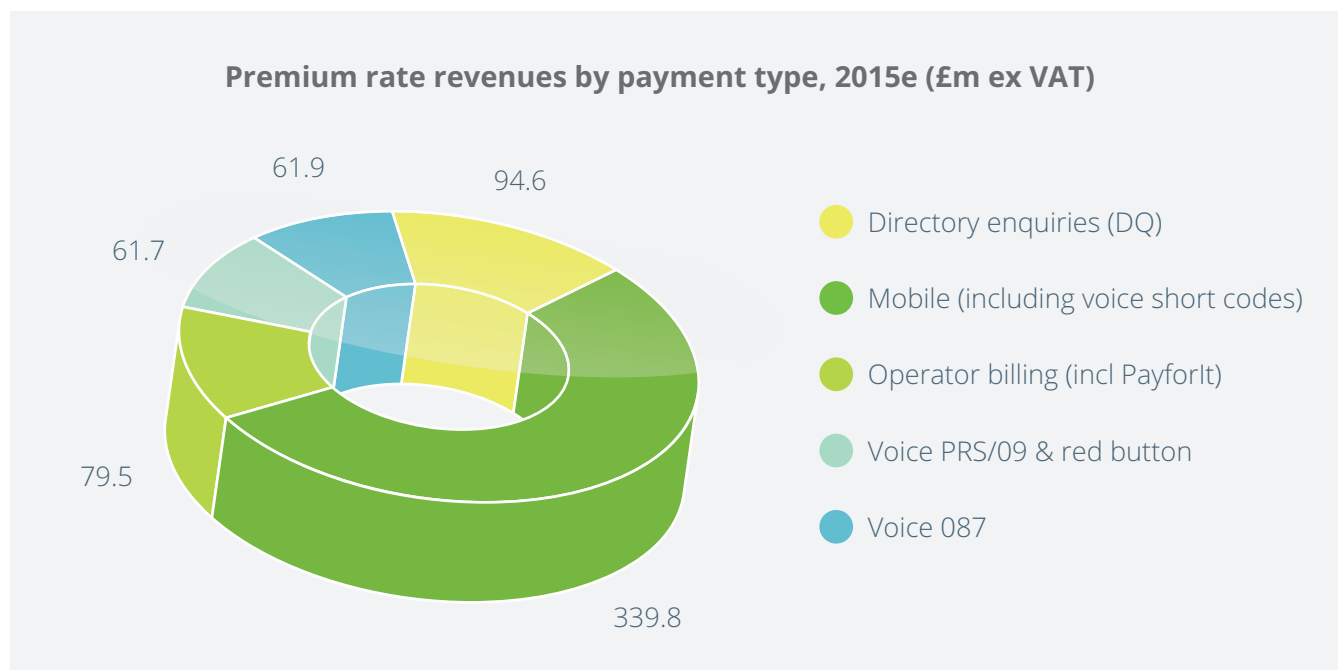


Source: PRS market sizing for PhonepayPlus, industry research

### Revenues by payment type, 2015

Mobile's dominance as a payment type for premium rate services – including PSMS, charitable donations, voice short codes, and operator billing – is expected to increase from 2014 to 2015 and account for 66% of total PRS revenues (see Fig. 6). In 2015, mobile categorised services will generate revenues of £419.3 million (est., excluding VAT).

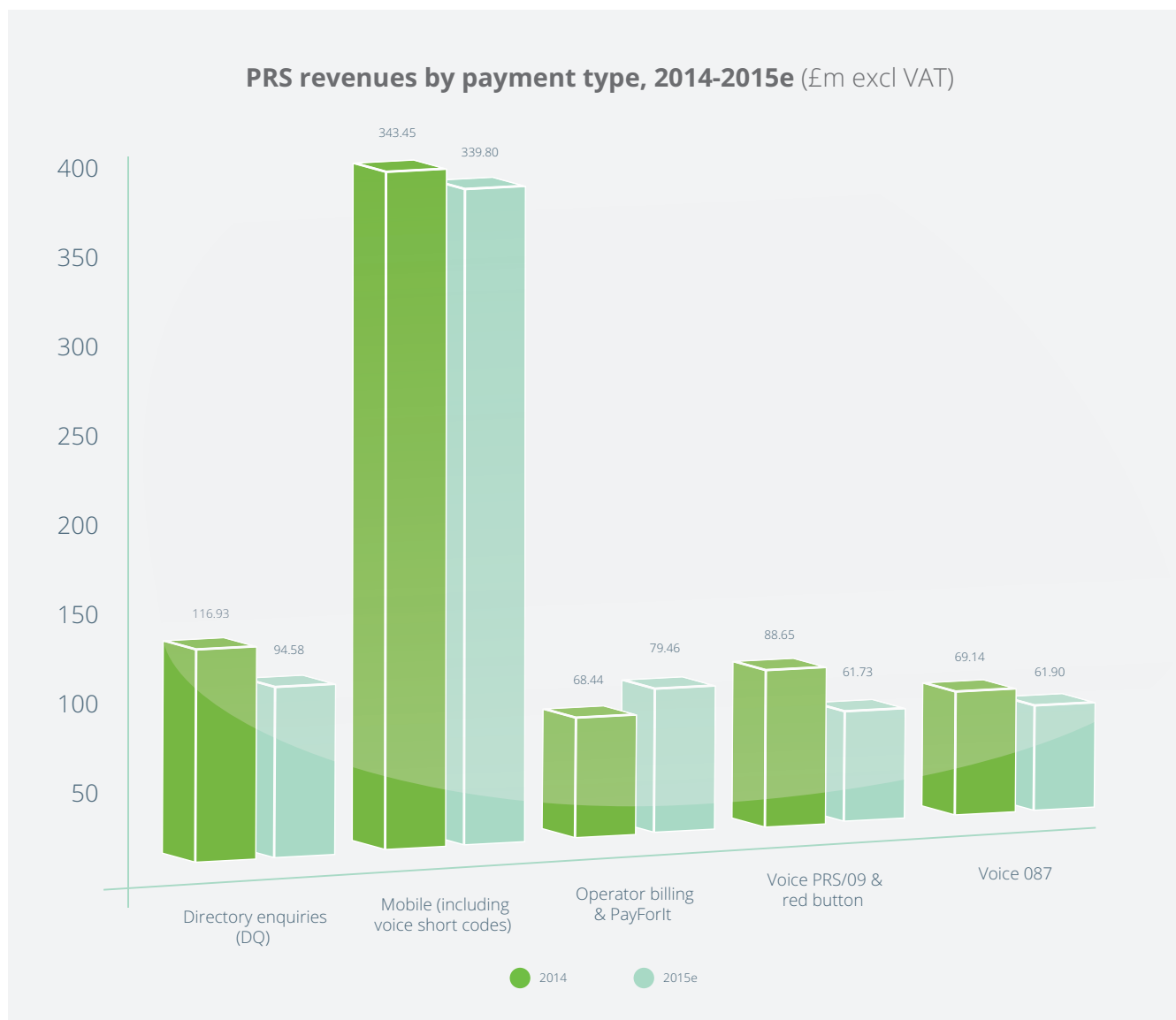
Fig 6: PRS channels by payment type, 2014-2015e (£m excl VAT)



Source: PRS market sizing for PhonepayPlus, industry research

Operator billing (including Payfortl) is the only payment type projected to experience growth between 2014 and 2015, however, the increase is projected to have slowed to 16% – considerably down on the 86% growth enjoyed between 2013 and 2014. This has been in part caused by Level 1 companies awaiting the release and contents of the updated Payments Services Directive (PSDII) in July 2015 to define their mobile payments strategy, coupled with a perceived lack of standardised operator billing requirements.

Fig 7: PRS channels by payment type, 2014-2015e (£m excl VAT)

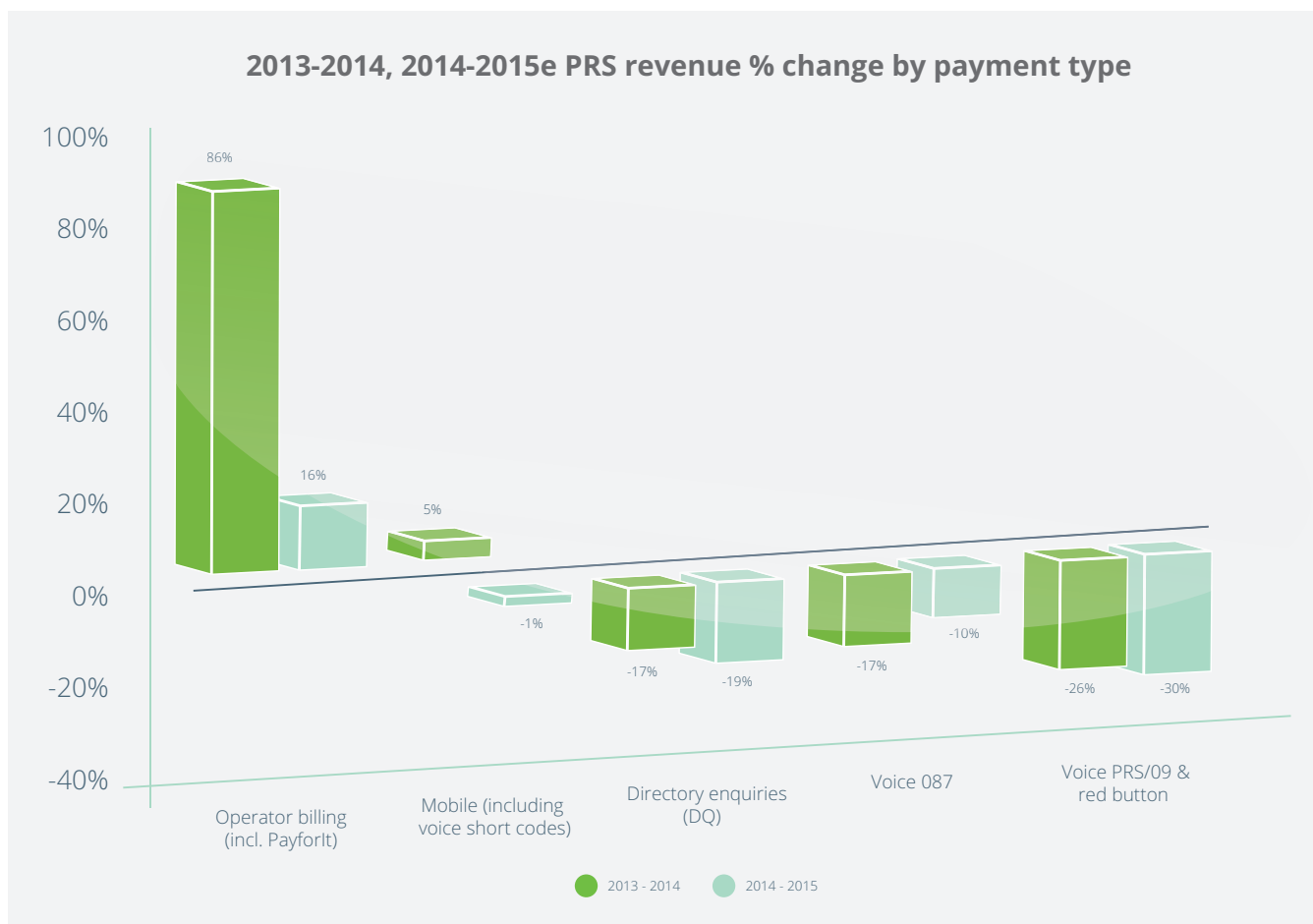


Source: PRS market sizing for PhonepayPlus, industry research

Overall, mobile-based payments (including operator billing) are expected to increase 2% between 2014 and 2015, while voice-based payments will fall 21%. Broken down by payment channel, voice PRS/09 will experience the largest decline in revenues (30%), while directory enquiries is projected to drop 19%.

The impact of changes to Non-Geographical Call Services (NGCS) in July 2015 on the voice PRS/09 segment of the market is expected to be minimal. While NGCS will increase the price ceiling for a 09 call from £1.53 per minute to £3.60 per minute, companies and PRS-based services are not expected to introduce dramatic cost-per-minute price hikes for fear of a consumer backlash.

Fig 8: 2013-2014, 2014-2015e PRS revenue % change by payment type



Source: PRS market sizing for PhonepayPlus, industry research

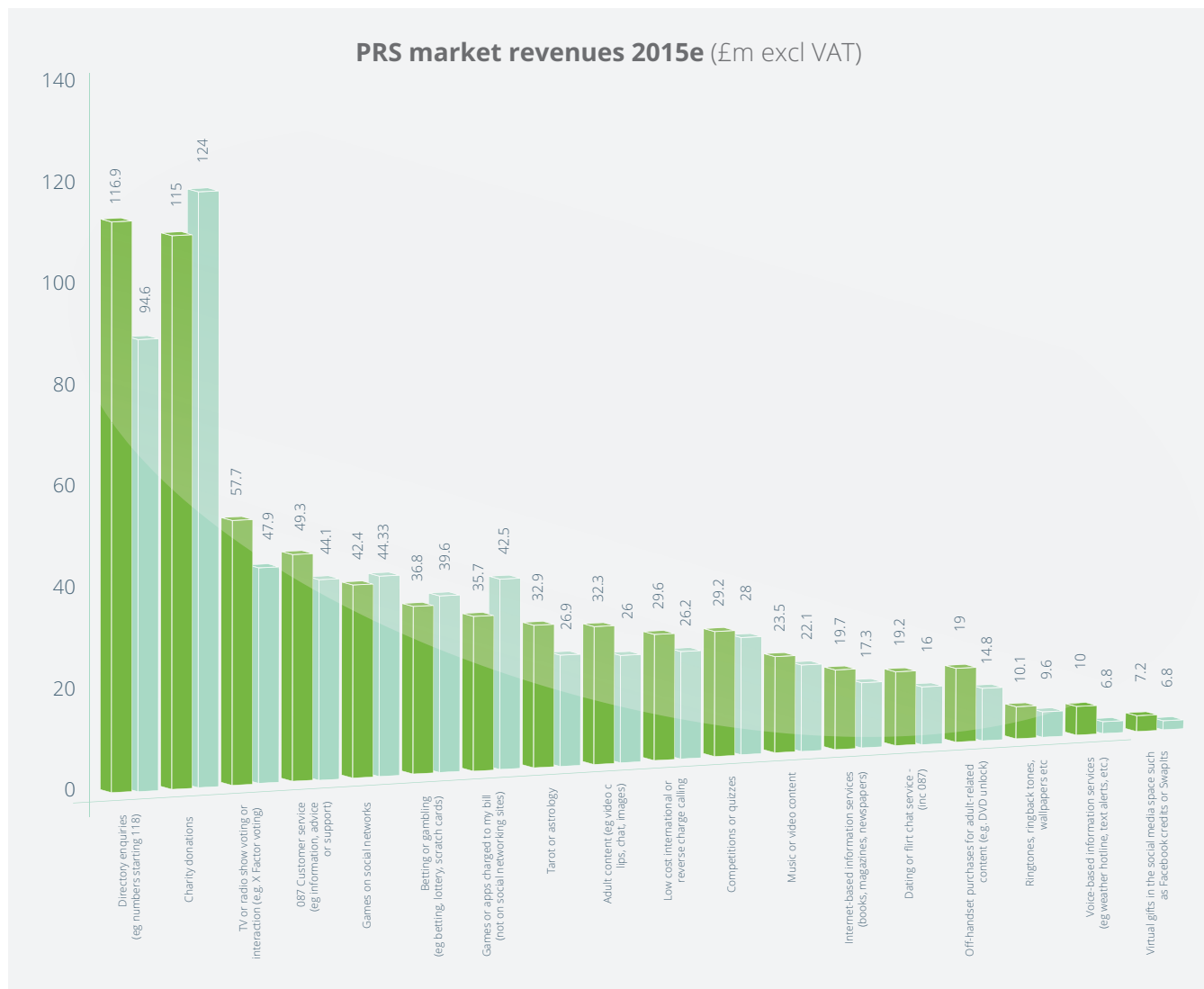
As Fig. 8 demonstrates, the revenue decline for directory enquiries and voice PRS/09 (and red button) will increase between 2014 and 2015 as consumers continue to use alternatives, including free internet-based services.

### PRS market by service type, 2015

Within the updated service taxonomy, 14 of the 18 services will likely experience a decline in revenues in 2015 (see Fig. 9). Voice-based information services is expected to experience the biggest year-on-year decline, 32%, followed by tarot and astrology (22%) and low-cost international or reverse-charge calling (20%).

Only the “3 Gs” of giving, gaming and gambling will likely experience an increase in revenues in 2015, accounting for 49% of the PRS market. Revenues for charitable donations and for gambling are set to each increase 8%, with gaming (including games or apps charged to bill and social gaming) revenues set to jump 11%.

Fig 9: PRS market revenues 2015e (£m excl VAT)



Source: PRS market sizing for PhonepayPlus, industry research



## Identifying PRS users

# THE SURVEY BACKGROUND

The consumer survey identified PRS users and usage trends in the UK. The survey was conducted between December 2014 and January 2015. The survey went out to a nationally representative online sample of 8,538 participants aged 11 and above.

Consumers were asked to recall which premium rate services they had used since the start of 2014. Only those respondents that selected at least one premium rate service progressed to the main survey. In total 5,538 were screened out to provide a representative sample of 3,000 users of premium-rate services<sup>9</sup>.

In previous years, the recall period used during the consumer research process had been 6 months, but this was extended to 12 months to incorporate major PRS consumer activity over a given 12-month period, ranging from charity fundraising events such as *Sport Relief* in March 2014, to TV voting for programmes in the latter half of 2014, for example *The X Factor*, *I'm A Celebrity Get Me Out Of Here*, and *Strictly Come Dancing*.

### PRS users 2014

Based on findings from the survey, the UK was estimated to have had 19.3 million PRS users as of the start of 2014<sup>10</sup>, which accounted for 35% of the total population<sup>11</sup> aged 11 and over.

By extrapolating data from survey questions regarding service taxonomy<sup>12</sup>, it is estimated that 087 customer services remained the most popular service among PRS users (with 8.8 million people using the service at least once in 2014), followed by broadcaster interaction (6.6 million people), charity donations (5.8 million people) and games or apps (4.8 million people). Virtual gifts (1.1 million) and voice-based information services (549,000) have the lowest number of users.

Based on the updated service taxonomy for 2014, the 18 PRS categories had an average of 3.1 million users as of January 2014 (see Fig. 10).

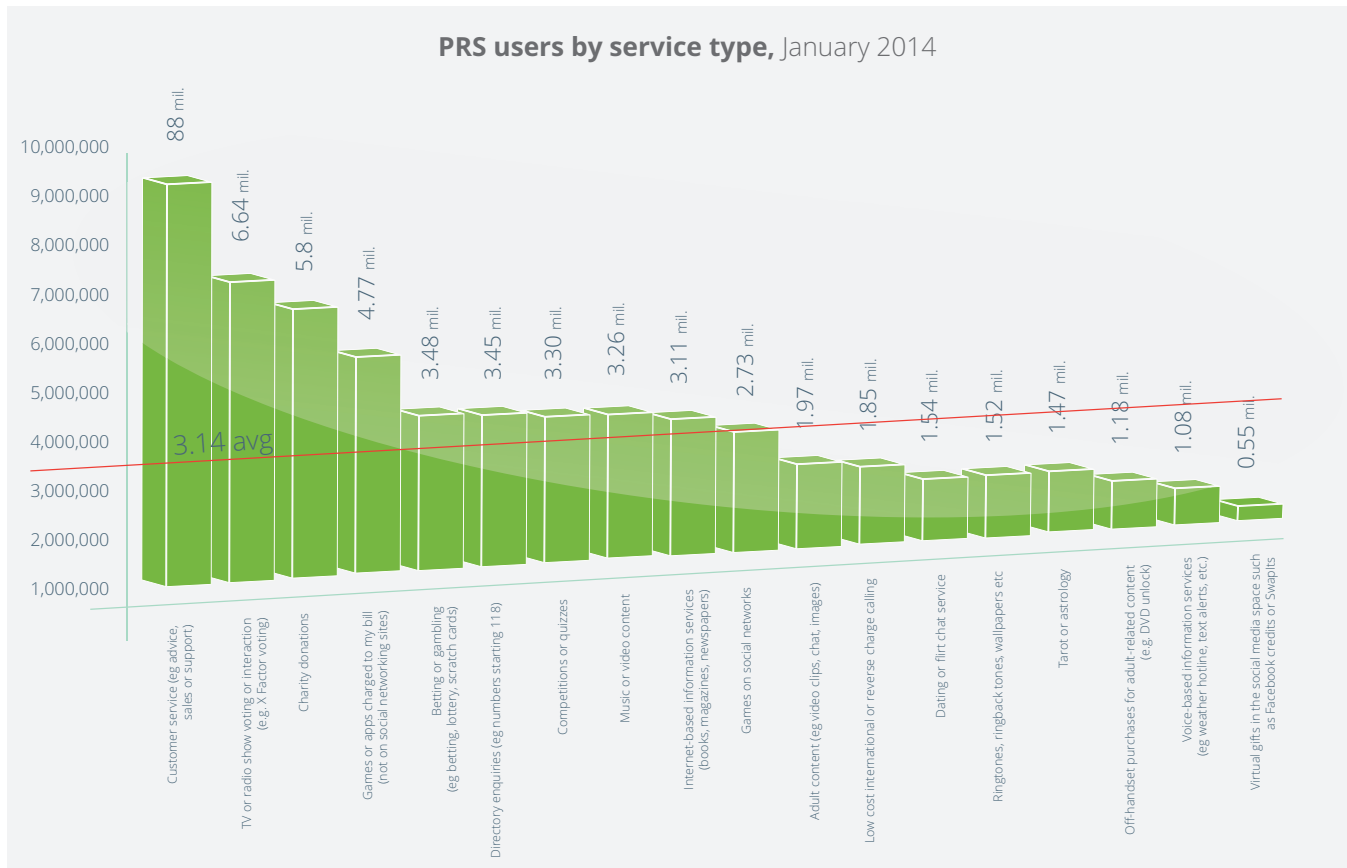
<sup>9</sup> Parental permission was requested for participants aged 11-15. Note that questions in relation to adult entertainment, dating and gambling did not go out to under-18's. The raw data provided by the consumer research was then sense-checked by 116 face-to-face consumer interviews.

<sup>10</sup> This figure has been extrapolated from the screening-out process applied at the start of the consumer survey and applied to the total UK population. See Methodology for full details.

<sup>11</sup> Source: 64.1 million. Office for National Statistics, National Records of Scotland, Northern Ireland Statistics and Research Agency, 2013

<sup>12</sup> Users by PRS service have been calculated using the weightings for over/understated use, which have been applied to the rest of the PhonepayPlus market model.

Fig 10: PRS users by service type, January 2014



Source: PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q25. In the last 12 months, have you used any of the following phone call-based or mobile-accessed goods or services (premium rate services) which cost money? Multiple choice. Base n= 3,000.

### ARPU (prices exclude VAT)

One of the Key Performance Indicators (KPIs) within telecommunications is average revenue per user (ARPU). For 2014, annualised average revenue per user (ARPU) for PRS was £35.60 (including charitable donations) and £29.62 (excluding charitable donations). This reveals that the average monthly spend by a PRS user was £2.97 including charitable donations and £2.47 excluding charitable donations in 2014.

The market decline should be compounded by the haemorrhaging of PRS users, with the number expected to fall from 19.3 million in 2014 to 16.5 million in 2015. However, annualised ARPU looks set to increase 9%, to £38.64. This indicates that it is the low-spending premium rate users who are no longer using services.

Fig 11: PRS, monthly ARPU, 2014 (excl VAT)

	Annualised ARPU	Monthly ARPU
Directory enquiries (eg numbers starting 118)	£33.90	£2.83
Charity donations	£19.78	£1.65
Low cost international or reverse charge calling (inc 087)	£17.43	£1.45
Adult content (eg video clips, chat, images)	£16.68	£1.39
Off-handset purchases for adult-related content (e.g. DVD unlock)	£16.31	£1.36
Games on social networks	£15.54	£1.29
Virtual gifts in the social media space such as Facebook credits or Swaplts	£13.07	£1.09
Tarot or astrology	£12.93	£1.08
Dating or flirt chat service (inc 087)	£12.75	£1.06
Betting or gambling (eg betting, lottery, scratch cards)	£10.57	£0.88
Voice-based information services (eg weather hotline, text alerts, etc.)	£9.23	£0.77
Competitions or quizzes	£8.98	£0.75
Music or video content	£8.94	£0.74
TV or radio show voting or interaction (e.g. X Factor voting)	£8.70	£0.72
Internet-based information services (books, magazines, newspapers)	£7.56	£0.63
Games or apps charged to my bill (not on social networking sites)	£7.48	£0.62
Ringtones, ringback tones, wallpapers etc	£6.65	£0.55
087 Customer service (eg advice, sales or support)	£5.60	£0.47

Source: PRS market sizing for PhonepayPlus, industry research



## Section 2

# PRS USER DEVELOPMENTS

- Change in user behaviour
- Impact on PRS

# THE 2014 PREMIUM RATE EXODUS

Due to revisions in the research methodology used in this report compared to previous years, it is not possible to provide a year-on-year comparison of PRS users in the UK prior to 2014. Based on the survey findings, it is estimated that there were 19.3 million PRS users at the start of 2014. However, due to the structure of the survey, it has been calculated that 2.8 million people stopped using premium rate services during 2014. By January 2015 it is estimated that there were 16.5 million PRS users (see Fig. 12).

Fig 12: Total PRS users, Jan 2014-Jan 2015

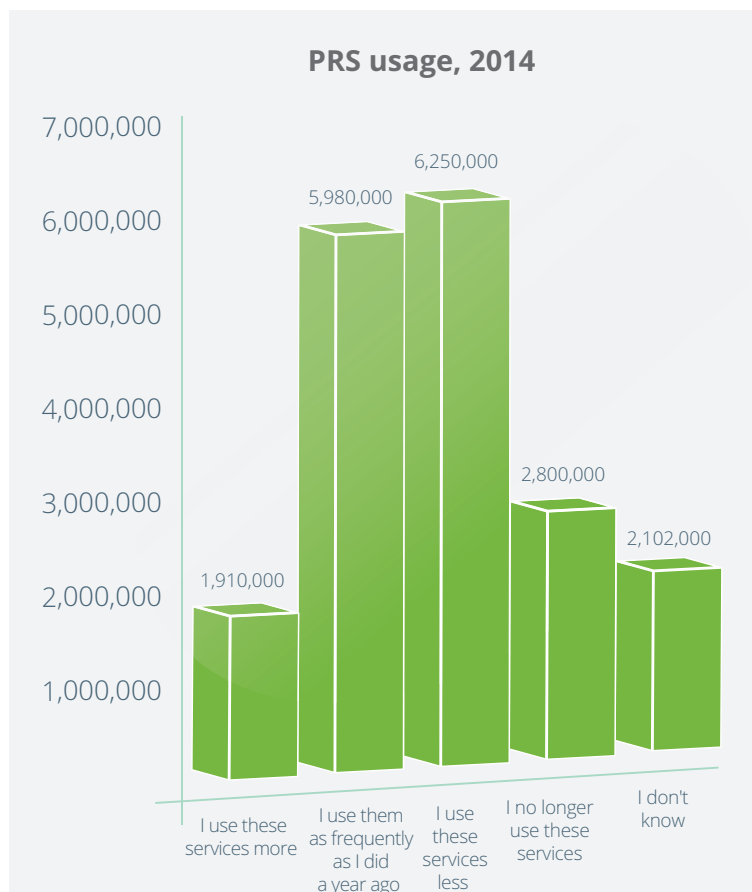


Source: *PRS market sizing for PhonepayPlus, industry research, PhonepayPlus quantitative consumer survey, December 2014-January 2015*. Q25. In the last 12 months, have you used any of the following phone call-based or mobile-accessed goods or services (premium rate services) which cost money? *Multiple choice. Base n=3,000.*

This means the PRS sector was haemorrhaging customers at an average rate of 233,000 per month during 2014.

Furthermore, an additional 6.3 million people claimed that they were using premium rate services less in 2014. As the projected rise in ARPU between 2014 and 2015 potentially highlights, the users that are no longer using PRS are those spending below the average. Therefore, the 6.3 million people that claim to be using PRS less are the ones most likely to stop using the service altogether during 2015, and should be classified as “high risk” (see Fig. 13).

Fig 13: PRS usage, 2014



Source: PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q33. Has your usage of these paid services changed over the last 12 months? Base n=3,000.

Almost half of PRS users claimed that they reduced their consumption of PRS, or stopped using PRS altogether, because of a cost-related reason, such as “less disposable income”, “can’t afford any more”, and “I wasn’t aware how much I was spending”.

One-quarter of total PRS users claimed they reduced or stopped consuming PRS because of a service-related issue, citing factors such as they no longer “see the value”, they are “no longer interested”, or “the services are not as good as they were”.

Cost, service relevance, and alternative content sources are the three main factors that present a mounting challenge to the longevity of premium-rate services. If not addressed, given the high number of high risk users, this could result in an even greater mass exodus of users in 2015.

Fig 14: Why have you reduced or stopped using PRS services over the past 12 months?

I can get content free elsewhere	2,836,000
I have less disposable income	2,185,000
I can't afford them anymore	2,641,000
I wasn't aware how much I was spending on these services	939,000
I'm using other paid services - like non-PRS mobile apps	149,000
I'm not as interested in the services anymore	1,869,000
The services are not as good as they were	576,000
I pay for these services using other means e.g. credit card	288,000
I no longer see value in these services	2,064,000
I had problems with a service, so I don't want to use them anymore	232,000
I don't trust these services anymore	1,060,000
I don't know	549,000

Source: PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q36: What reason/reasons can you attribute for using these services less or stopping using them altogether? Multiple choice. Base n=1,446.

According to the survey, 5% of PRS users stopped using the service because they claimed they had “stopped trusting” the services. The survey also revealed that 1% of PRS users have had “problems with a service, so don’t want to use [PRS] any more”. Due to the reasons these users have stopped using PRS – most likely because of perceived non-compliant activity – they are unlikely to return to the sector.

But for those users that have stopped using the services because of cost, service relevance, and alternative content sources – and not perceived non-compliance-related reasons – they could be attracted back to using premium-rate services through innovation or revisions to pricing.

Estimates of the number of PRS users exiting the industry every month, based on the survey findings reveals around 108,000 (46%) of those users will leave as a direct consequence of perceived non-compliant activity, whereas approximately 125,000 (54%) will leave because of a cost, service relevance and alternative content-related issue.

Fig 15: Reasons for leaving PRS in 2014



Source: PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q36: What reason/reasons can you attribute for using these services less or stopping using them altogether? Multiple choice. Base n=1,446.



But the data also suggests that the majority of discontented PRS users did not complain about their experience to PhonepayPlus, which received 20,719 complaints<sup>13</sup> in 2014; the survey data indicates that there were significantly higher levels of perceived non-compliant activity within the PRS sector during 2014 than was reported by end users.

According to service providers within the PRS industry, compliance levels averaged 80% in 2014<sup>14</sup> and non-compliant activity accounted for one-fifth.

PhonepayPlus will consider further investigation of a complaint lodged by a consumer based on evidence of any potential breaches in the Code. Industry looks to categorise the severity of the breach by applying a yellow and red card scheme that has been written into the cross-network process. More recently, individual mobile operators are looking to introduce additional colours to the scheme to provide four levels of Code breach as opposed to the existing two.

Industry research reveals that the PRS sector (service providers and mobile operators) are targeting compliance levels to reach 85% in 2015.

In 2014, the four most complained-about services - adult, competition, digital content and directory enquiries - accounted for almost two-thirds of complaints for the year<sup>15</sup>. Based on complaints originated from a promotional channel, adult display networks received the most complaints, followed by affiliate networks, in-app banners, and TV.

Affiliate networks do not pose quite the threat to the PRS industry that they did in 2013. The PRS industry collectively believes that significant progress has been made on affiliate marketing since 2013, attributing the work to co-operation between the PRS industry and PhonepayPlus.

### A core of PRS users

Despite the survey revealing a decline in PRS users during 2014, it also highlighted frequency of usage increased for 10% of users (1.9 million), with these users citing affordability, likability, an increase in disposable income, and more spare time as the principal reasons.

Almost one-third of PRS users (6 million) said their usage levels did not change between 2013 and 2014 because of pricing stability and their continued enjoyment of the content or service. Combined, the survey reveals a core of 7.9 million satisfied users.

That leaves 2.1 million PRS users that claimed “don’t know” with regard to their PRS usage status.

<sup>13</sup> This figure does not include the 11,081 enquiries made per year to PhonepayPlus

<sup>14</sup> Source: Industry research

<sup>15</sup> Note, a consumer complaint is not necessarily an indicator of non-compliance.

## Section 3

# PRS SERVICE OVERVIEW

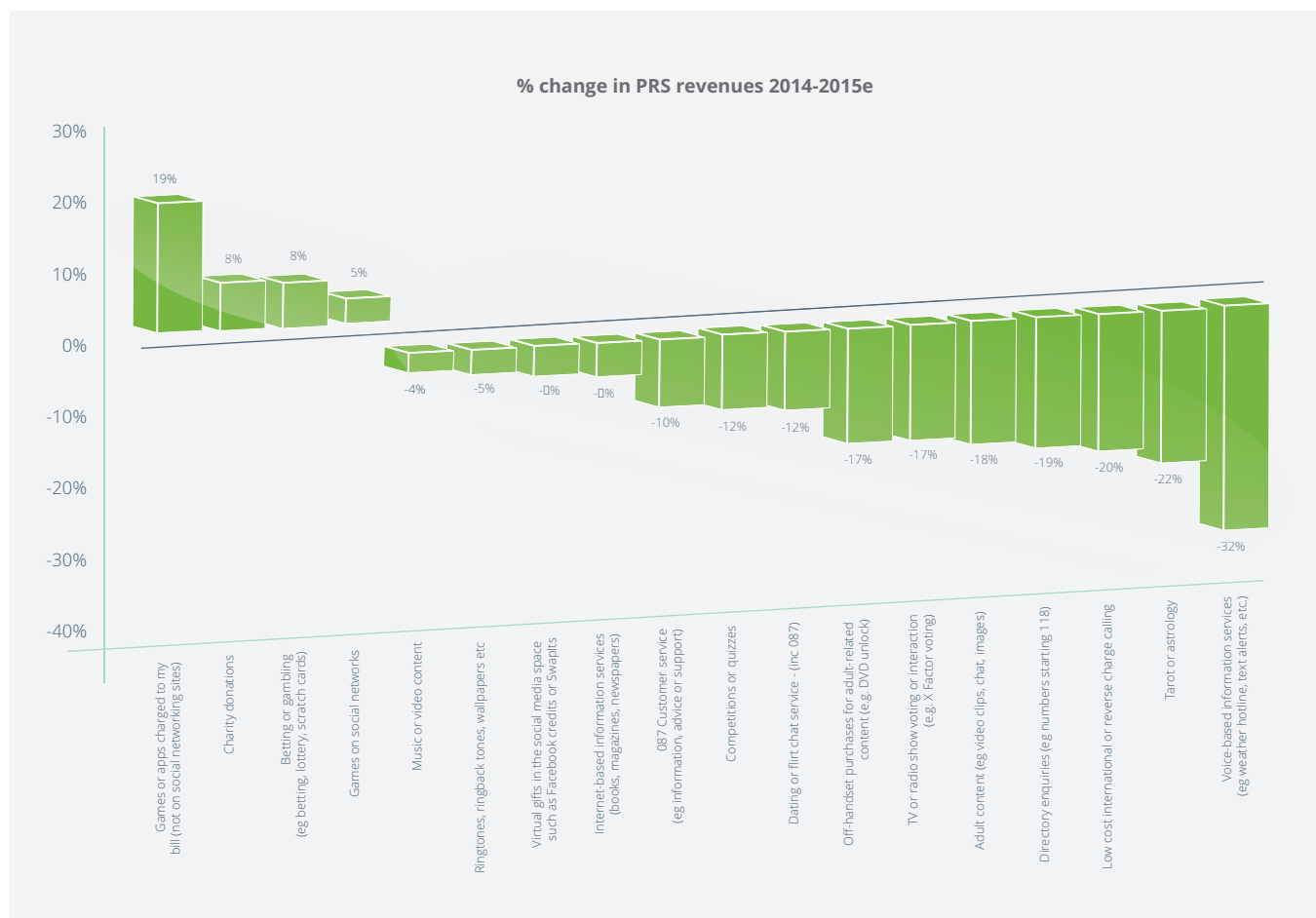
- Revenues
- Payment type
- Forecasts

# PRS RISK ASSESSMENT

As previously highlighted in Section 1, only four service categories are projected to experience growth between 2014 and 2015, these encompass the 3 Gs of giving, gaming (including apps) and gambling. These categories are projected to grow by between 5% and 19% between 2014 and 2015 (see Fig. 16).

During the same timeframe, 14 of the 18 PRS categories are projected to experience a decline in revenues of between 4% and 32%.

Fig 16: % change in PRS revenues 2014-2015e



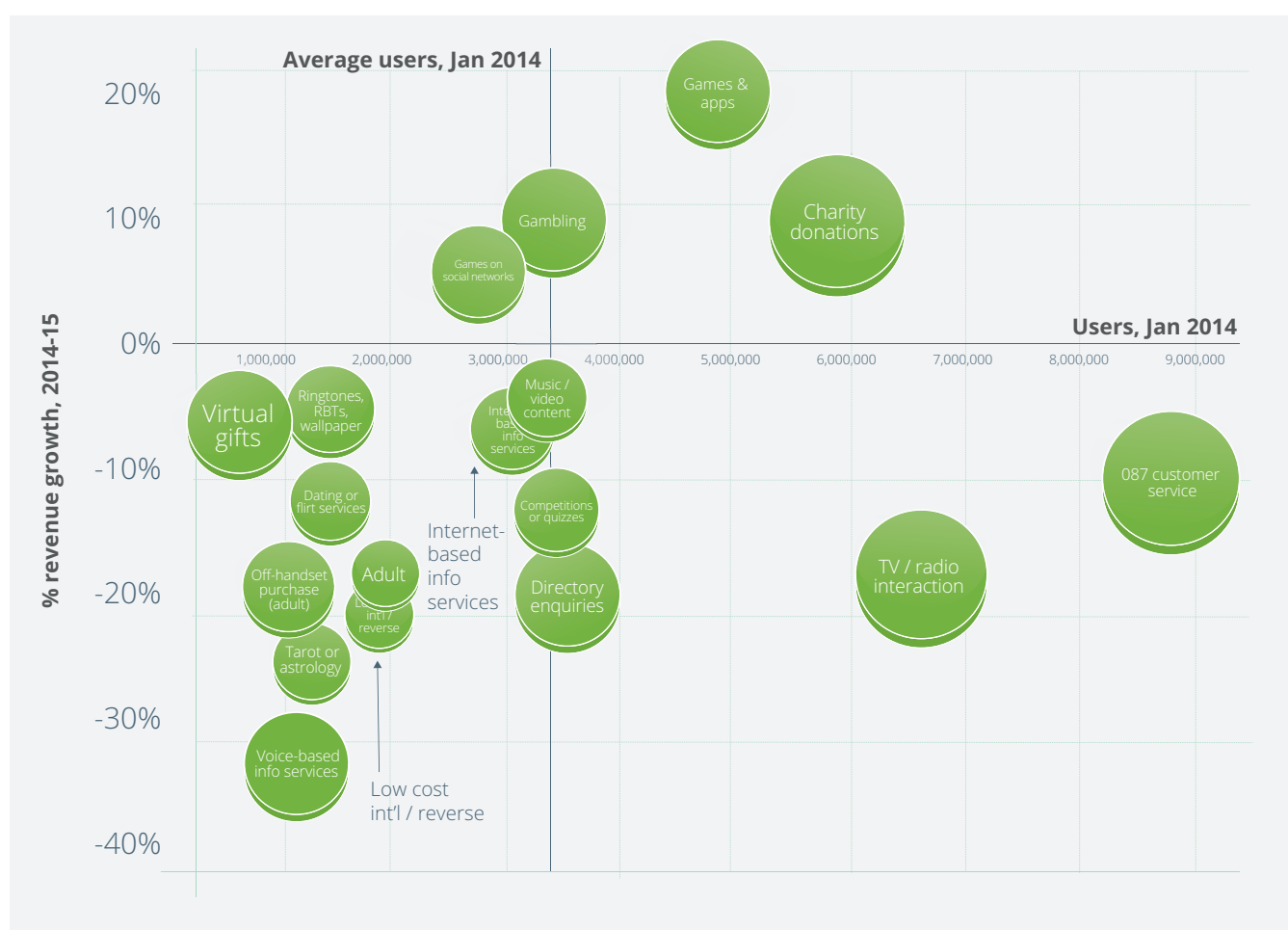
Source: PRS market sizing for PhonepayPlus, industry research

To create a risk assessment of each premium rate service category, the percentage year-on-year revenue change for 2014 to 2015 has been applied to the total users for each category as featured in Fig 17.

Using “average users, Jan 2014” to create a quadrant, it reveals that three of the four growth sectors - gambling, games (and apps) and charity donations – have an above average user base, with games on social networks yet to achieve a substantial user base.

Of those services with a negative revenue growth for 2014-2015e, 087 customer service and TV & radio interaction have strong user bases. Two services have negative revenue growth but have an above average user base (competitions or quizzes, and directory enquiries), while two categories (internet-based info services, music & video content) have an average user base. Leaving eight categories with a negative revenue growth and a below average user base.

Fig 17: Risk assessment; % revenue change vs user base



Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q25. In the last 12 months, have you used any of the following phone call-based or mobile-accessed goods or services (premium rate services) which cost money? Multiple choice. Base n= 3,000.

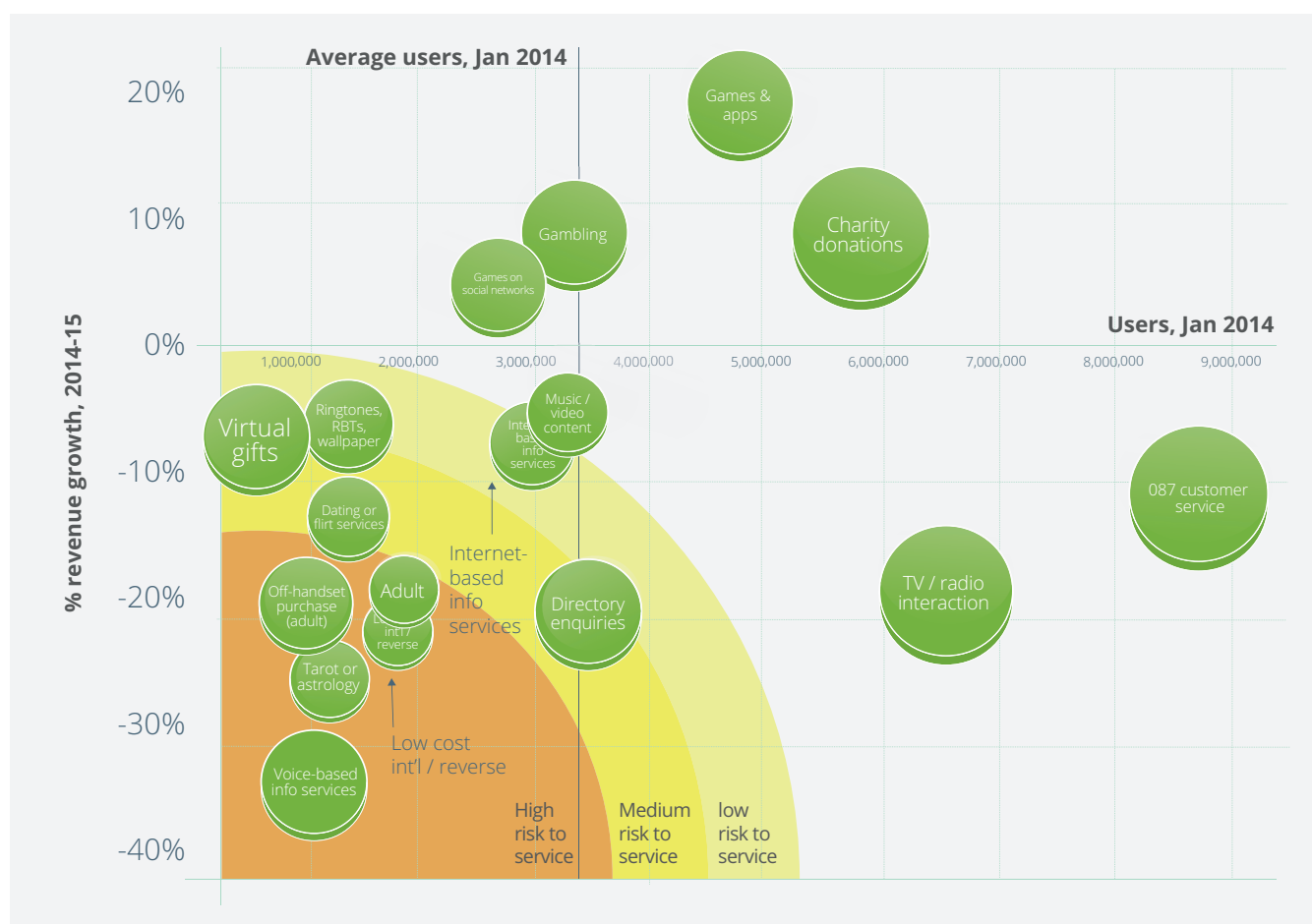


Fig 18: PRS risk assessment

The PRS risk assessment is based on the following categorisation:

Low risk to service	Annual decline in revenues less than 10%, below-average to average user base
Medium risk to service	Annual decline in revenues up to 15% with lower-than-average user base
	Annual decline in revenues greater than 15% with higher-than-average user base
High risk to service	Annual decline in revenues greater than 15%, lower-than-average user base

Fig 19: Risk assessment; % revenue change vs user base



Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q25. In the last 12 months, have you used any of the following phone call-based or mobile-accessed goods or services (premium rate services) which cost money? Multiple choice. Base n= 3,000.

In total four categories are projected to experience revenue growth between 2014-2015e, three services can be classified as “no risk”, although music & video content is on the cusp of dropping into “low risk”, which has four services of which virtual gifts is also on the verge of dropping into the greater risk category.

Fig. 20: Risk assessment overview

Growth	Games/apps	Games on social networks	Gambling	Charitable donations
No risk to service	087 customer service	Music and video content	TV & radio interaction	
Low risk to service	Internet-based info services	Competitions or quizzes	Virtual gifts	Ringtones RBTs, wallpaper
Medium risk to service	Directory enquiries		Dating or flirting services	
High risk to service	Adult	Off-handset purchase (adult)	Tarot & astrology	Low cost int'l & info services Voice-based info services

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q25. In the last 12 months, have you used any of the following phone call-based or mobile-accessed goods or services (premium rate services) which cost money? Multiple choice. Base n= 3,000.

### Please note

The following section provides top-line data points associated with each of the PRS categories, as well as key findings extracted through extensive industry research.

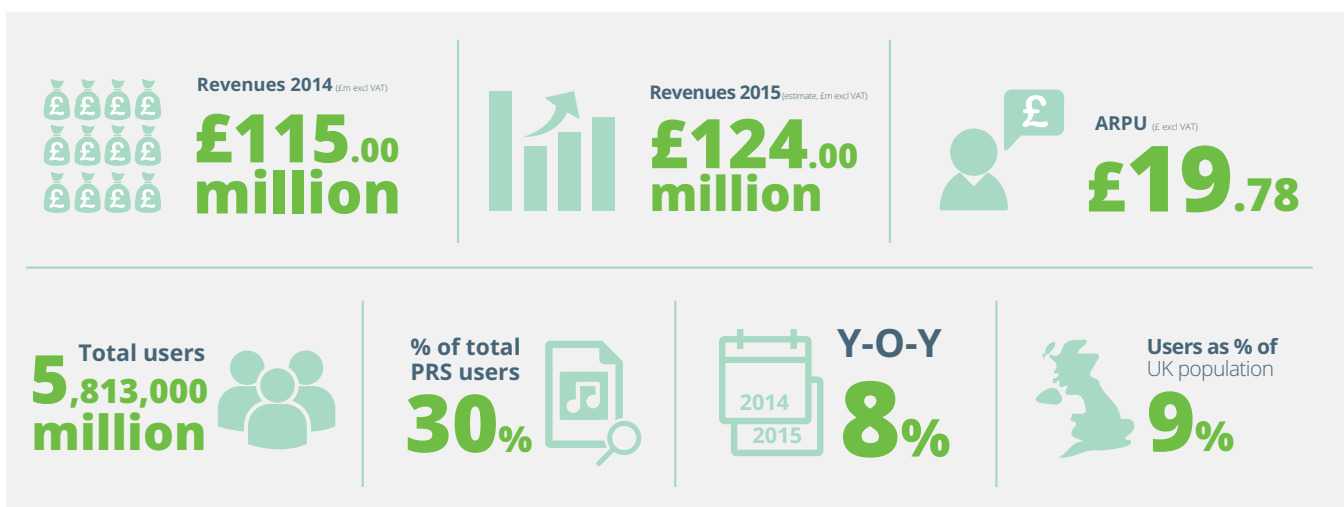
Where applicable, year-on-year changes in revenues (2013-2014) have been included, however, due to the updating of the service taxonomy, coupled with this year's methodology, this is not possible for every PRS category. Where the methodology or service area remains unaffected, year-on-year revenues have been included.

## Section 3:

# GROWTH

### Charitable donations

Fig. 21: Charitable donations



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	3,840,000	124,000	97,000	234,000	524,000	538,000	710,000	587,000	1,026,000
Once or twice a month	1,117,000	55,000	41,000	124,000	283,000	165,000	165,000	96,000	186,126
Two to five times a month	587,000	28,000	21,000	179,000	124,000	110,000	55,000	28,000	42,000
More than once a week	186,000	21,000	-	28,000	69,000	48,000	7,000	13,000	-
Daily	83,000	21,000	7,000	14,000	21,000	20,000	-	-	-

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used charitable donations over the last 12 months? Base n= 843

Charitable donations have become a consumer “favourite”. It commands the greatest user base (5.8 million) out of all the PRS categories enjoying revenue growth. Furthermore, it has the opportunity of becoming something of a “hero service” for the PRS industry as it looks to re-establish a trusted connection between the consumer and the PRS industry via PSMS, despite 100% of the payment going to charity and no VAT payment to the government.

Research from the charity sector<sup>16</sup> reveals that the average person in the UK has been giving 0.4% of their income per year over the past decade. The ubiquity of SMS and the simplicity of the service have encouraged millions of users to use mobile as an alternative payment mechanic to 087 and online-based payment channels. And part of the appeal from the charity sector itself, was the creation of VAT free 07 text short codes which has enabled charities of all sizes to capitalise on the opportunity.

Mobile has proved an effective user-acquisition tool for charities. In 2014, the average annual donation by the 5.8 million people using PSMS was £19.78 (see Fig. 21). Understandably,

<sup>16</sup> Source: Industry research



the charity sector is encouraged by consumer take-up of PRS as a payment channel and is looking to capitalise on this opportunity.

The introduction of monthly donations via PRS in 2014 has supplemented the appeal PSMS and encouraged repeat donations. This is estimated to have amassed over 100,000 users by the end of 2014 and is projected to be growing by about 5,000 per month<sup>17</sup>. With marketing and social media, this figure is expected to accelerate in 2015.

Regular text giving can be attributed to the collaboration between industry and PhonepayPlus, including the introduction of “SKIP” messages to replace “STOP”, permitting consumers to miss a payment for a month should they choose. The SKIP development has been welcomed by industry and has lowered attrition rates. In conjunction with PSMS, the big charities are also exploring Payfort<sup>18</sup>. The mobile operators, on the other hand, are looking to cover costs by applying standard network charges of between £0.03 and £0.10 per message.

PRS has also become the glue linking donations with the monetisation of social media. Facebook users in particular embraced the ‘no make-up’ and ‘ice bucket challenge’ concepts, which contributed almost £20 million in donations in 2014<sup>19</sup>. What’s more, these initiatives were birthed not from charities’ marketing teams but from a desire among Facebook users to do good. The charity sector expects these viral campaigns to become a regular fixture and believes social media will be able to support three or four viral campaigns per year.

Based on the consumer survey, two-thirds of users donate via PSMS on a quarterly basis, one-fifth of users give fortnightly, and the remaining 14% donating on a weekly or daily basis. With almost half of PRS users donating at least once a month, charities clearly have good reason to encourage users to sign up to a monthly donation via PRS.

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<sup>17</sup> Source: Industry research

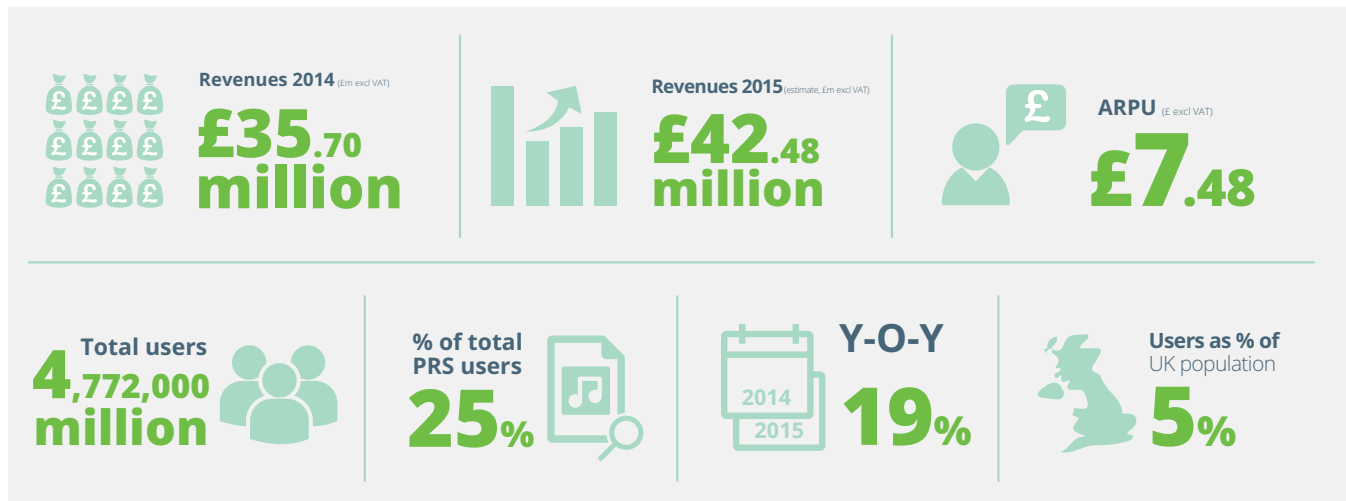
<sup>18</sup> Source: Industry research

<sup>19</sup> Source: Industry research

## Growth

### Games or apps charged to my bill (not on social networking sites)

Fig. 22: Games or apps charged to my bill



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	1,902,000	203,000	114,000	379,000	352,000	396,000	229,000	115,000	114,000
Once or twice a month	1,154,000	176,000	44,000	229,000	317,000	185,000	114,000	36,000	53,000
Two to five times a month	863,000	106,000	18,000	167,000	290,000	211,000	35,000	10,000	26,000
More than once a week	572,000	88,000	44,000	114,000	141,000	141,000	18,000	9,000	17,000
Daily	281,000	44,000	9,000	62,000	62,000	62,000	35,000	7,000	-

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used games or apps charged to my bill over the last 12 months? Base n= 542

Games (or apps) charged to a phone bill represents the greatest year-on-year growth (19%) for 2014-2015 of all PRS services. This is not surprising given that gaming is the one area of mobile content that has experienced sustained growth since its advent. The UK mobile games market was worth £674.4 million in 2014<sup>20</sup>. Transactions using PRS accounted for 5.3% of total spend in 2014.

Although gaming is one of the few sectors within PRS projected to experience growth between 2014 and 2015, growth will be hindered by the dominance of iOS and iTunes as a payment platform, as well as the multiple payment options associated with Android. Nevertheless, Google has entered the operator-billing space by teaming up with O2, 3 and EE, and is enjoying considerable growth. Vodafone stopped supporting direct operator billing on Google Play in 2014, and is yet to reverse its decision.

Similarly, the view from games developers is that if there is a need for an alternative in-app payment mechanism they would support it, but they are not yet seeing the demand from consumers for operator billing.

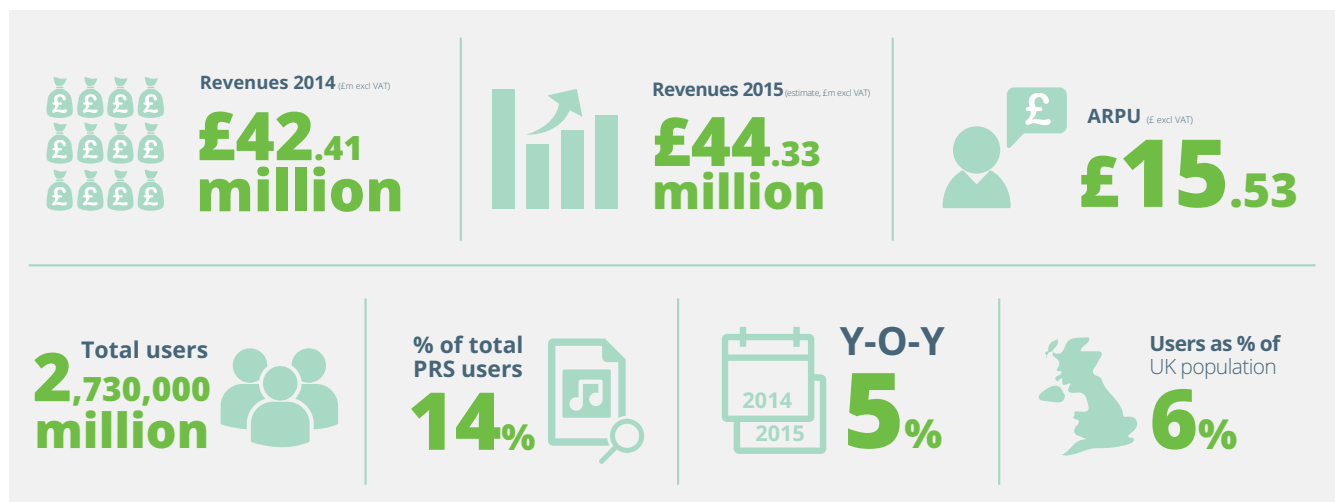
The gaming opportunity is not restricted to smartphones. Featurephone users still represent a gaming market for mobile operators in the UK. And those operators that maintain their portal generate revenue from the sale of games, the majority of which are repurposed for featurephones.

<sup>20</sup> Source: Newzoo Global Games Market Report Premium

## Growth

### Games on social networks

Fig. 23: Games on social networks



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	728,000	79,000	13,000	101,000	136,000	127,000	106,000	84,000	82,000
Once or twice a month	593,000	106,000	40,000	97,000	167,000	114,000	53,000	13,000	3,000
Two to five times a month	470,000	92,000	22,000	119,000	75,000	83,000	44,000	13,000	22,000
More than once a week	556,000	84,000	26,000	88,000	127,000	115,000	70,000	18,000	28,000
Daily	383,000	40,000	14,000	62,000	66,000	70,000	62,000	48,000	21,000

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used games on social networks over the last 12 months? Base n= 621

Games on social networks is a recent inclusion to the premium-rate service taxonomy, and this is also reflected by the fact its user base is yet to surpass the PRS average of 3.1 million. Nevertheless, as one of the 3 Gs, the service is projected to experience revenue growth of 5% between 2014 and 2015.

The rise of games on social networks as a standalone category within PRS is borne out of the phenomenal gaming opportunity in the UK. There are 37.91 million gamers in the UK generating a total gaming market worth £2.46 billion in 2014, of which £180 million is generated from online social gaming<sup>21</sup>. Transactions via PRS accounted for 23.6% of total online-social-gaming spend in 2014<sup>22</sup>.

Clearly, where gamers are presented with multiple payment options, operator billing is becoming an acceptable payment mechanic. This is being driven by the purchase of credits to play, or the freemium model of users buying the game after having played a demo version.

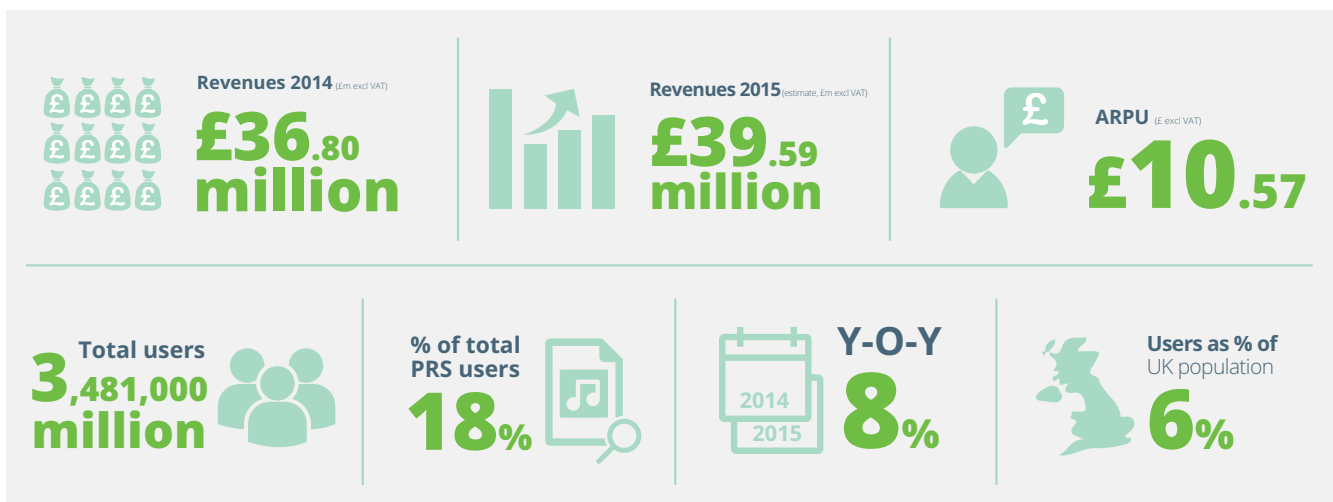
<sup>21</sup> Source: Newzoo Global Games Market Report Premium

<sup>22</sup> Source: Newzoo Global Games Market Report Premium

## Growth

### Gambling or betting (e.g. betting, lottery, scratch cards)

Fig. 24: Gambling or betting



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	1,237,000	-	-	179,000	217,000	249,000	198,000	140,000	254,000
Once or twice a month	587,000	-	-	57,000	236,000	172,000	97,000	19,000	6,000
Two to five times a month	803,000	-	-	128,000	242,000	172,000	115,000	77,000	69,000
More than once a week	631,000	-	-	121,000	153,000	134,000	96,000	77,000	50,000
Daily	223,000	-	-	45,000	57,000	64,000	38,000	6,000	13,000

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used gambling or betting over the last 12 months? Base n= 546

The last of the 3 Gs, gambling (or betting) is the fourth PRS category expected to experience revenue growth (of 8%) between 2014 and 2015. With a just-above-average user base, revenue growth is expected to be limited by competition from other payment mechanisms, namely debit or credit cards.

Payments via PRS have been deployed as part of a broader user-acquisition programme, with service providers looking to rapidly migrate the user onto a credit or debit card, primarily to overcome the £30-a-day spending cap imposed on PRS by the mobile operators. The service providers in this sector view this cap as restrictive.

Service providers also view operator billing as cost prohibitive<sup>23</sup> because mobile operators command a revenue share of 9.9%, compared to a transaction fee of 6-8% on e-wallets and 1-3% on credit cards.

While service providers believe PRS presents a viable alternative payment mechanism for the consumer and expect gambling (or betting) spend to increase via PRS, its revenue generation capabilities will be curtailed until the cap is lifted and the transaction fee is reduced.

A number of service providers offer operator billing as a payment option within their service offering, and it is generating up to 25% of their monthly revenues<sup>24</sup>.

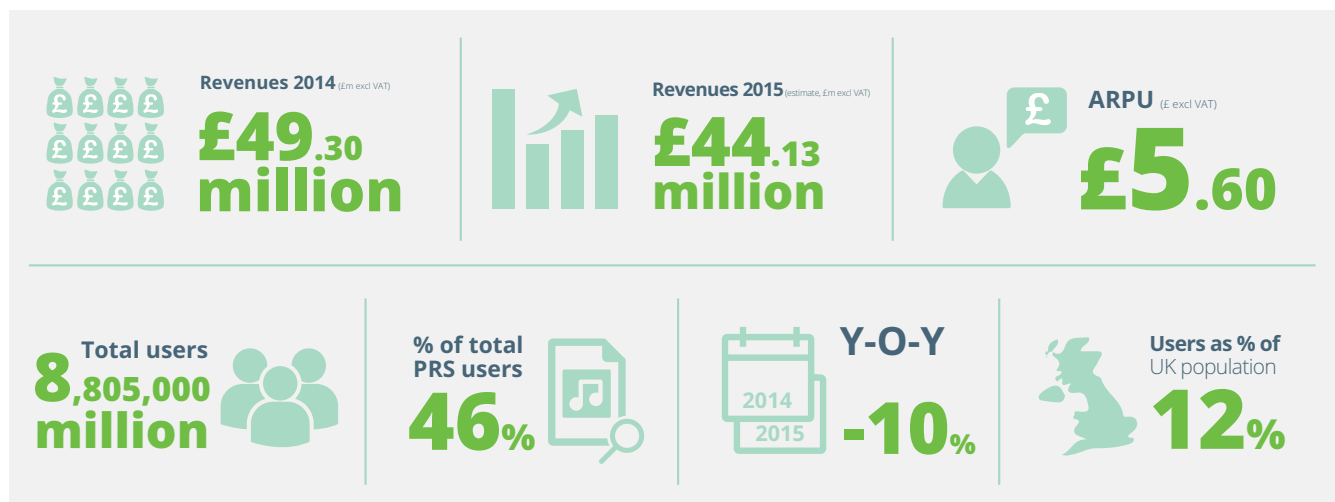
<sup>23</sup> Industry research

<sup>24</sup> Industry research

### No risk to service

#### 087 Customer service (e.g. information, advice or support)

Fig. 25: 087 Customer service



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	5,104,000	81,000	59,000	272,000	514,000	705,000	1,035,000	925,000	1,513,000
Once or twice a month	2,071,000	29,000	37,000	250,000	345,000	294,000	433,000	257,000	426,000
Two to five times a month	962,000	44,000	37,000	147,000	242,000	184,000	125,000	81,000	102,000
More than once a week	521,000	44,000	22,000	110,000	176,000	74,000	51,000	7,000	37,000
Daily	147,000	15,000	7,000	22,000	37,000	44,000	15,000	7,000	-

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used customer service over the last 12 months? Base n= 1,199

Although 087 customer service is projected to experience a negative revenue growth of 10% between 2014 and 2015, the service has been classified as “no risk” because of its extensive user base that will ensure a demand for the service in the foreseeable future, regardless of their frequency of usage.

More than 8.8 million PRS users call 087 customer service numbers, but the majority of users are infrequent, with just one-quarter likely to use the service several times a month. ARPU is the lowest across all premium rate services.

Regardless, service providers acknowledge that 087 is competing with social media, IM and email as more users seek alternative, and free, internet-based communication channels. Consequently, the overriding industry view is that revenues will continue to fall, however, research into how consumers contact businesses reveals that a person-to-person voice call remains their preferred channel<sup>25</sup>.

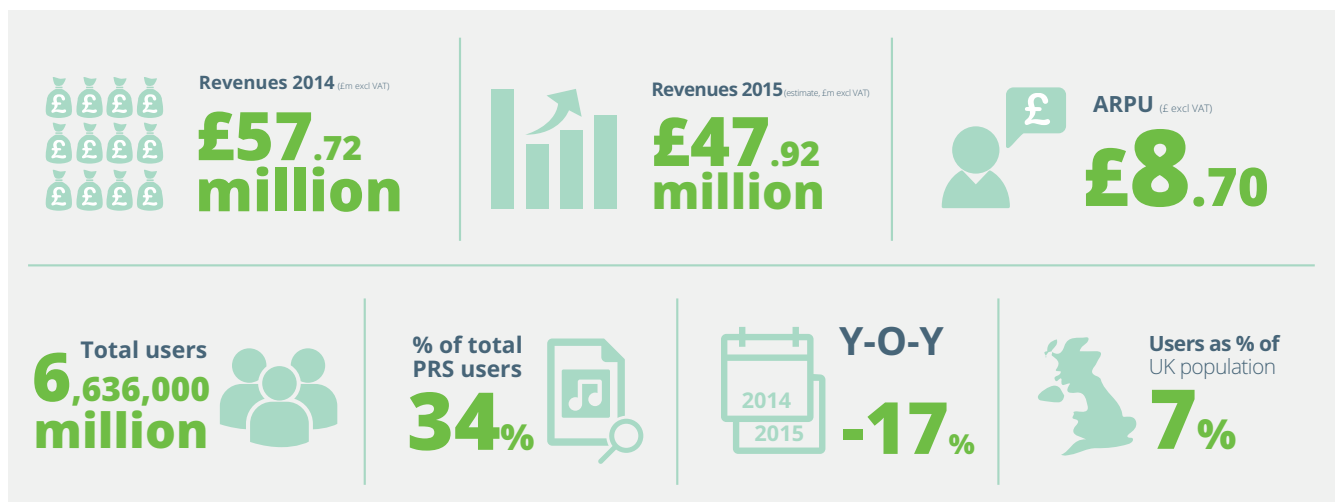
<sup>25</sup> Mobilesquared research, Astellia 2015



## No risk to service

### TV or radio show voting or interaction (e.g. X Factor voting)

Fig. 26: TV or radio show voting or interaction



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	3,410,000	185,000	62,000	370,000	452,000	462,000	483,000	473,000	923,000
Once or twice a month	1,500,000	216,000	41,000	134,000	329,000	257,000	236,000	92,000	195,000
Two to five times a month	1,192,000	154,000	51,000	205,000	339,000	186,000	123,000	41,000	93,000
More than once a week	411,000	82,000	10,000	62,000	51,000	154,000	31,000	11,000	10,000
Daily	123,000	10,000		31,000	51,000	31,000			

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used TV or radio show voting or interaction over the last 12 months? Base n= 646

Because of its vast user base and the assuredness of ongoing audience demand for interaction with TV and radio, TV or radio show voting or interaction has also been classified as “no risk”. Despite a projected negative revenue growth of 17% between 2014 and 2015, the sector is predicted to be worth £47.92 million in 2015. Across PRS, TV or radio show voting or interaction is second only to 087 customer service when it comes to size of user base.

Based on industry estimates that TV or radio voting or interaction was worth approximately £75 million (excl. VAT) in 2013, the figure for 2014 of £57.7 million (excl. VAT) represents a fall in revenues of 23%.

Broadcasters have concentrated on the simplicity of voice short codes and PSMS to drive interaction with mainstream TV shows - though 09 has not been phased out altogether - but levels of interaction are generally waning, though also unpredictable.

The allure of encouraging viewers to engage using a second or third screen is presenting something of a dilemma to broadcasters. Do they continue to use existing PRS channels for voting, develop sponsored apps with free votes, develop apps with limited free votes and the option of additional paid-for votes, develop apps with paid-for votes only, or simply use social media, such as Twitter?



A sponsored app provides the broadcaster with guaranteed revenue based on an advertising model it is familiar with. Yet by developing apps, broadcasters are leading their audience into an IP environment that presents the option of either free votes or paid-for. If a user is presented with the opportunity to vote free of charge, will they then revert to paid-for voting when the free votes have been used, or should the broadcaster decide to revert back to paid-for votes at a later date? When TV programme *The X Factor* amassed over 40 million votes in 2014, it was the most of any series, and that was because the accompanying app provided free votes.

The view within the industry is that a broadcaster looking to monetise a programme should use PRS, namely PSMS or voice short codes. However, a number of service providers questioned the longevity of voice short codes, because of not only the impact that NGCS will have, but also the impact of the use of social media as an interactive medium.

Clearly, a shift in business model to offer an advertising-funded sponsored app or switch channels to social media, present the greatest threat to the longevity of PRS as a revenue-generating mechanism for broadcasters. But while mobile provides broadcasters with the opportunity to interact with 6.6 million viewers via PRS, it will continue to feature as a revenue driver.

Interestingly, broadcaster viewer polls reveal an ongoing consumer mistrust of broadcasters in relation to TV voting, especially when a broadcaster needs to refund the cost of a vote to a viewer<sup>26</sup>. This suggests the mistrust is of the broadcaster and not of the payment mechanism (PRS). Therefore, the relationship between consumer and broadcaster remains fractious and will only be overcome when there is no cost associated with the interaction.

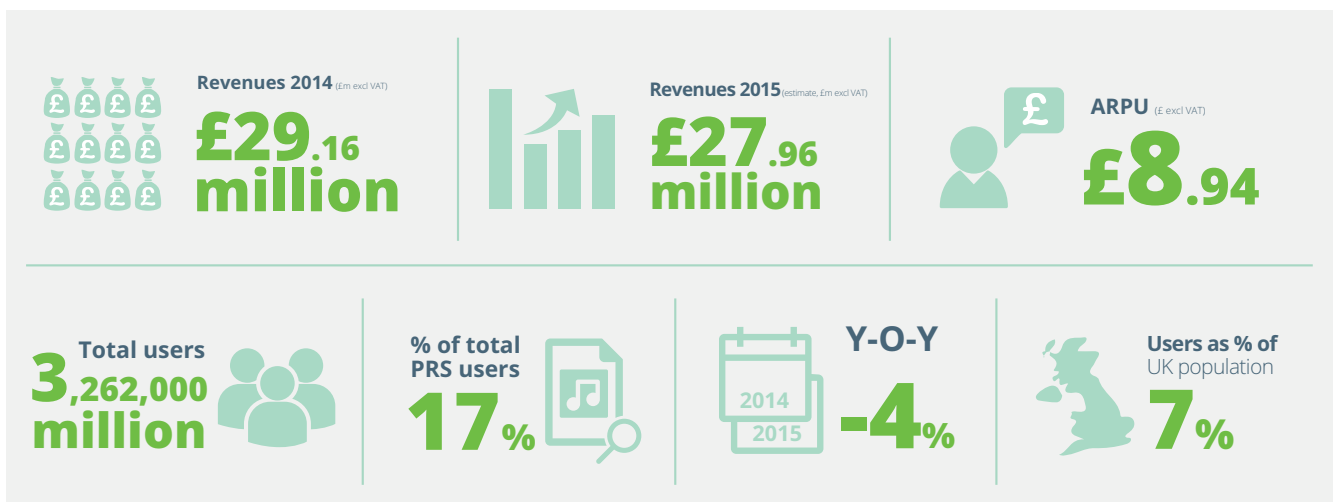
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<sup>26</sup> Source: Industry research

## No risk to service

### Music or video content

Fig. 27: Music or video content



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	801,000	92,000	31,000	128,000	124,000	136,000	128,000	75,000	87,000
Once or twice a month	651,000	88,000	18,000	88,000	163,000	128,000	79,000	44,000	43,000
Two to five times a month	687,000	101,000	44,000	145,000	176,000	111,000	62,000	26,000	22,000
More than once a week	700,000	66,000	40,000	123,000	154,000	137,000	101,000	53,000	26,000
Daily	423,000	48,000	48,000	106,000	88,000	71,000	53,000	9,000	-

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used music or video content over the last 12 months? Base n= 741

Music or video content has received a marginal classification as it is on the border of dropping from “no risk” to “low risk”, primarily because it has just over the average number of users for PRS, as well as an expected negative revenue growth between 2014 and 2015. Revenues totalled £29.16 million (excl. VAT) in 2014, and are projected to drop 4% in 2015, to £27.96 million (excl. VAT).

Although it is a declining market - albeit with the lowest year-on-year revenue loss across the 14 PRS categories in decline - service providers continue to explore new opportunities. New services include mobile web-based video-streaming in the UK. But as with the majority of cozbased services in the PRS sector, providers of video-streaming services are competing against the dominance of the app-based world and alternative card-based payment mechanisms, as well as free content.

Subscription models continue to present an opportunity for service providers, which are now looking to migrate payments from PSMS toward operator billing.

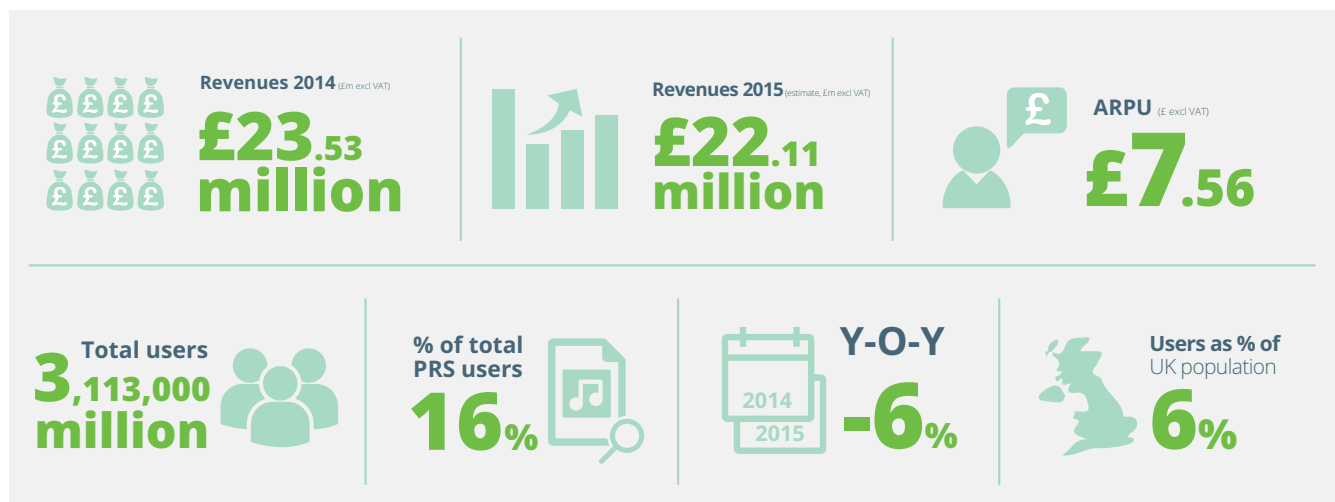
Music is dominated by the major brands. However one of the major subscription services provides operator billing as one of 10 payment mechanisms available to users. However, the industry believes that for operator billing to gain any traction in this sector, it has to be presented as one of the main payment mechanisms and not a peripheral one.

A significant number of service providers have withdrawn from the UK space and are focusing on emerging markets.

### Low risk to service

#### Internet-based information services (books, magazines, newspapers)

Fig. 28: Internet-based information services



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	1,168,000	62,000	31,000	144,000	160,000	185,000	139,000	160,000	287,000
Once or twice a month	700,000	51,000	36,000	93,000	190,000	114,000	108,000	41,000	67,000
Two to five times a month	581,000	21,000	10,000	108,000	165,000	123,000	77,000	41,000	36,000
More than once a week	448,000	31,000	15,000	93,000	118,000	83,000	46,000	21,000	41,000
Daily	216,000	21,000	15,000	15,000	36,000	31,000	26,000	46,000	26,000

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used internet-based information services over the last 12 months? Base n= 605

With an average user base and a projected decline in revenues of 6% between 2014 and 2015, internet-based information services have been classified as a low risk service. This category continues to see reasonable demand from PRS users in the UK, which should be viewed as encouraging to the service providers operating in the space, given that the services face increasing pressure from free content on the internet.

Not surprisingly, publishers are facing the dichotomy of pursuing a premium content strategy or migrating to a free-based, ad-funded model. Recently, one publisher reversed the trend altogether and introduced PRS as a payment option. By introducing PRS as a payment option, IPC Media is allowing new subscribers to sign up for print magazine subscriptions using a keyword and short code. The company claims the PRS-based payment solution will significantly increase print magazine subscriptions among young, mobile-first, consumers. At the time of launch in August 2014, the company said "soon our readers will start discovering keywords that they can subscribe with via insert cards, print ads and on the covers on their favourite magazines."<sup>27</sup>

<sup>27</sup> Source: <http://www.boku.com/ipc-media-boku-partner-innovative-text-pay-solution-offering-print-magazine-subscriptions-marie-claire-instyle-many-via/>



Traditional PRS service providers offering editorial-based content subscriptions claim their services continue to have a loyal user base despite the widespread availability of free information on the internet. These services typically can be located on mobile web-based portals which will be HTML5-based moving forward<sup>28</sup>. This will reduce the pressure on this PRS industry sector to develop separate web-based and app-based products.

In 2015, the industry anticipates the launch of education-based subscription services for minors<sup>29</sup>.

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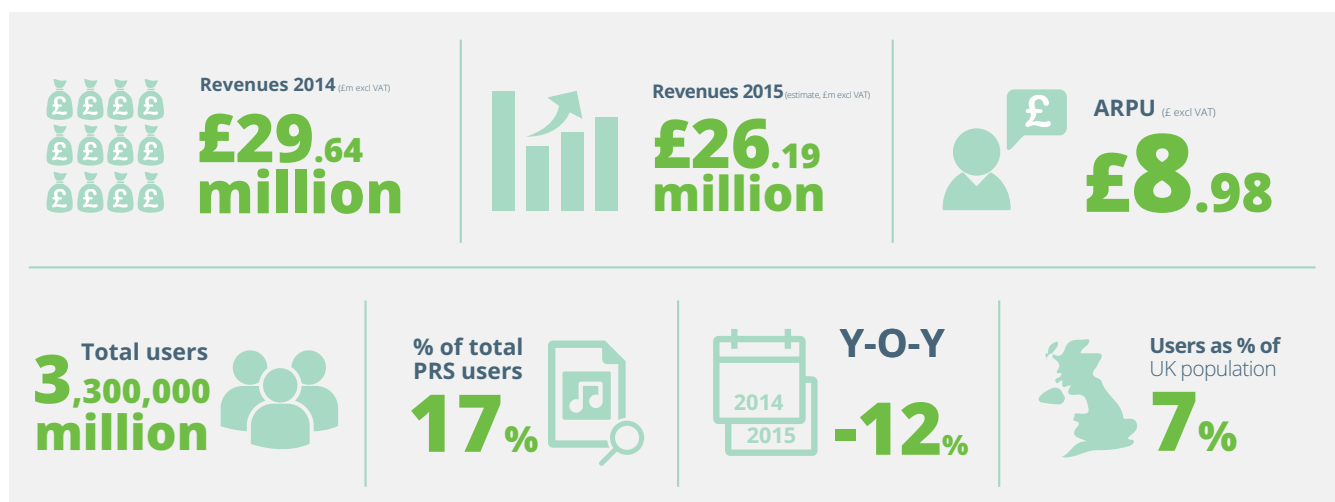
<sup>28</sup> Source: Industry research

<sup>29</sup> Source: Industry research

## Low risk to service

### Competitions or quizzes

Fig. 29: Competitions or quizzes



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	1,675,000	72,000	43,000	119,000	224,000	225,000	339,000	224,000	429,000
Once or twice a month	710,000	67,000	-	91,000	201,000	105,000	105,000	43,000	98,000
Two to five times a month	542,000	86,000	24,000	57,000	86,000	114,000	77,000	48,000	50,000
More than once a week	267,000	29,000	14,000	48,000	57,000	53,000	29,000	10,000	27,000
Daily	106,000	5,000	5,000	14,000	14,000	24,000	29,000	10,000	5,000

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used competitions or quizzes over the last 12 months? Base n= 691

Competitions or quizzes, which range from competitions run by broadcasters promoted at the end of programmes before advertising breaks, to interactive mobile internet-based competitions driven by mobile advertising or opt-in messaging campaigns, has a low risk to service rating due to its slightly above-average user base and an estimated year-on-year revenue decline of 12% between 2014 and 2015.

The belief within the sector is that the actual and potential number of users entering mobile-based competitions and quizzes is on the rise, primarily because of the growing popularity of mobile gambling. However, this is not translating into an increase in revenues: in 2014 and 2015, competitions or quizzes will generate £29.6 million falling to an estimated £26.2 million.

One explanation for this is that more users are utilising the one-off entry mechanism provided by PayforIt, as opposed to signing-up to a subscription service. Consequently, the number of users on subscriptions is falling year-on-year, with the average length of a subscription believed to be approximately one month.

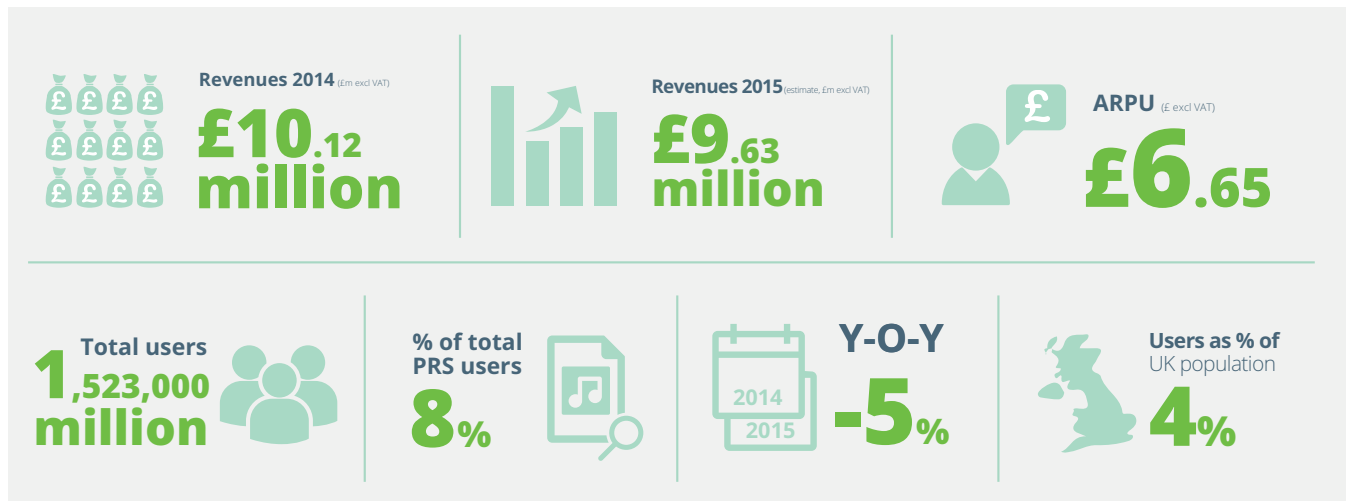
As already highlighted earlier with regard to TV & radio voting, the audience also has a level of mistrust when it comes to entering PRS-based broadcaster competitions. A viewer-insight poll conducted by one broadcaster revealed that people think they have a better chance of winning the lottery (a 1-in-14 million chance) than of winning a TV competition.

TV quizzes have been cited as the main opportunity to capitalise on the raised £6.00 drop charge option as a result of non-geographic call services (NGCS) changes in July.

## Low risk to service

### Personalisation (ringtones, ringback tones and wallpaper)

Fig. 30: Personalisation



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	572,000	73,000	29,000	50,000	65,000	106,000	117,000	66,000	66,000
Once or twice a month	341,000	66,000	4,000	32,000	69,000	61,000	54,000	22,000	33,000
Two to five times a month	317,000	70,000	11,000	59,000	73,000	68,000	29,000	7,000	-
More than once a week	193,000	29,000	-	40,000	60,000	45,000	8,000	11,000	-
Daily	100,000	16,000	-	15,000	22,000	28,000	15,000	4,000	-

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used ringtones, ringback tones and wallpaper over the last 12 months? Base n= 415

Although revenues were £10.1 million in 2014, and personalisation has a user base almost less than half the average, its year-on-year revenue decline of 5% between 2014 and 2015 places the category in low risk. In 2015 personalisation is projected to generate revenues of £9.6 million.

This slow decline in revenues is largely down to the fact that 24% of PRS users still own a featurephone and continue to personalise their device. Smartphones and apps have all but eaten into the revenue-generating potential of the personalisation market. What remains is based on a mix of PSMS and Payfort.

However, the industry view is that personalisation could see a turnaround in fortunes. The most widely discussed phenomenon is WhatsApp wallpapers, which have been driving PRS personalisation spending around Europe and Asia and are set to be introduced in the UK (at the time of writing) by multiproduct content providers. WhatsApp wallpapers are effectively add-ons for the WhatsApp IM service, of which there are approximately 11 million users in the UK<sup>30</sup>.



The industry has a mixed view of WhatsApp wallpapers that will be offered on a £4.50 subscription model. The overriding opinion is that they could become the “modern Crazy Frog” and could set the industry back a number of years by damaging the delicate relationship constructed between the consumer and the PRS sector with non-compliant activity.

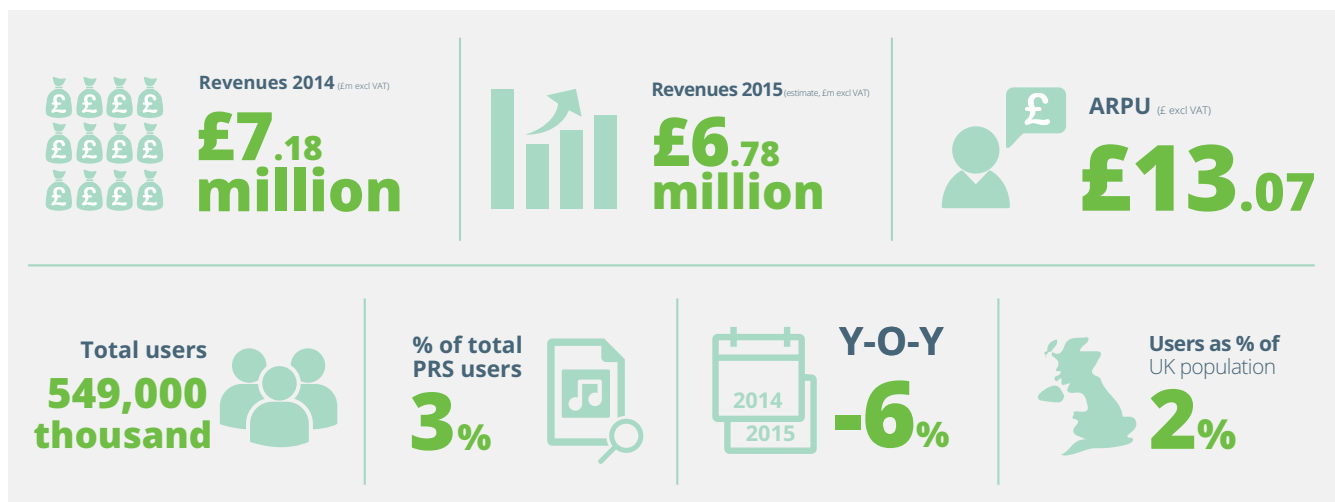
What could curtail the take-up of WhatsApp wallpaper, and all personalisation services on PRS, is the cost. Personalisation ARPU is among the lowest of all PRS categories (£6.65 per annum).



## Low risk to service

Virtual gifts in the social media space, such as Facebook credits and SwapIts

Fig. 31: Virtual gifts



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	124,000	12,000	3,000	24,000	32,000	27,000	18,000	6,000	2,000
Once or twice a month	127,000	21,000	-	35,000	41,000	24,000	-	6,000	-
Two to five times a month	142,000	21,000	-	38,000	41,000	30,000	9,000	3,000	-
More than once a week	97,000	15,000	-	12,000	38,000	27,000	3,000	2,000	-
Daily	59,000	6,000	-	21,000	18,000	14,000	-	-	-

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used virtual gifts in the social media space over the last 12 months? Base n= 186

Year-on-year revenue decline between 2014 and 2015 is predicted to be 6%, but the fact virtual gifts has the smallest user base places the service between low risk and medium risk. The virtual gifts market was worth £7.18 million in 2014 and is expected to fall to £6.78 million in 2015.

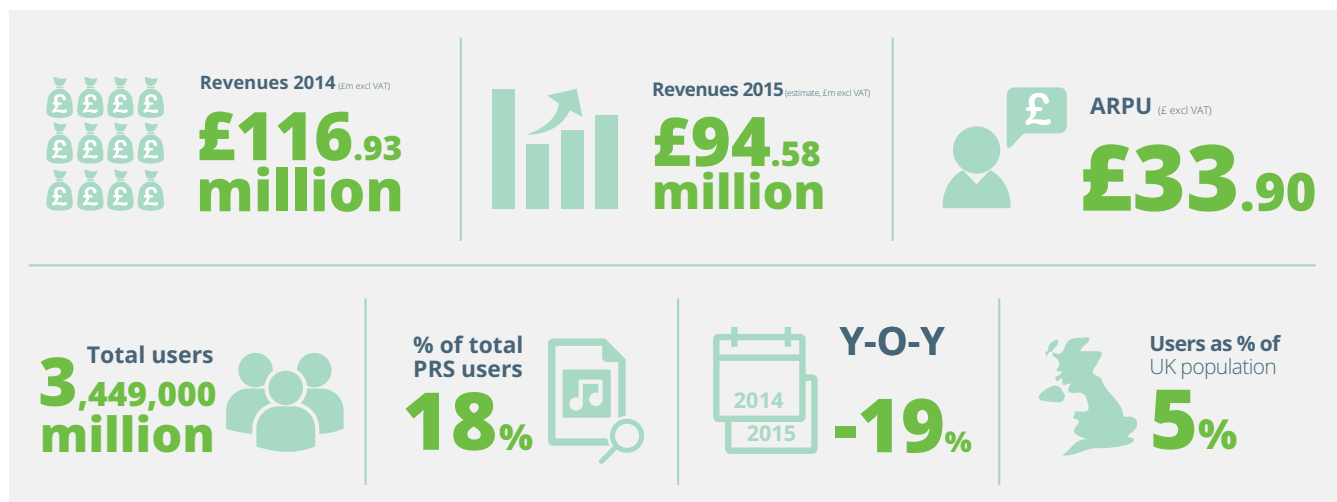
The appeal of virtual gifts failed to ignite significant consumer interest in the service, even at its peak between 2009 and 2011, and with Facebook now having stopped Facebook Credits, the service has maintained a niche audience.

Virtual gifts opportunity emanated from the online flirt and dating environment, permitting users to boost their rating or send potential suitors virtual flowers, for example. But the migration of the majority of flirt and dating online services to apps has vastly limited the size of the available audience.

## Medium risk to service

### Directory enquiries

Fig. 32: Directory enquiries



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	2,209,000	73,000	7,000	132,000	294,000	286,000	514,000	389,000	514,000
Once or twice a month	800,000	37,000	29,000	81,000	176,000	176,000	103,000	103,000	95,000
Two to five times a month	279,000	29,000	-	29,000	73,000	74,000	38,000	29,000	7,000
More than once a week	117,000	22,000	-	15,000	29,000	22,000	29,000	-	-
Daily	44,000	-	-	15,000	22,000	7,000	-	-	-

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used directory enquiries over the last 12 months? Base n= 470

Directory enquiries (DQ) is a service in decline and one of the main premium rate services under threat from widespread mobile internet adoption. Between 2013 and 2014, revenues fell 17%, from £140.93 million to £116.93 million, and they are projected to drop 19%, to £94.58 million in 2015. Because DQ has an average user base, DQ has been classified as a medium risk.

Until now, DQ service providers have increased pricing to offset the decline in revenues as a direct consequence of the drop in users, but there is growing concern within the sector that consumers will not tolerate further increases.

Until actual changes to market pricing occur, industry views remain largely theoretical. However, the average DQ customer spent £2.80 per month on the service in 2014, and on an annualised basis DQ represents the highest ARPU of any premium-rate service. Nevertheless, an increasing number of DQ customers experienced "bill shock" in 2014 and contacted PhonepayPlus.

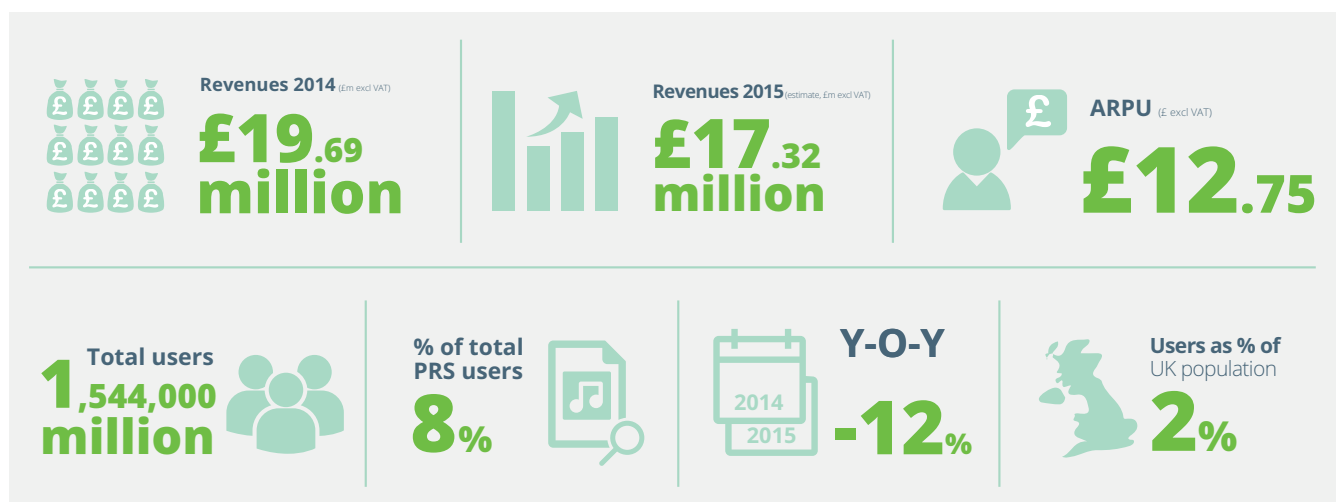
In 2015, DQ is expected to be replaced by charitable donations as the number one PRS service.

In terms of usage, two-thirds of users call the service on a quarterly basis, one-quarter use it monthly, with most of the rest using it weekly and just 1% using it on a daily basis.

## Medium risk to service

### Dating or flirt chat service - (incl. 087)

Fig. 33: Dating or flirt chat service



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	462,000	-	-	55,000	148,000	130,000	92,000	37,000	-
Once or twice a month	324,000	-	-	83,000	92,000	103,000	28,000	9,000	9,000
Two to five times a month	361,000	-	-	111,000	102,000	102,000	46,000	-	-
More than once a week	240,000	-	-	102,000	46,000	65,000	9,000	18,000	-
Daily	157,000	-	-	18,000	28,000	83,000	28,000	-	-

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used dating or flirt chat service over the last 12 months? Base n= 167

Dating or flirt chat service has been classified medium risk primarily because its user base is half the average number of users per PRS category, and its revenues are forecast to drop 12% between 2014 and 2015 from £19.69 million to £17.32 million.

As revenues for this sector are on a downward trajectory, service providers are becoming increasingly competitive and using multiple PRS payment mechanisms to reach as many of their target customers as possible: 087 numbers, PSMS or PayforIt. There are 1.5 million people using PRS to process transactions.

A number of service providers continue to use 087 numbers to capitalise on the lower cost-per-minute compared to 09 numbers, as they compete for a shrinking user base. As changes to spend caps as part of non-geographic call services (NGCS) do not target 087 numbers, its introduction in July 2015 will not have an impact on companies operating 087.

Increased pressure is coming from alternative billing mechanisms such as credit cards. A number of service providers have stopped using premium rate as a billing mechanism in a bid to migrate users to credit cards, where the industry claims a small percentage of users are spending more than £2,000 a month. Service providers using PRS as a payment mechanism are competing for users that on average spend around £1 per month: Annualised ARPU is £12.75 (excl VAT).



Consequently, PRS-based service providers are minimising their marketing spend and the acquisition of new customers in favour of maintaining their existing customer base, in a bid to counter month-on-month drops in revenue.

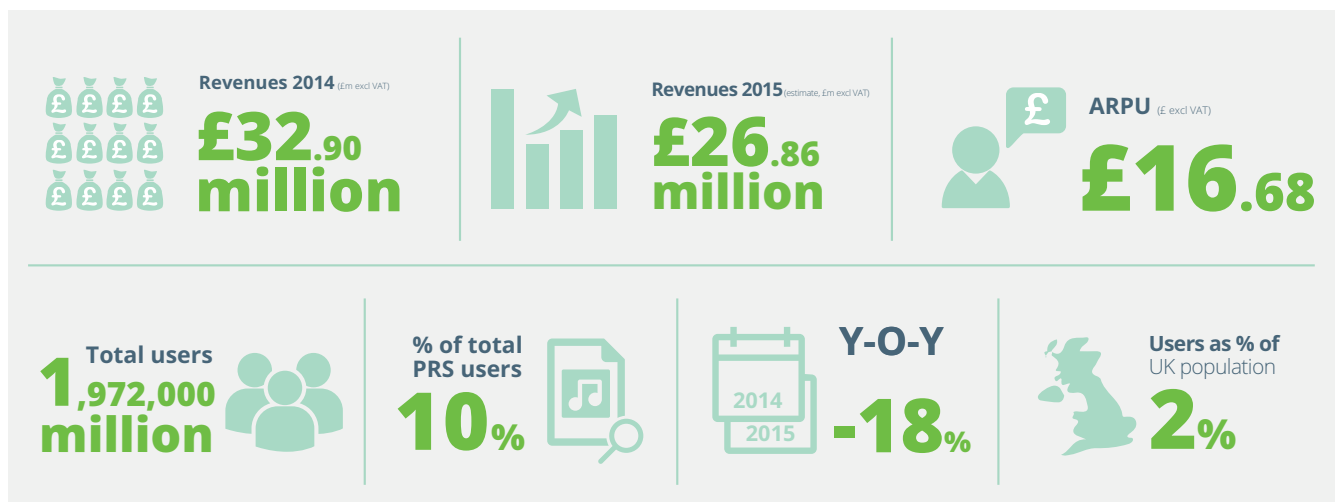
The consumer research supports this strategy, given the high frequency of users. Over two-thirds of users access the service once a month or more. One-quarter of consumers will use the service more than several times a week.

Although social networks were perceived to be the major threat to these services, the industry believes the proliferation of smartphones and the availability of dating and flirt apps are having the most destructive impact on this sector.

## High risk to service

### Adult content (video, images, chat)

Fig. 34: Adult content



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	627,000	-	-	142,000	119,000	119,000	150,000	32,000	65,000
Once or twice a month	440,000	-	-	75,000	216,000	108,000	22,000	-	19,000
Two to five times a month	453,000	-	-	119,000	172,000	140,000	22,000	-	-
More than once a week	259,000	-	-	65,000	75,000	97,000	11,000	11,000	-
Daily	193,000	-	-	54,000	75,000	54,000	10,000	-	-

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used adult content over the last 12 months? Base n= 182

Free adult content on the internet saw PRS revenues plummet 70% between 2013 and 2014, from £108.1 million (excluding VAT) to £32.90 million (excluding VAT). Even with the revised service taxonomy, no other premium rate service experienced such a dramatic decline in revenues.

Between 2014 and 2015 revenues are projected to fall 18%, from £32.9 million to £26.86 million, and with a below average user base, adult content is considered a service at high risk. Video accounted for over two-thirds of revenues in 2014.

PayforIt is becoming the primary platform for processing adult purchases, resulting in conversions falling by half. Changes to the customer flow from Enhanced Single Click to Enhance Purchase Flow in the latter part of 2014<sup>31</sup> - the insertion of an additional layer to the consumer journey and purchase process - is having a direct impact on conversions. The impact of Enhance Purchase Flow is expected to impact adult revenues in 2015.

The companies involved within the adult PRS industry, as well as companies close to the sector, believe that half of all adult-video purchases are made inadvertently. What is likely to limit the number of inadvertent purchases, was the introduction of a smaller click button in January 2015. Prior to this, the click button to purchase content filled 80% of the mobile screen, but was reduced to 20% in 2015.

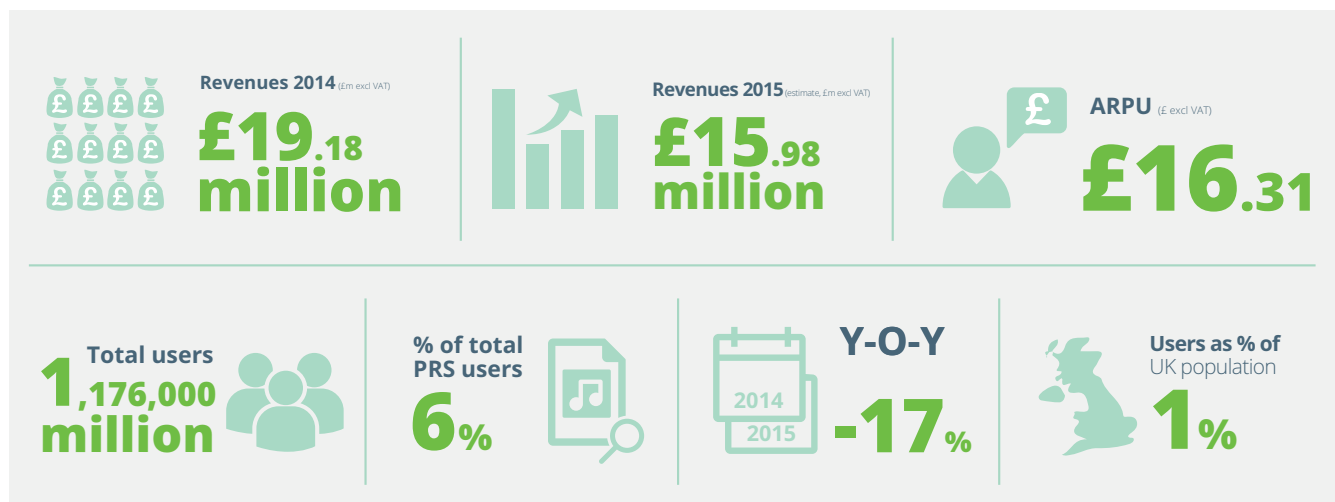
Nevertheless, in 2014, one-third of monthly complaints to PhonepayPlus related to adult content.

<sup>31</sup> Source: Industry research

### High risk to service

#### Off-handset purchases for adult-related content (e.g. DVD unlock)

Fig. 35: Off-handset purchases for adult-related content



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	172,000	-	-	57,000	43,000	57,000	15,000	-	-
Once or twice a month	301,000	-	-	86,000	143,000	72,000	-	-	-
Two to five times a month	359,000	-	-	72,000	143,000	115,000	29,000	-	-
More than once a week	258,000	-	-	86,000	86,000	72,000	-	14,000	-
Daily	86,000	-	-	29,000	14,000	43,000	-	-	-

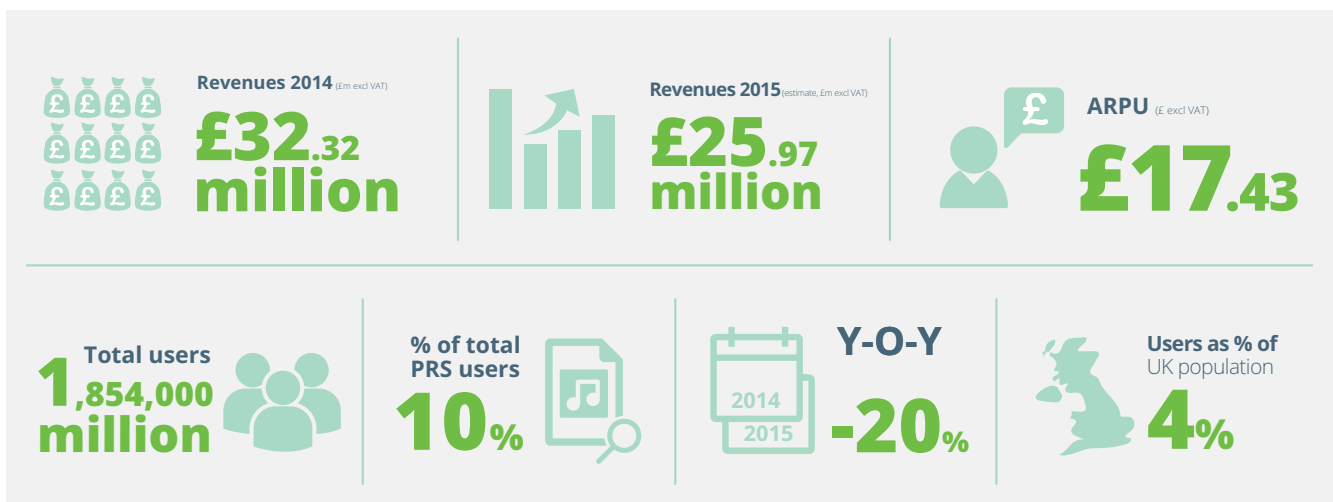
Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used off-handset purchases for adult-related content over the last 12 months? Base n= 82

Off-handset purchases for adult-related content refers to the purchase of content not on a phone – such as pictures on the internet – by calling an 09 premium line or a 5-digit voice shortcode. The service is in decline and is expected to fall from £19.18 million (excl VAT) in 2014 to £15.98 million (excl VAT) in 2015, a fall of 17%. With year-on-year decline in revenues, coupled with a well-below-average user base of around 1.1 million users, the service has been classified as high risk.

## High risk to service

### Low cost international or reverse charge calling

Fig. 36: Low cost international or reverse charge calling



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	686,000	-	26,000	61,000	143,000	128,000	103,000	82,000	143,000
Once or twice a month	395,000	20,000	5,000	67,000	133,000	52,000	36,000	31,000	51,000
Two to five times a month	441,000	36,000	6,000	67,000	92,000	107,000	61,000	31,000	41,000
More than once a week	256,000	5,000	5,000	51,000	61,000	72,000	26,000	10,000	26,000
Daily	76,000	5,000	5,000	20,000	31,000	5,000	10,000	-	-

Source: PRS market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used low cost international or reverse charge calling over the last 12 months? Base n= 362

The rise of over-the-top communications providers, such as Skype and Viber, providing free or ultra-low-cost international call rates is having a major impact on mobile operator revenues, including on revenue related to international traffic and low-cost international or reverse-charge calling. The introduction of voice-over-IP (VOIP) on leading apps, such as WhatsApp, is expected to exacerbate the impact on this sector.

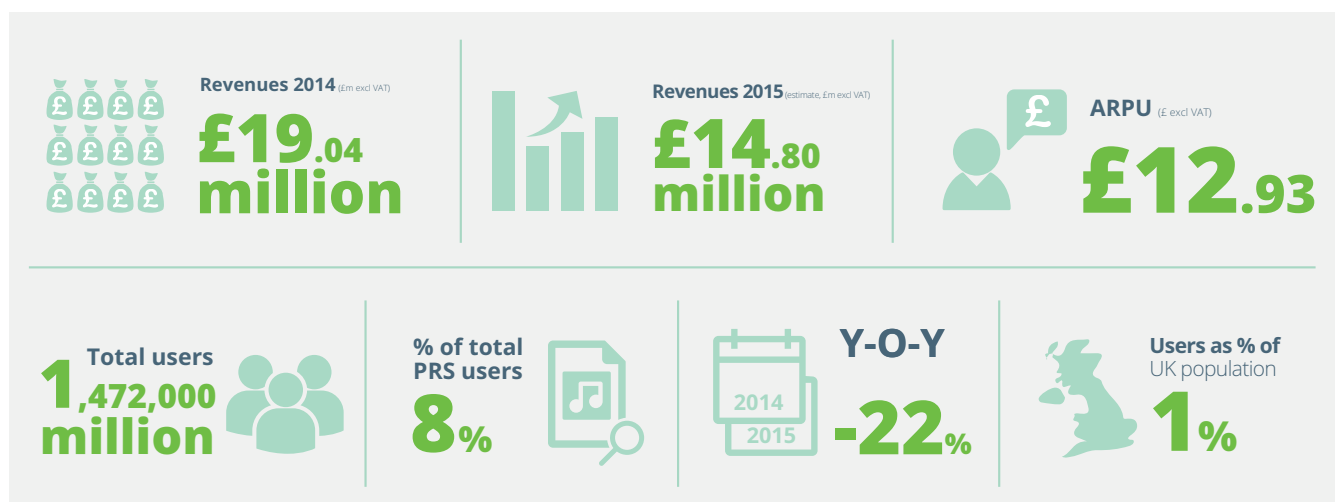
Regulation could also play its part by reducing the per-minute call rate to and from a mobile phone. UK communications regulator Ofcom announced plans in June 2014 to reduce the mobile termination rates in the UK from £0.08 per minute to £0.05 per minute. Similarly, the proposed abolition of roaming charges across Europe could potentially stimulate the international call market from mobile phones. The impact of these regulatory developments on the low-cost international and reverse-charge calling sector is incumbent on the savings being passed onto the end consumer.

Even without regulatory intervention, low-cost international and reverse-charge calling is forecast to experience a 20% year-on-year decline from 2014 to 2015, and with a below-average user base, the service is considered high risk.

## High risk to service

### Tarot or astrology

Fig. 37: Tarot or astrology



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	387,000	12,000	-	62,000	75,000	100,000	88,000	38,000	12,000
Once or twice a month	362,000	25,000	12,000	75,000	100,000	87,000	51,000	12,000	-
Two to five times a month	337,000	25,000	-	87,000	75,000	88,000	37,000	25,000	-
More than once a week	287,000	12,000	37,000	87,000	51,000	100,000	-	-	-
Daily	99,000	25,000	-	12,000	50,000	12,000	-	-	-

Source: PRs market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used tarot or astrology over the last 12 months? Base n= 118

Tarot or astrology (including horoscopes) has a below-average user base and is projected to experience a revenue decline of 22% between 2014 and 2015, placing the service as high risk. During this timeframe, revenues will fall from £19.04 million to £14.8 million.

To a certain extent, the tarot or astrology (and horoscopes) sector mirrors the developments that have unfolded in the dating and chat-line market. Namely, internet-based alternatives and rival payment platforms are driving down the PRs-based user base and prompting service providers to compete on price, using a number of PRs options, ranging from 087 numbers, 09 and voice short codes. A number of service providers also continue to offer these services as a subscription model and claim to have a loyal user base.

However, the principal ambition of service providers is to migrate high-spending users from PRs to credit card payment where spend is not capped, although the majority of service providers provide set-priced time-based sessions, such as £15 for 20 minutes.

Based on ARPU for the sector, which equates to a little over £1 per month, it suggests that the lower price points will appeal to the majority of users and that potential price changes, such as the introduction of changes to NGCS in July, will provoke an adverse reaction among users.





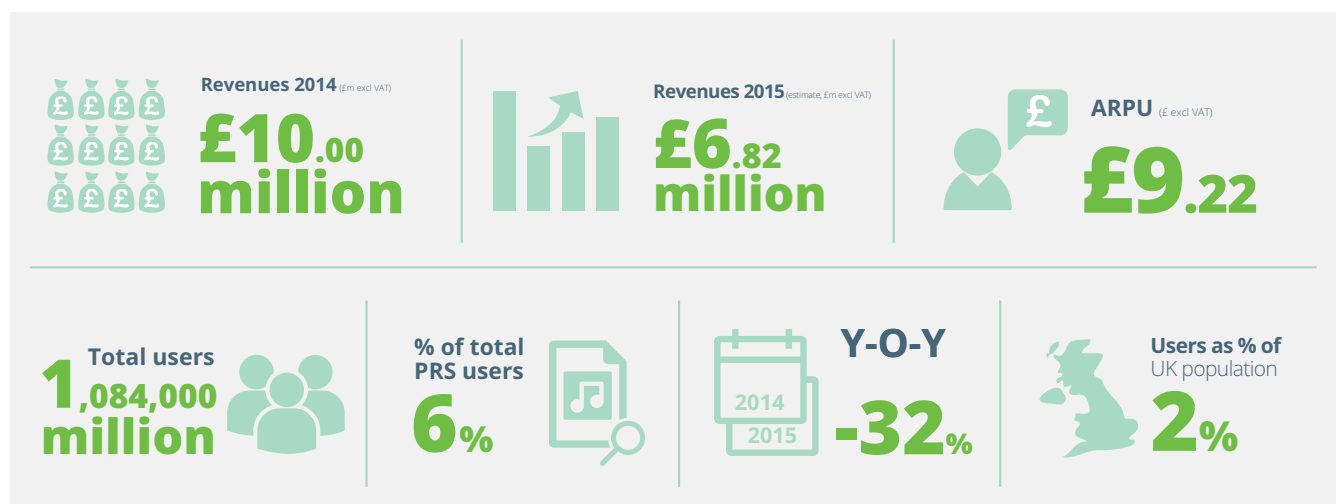
Changes to NGCS are not expected to have a major impact on the sector, although the increase of the £1.53 per minute ceiling to £3.60 per minute on 09 numbers will potentially increase the appeal of PRS to service providers and could potentially appeal to users not wanting to share their credit card details.

To potentially offset the decline in spending and the number of users – while maintaining that there is an opportunity with these services – companies offering tarot and astrology services are initiating new business strategies that use PRS to promote the use of alternative channels. Service providers are looking to use revenue from these services to fund online editorial costs to drive traffic to related websites and increase advertising revenue.

### High risk to service

Voice-based information services (eg weather hotline, text alerts, etc.)

Fig. 38: Voice-based information services



Customer usage	Total	11-15	16-17	18-24	25-34	35-44	45-54	55-64	65+
Less than once a month	392,000	15,000	15,000	41,000	81,000	77,000	71,000	51,000	41,000
Once or twice a month	249,000	20,000	5,000	71,000	41,000	57,000	10,000	25,000	20,000
Two to five times a month	275,000	25,000	10,000	36,000	92,000	66,000	25,000	11,000	10,000
More than once a week	117,000	15,000	-	20,000	31,000	15,000	31,000	5,000	-
Daily	51,000	15,000	-	10,000	5,000	20,000	-	-	-

Source: PRs market sizing for PhonepayPlus, industry research. PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q26. How frequently have you used voice-based information services over the last 12 months? Base n= 212

Information available freely on the internet is having a debilitating impact on revenues for voice-based information services. However, the consumer survey has revealed that mobile internet penetration among PRs users stands at 76%, which leaves 24% (approximately 4.6 million people) that do not browse on their mobile device and would potentially be the target audience for voice-based information services – though that is not to exclude mobile internet users from using voice-based information services. However, the number of users as of January 2014 stood at 1.1 million, which is less than one-quarter of the potential 4.6 million PRs users.

Clearly, the rapid adoption of smartphones and the growing number of mobile internet users mean voice-based information services' days are numbered.

Subsequently, voice-based information services market generated £10 million (excl VAT) revenues in 2014, and this is projected to fall 32% in 2015 to £6.82 million, representing the greatest year-on-year decline across all PRs services. This is a high risk service.

Section 4

# ANALYSIS

**10 key findings**

There will continue to be a role for premium rate services, but that role will become more niche, particularly across the 14 PRS categories in decline. Consequently, much of the premium rate service industry experienced a year of either preservation (Level 2 providers) or transition (Level 1 providers) in 2014.

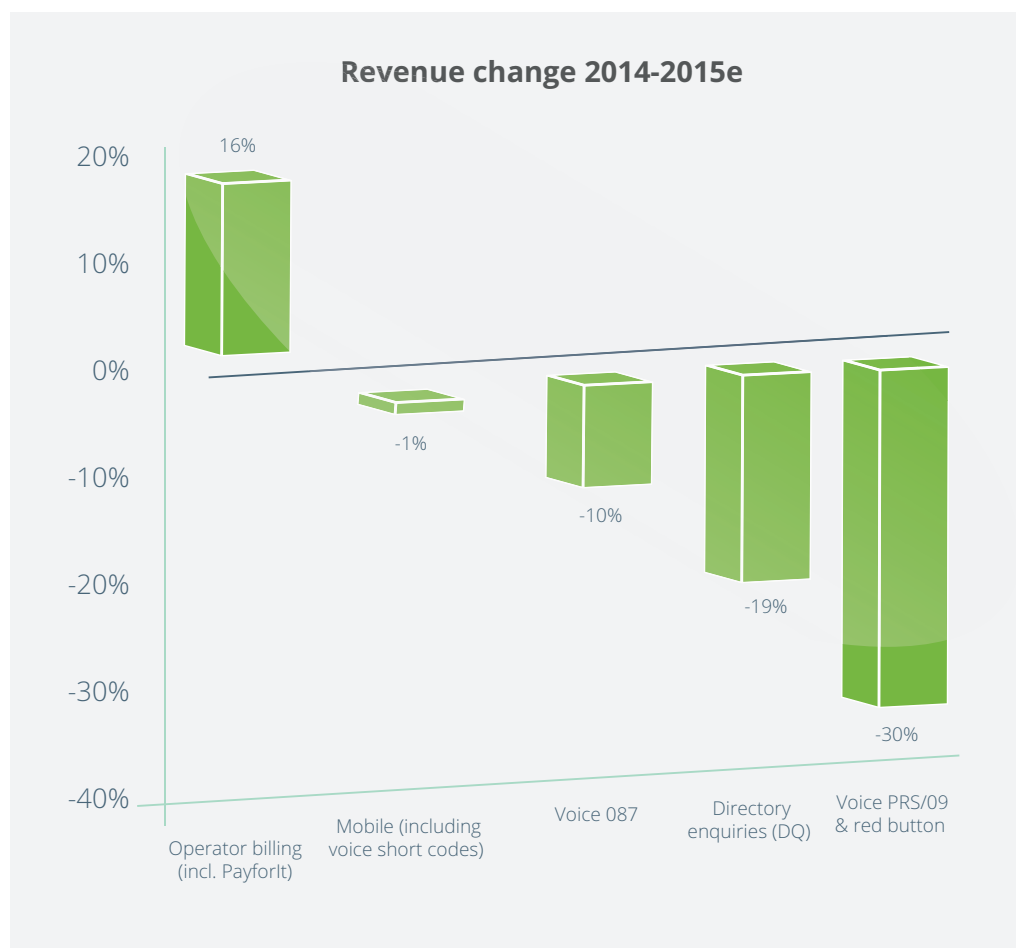
### 1. Voice revenues on the decline, mobile revenues on the rise

The PRS market is in decline and it is voice-based services that are bearing the brunt of the decline in revenues. As already highlighted in Section 1, revenues from voice-based payments are projected to fall 21% between 2014 and 2015, compared to a 2% increase in revenues for mobile-based payments.

In fact, it is the 16% year-on-year revenue growth from operator billing that ensures mobile experiences growth of 2%. However, without the inclusion of operator billing generated revenues to the overall “mobile” category, revenues generated by mobile-based PRS payments (such as PSMS and voice short codes) are predicted to fall 1% between 2014 and 2015.

Despite this, in 2015, mobile-based PRS payments will account for 66% of total PRS transactions, up on 60% the previous year. Mobile presents the greatest opportunity for the longevity of PRS and the safeguard of sustained revenues.

Fig 39: Revenue change 2014-2015e



Source: PRS market sizing for PhonepayPlus, industry research



Despite revenue growth in mobile-based services, there is discontent. For example, PSMS' position within sectors of the PRS industry as a payment mechanism is looking increasingly tenuous for services other than charitable donations. Its role within mobile operators and some service sectors, such as adult, started being phased out in favour of PayforIt during 2014 and this is expected to accelerate throughout 2015.

The meteoric revenue growth enjoyed by PayforIt between 2013 and 2014 of 86% was due to the fact operator billing was a nascent payment technology. But this level of growth – at least via PayforIt – is not projected to be sustained into 2015, with revenue growth expected of 16% between 2014 and 2015. Part of this slow down in growth can be attributed to PayforIt's evolution from Enhanced Single Click to Enhance Purchase Flow in 2014 affecting conversion rates by up to 50% on certain PRS, such as Adult.

## 2. PRS survives technological advancement

The consumer survey revealed that PRS lost an estimated 2.8 million users during 2014. However 16.5 million users, as estimated at the start of 2015, remains a considerable base. There could be more users. The supplementary consumer survey<sup>32</sup> revealed that one-third of people were aware of PRS services – which correlates with the main consumer survey – while a further 12% of respondents required clarification of what PRS were. This suggests there could be an extended base of PRS users beyond the known 16.5 million.

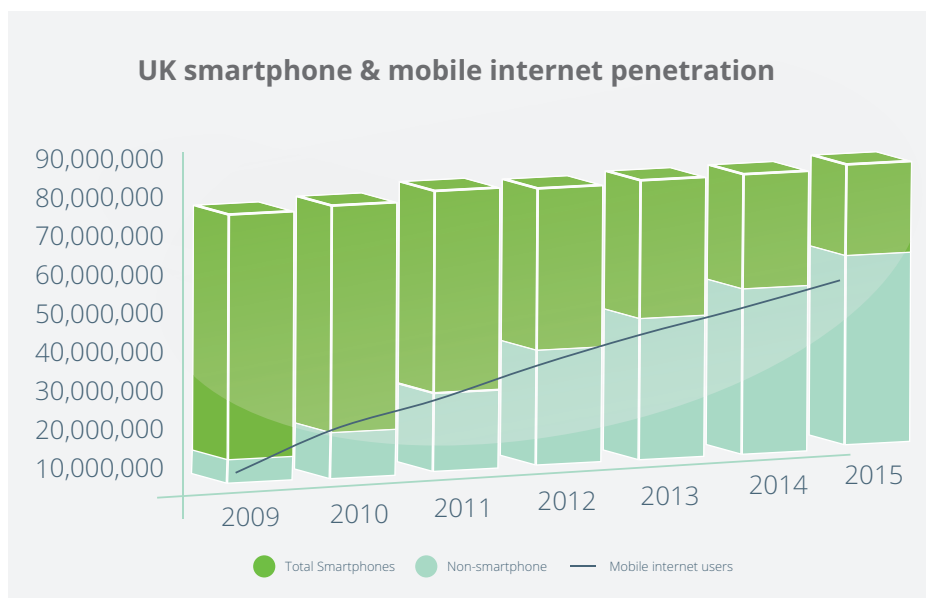
What is all-the-more encouraging, is that PRS has survived tremendous technological developments in devices and networks. Devices have evolved from basic mobile phones, cameraphones, gaming phones, featurephones, and most recently smartphones and tablets. During which time, basic 2G voice and messaging networks have evolved into 3G and most recently 4G networks, complemented by Wifi.

Combined, these technological advancements have created and subsequently enhanced the mobile internet experience and spawned the app phenomenon, delivering rich-media content, entertainment and information services to consumers on the go.

These developments have had a direct impact on the demand for PRS. The consumer survey confirmed the “availability of free content elsewhere” and “a lack of interest” are among the primary reasons for the departure of users during 2014.

<sup>32</sup> Street research; see Methodology

Fig. 40: UK smartphone & mobile internet penetration



Source: Ofcom Communications Report 2014, mobilesquared UK market data

But there are smartphone users that also use PRS. Based on the consumer survey, 72% of PRS users had a smartphone in 2014 – 24% with a featurephone and 4% with fixed-line access only – which suggests that PRS has to a certain extent navigated the consumer's evolution from basic mobile phone through to smartphone and competed with the rise of the mobile internet. So much so, that 16.5 million PRS users remain.

### 3. The app opportunity

For many Level 2 providers, 2014 represented a period of consolidation to preserve, protect and monetise their existing user base within a shrinking PRS market. This resulted in a distinct lack of innovation within the sector, with new services and content entering the UK based on extensions of existing concepts and models, such as video streaming services and educational content.

As devices have evolved, so too has consumer behaviour. Based on findings from the consumer survey, it is estimated that the average PRS user will spend 60% of the time on their device on a daily basis using apps. Typically, iOS users spend an average of 80 minutes per day on their iPhones, and Android users spend an average of 50 minutes per day<sup>33</sup>.

<sup>33</sup> Source: Industry research, mobilesquared research



Fig 41: Estimated daily mobile usage, PRS users, 2013-2014

	Phone-based comms (voice, messaging, email)	Browser-based activity	App-based activity
2013	25.58%	13.47%	60.96%
2014	29.26%	12.92%	57.82%

Source: PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q10. For what and how often do you use a mobile phone for? Base n= 2,877. Q11. On an average day using your mobile phone, what percentage of your time is spent [using selected services]? Base n=2,877. Q12. How has your mobile usage changed over the last 12 months? Base n=2,877.

As smartphone users account for 72% of the PRS user base in 2014, it is imperative that premium rate service providers look to position (and present) their content and services in a widely-adopted format – an app – to extend the longevity of their offering based on consumer behaviour. Otherwise, competing apps and the internet coupled with alternative payment options, like credit cards, will become the death knell for a number of premium-rate services.

Apps present one of the greatest opportunities for the PRS industry and could potentially safeguard the longevity of a premium rate service, provided PRS providers can morph their service into an app. As highlighted by the consumer survey of PRS users, apps account for almost three-fifths of daily activity on a mobile phone. Apps are therefore the most popular channel for engaging users on a frequent basis.

There are encouraging signs that a section of Level 2 providers operating within tarot or astrology, games, and personalisation are exploring app-based versions of their premium-rate services during 2015<sup>34</sup>.

#### 4. Trust in charitable donations

The PRS industry might be in decline but it can demonstrate that opportunities can arise. From an inauspicious beginning, charitable donations has grown exponentially to become a possible “hero service” for PRS.

Clearly consumers have been attracted to the simplicity of PRS as a payment mechanism for charitable donations, compared to alternative payment channels like credit or debit cards.

While the service does not generate revenues in the form of out-payments for industry, it reaffirms belief that consumers trust payments via PRS, and PSMS in particular, to deliver their donations of £3, £5, or £10, as well as the option of regular monthly payments.

As charities look to increase their PRS payment options in 2015 to include Payfortl, the consumer trust associated with PSMS to make a donation could extend to incorporate operator billing and help drive its adoption in other areas.

Equally, the ongoing appeal for games (including apps and games on social networks) continues to present an opportunity for PRS. Given that operator billing is one of the most recent additions to the payment options available to consumers, the rise of the 3 Gs – and the associated revenues – confirms consumers want payment options, such as PRS. This has been further boosted by the early success enjoyed by Google since it introduced operator billing as a payment option for apps and in-app purchases on the Play app store.

<sup>34</sup> Source: Industry research

### 5. Consumer perception of PRS

The cost of PRS services remains something of an enigma for consumers. The supplementary consumer survey<sup>35</sup> revealed that only one-quarter of respondents claimed to know how much premium rate services cost. A further 34% thought they knew the cost, while 41% said they did not know.

When asked the cost of premium rate services such as voting on the X Factor, calling directory enquiries or calling chat lines, the average response was £1.63 per vote, £1.08 per minute and £2.77 per minute, respectively. In total, the broad range of answers stretched from £0.25 to £10.

Despite the clarity required when promoting PRS as mandated by regulation, consumer perception of PRS pricing is generally inaccurate. This implies that consumers are yet to grasp the tariff structure associated with PRS, which itself presents a dichotomy concerning PRS pricing. Cost-related issues were the principal reasons for PRS users to reduce their usage of PRS or stop using the services altogether, as highlighted by the main consumer survey findings.

Fig. 42: Cost-related issues for reducing usage of, or stopping PRS

Reason	PRS users
I can get content free elsewhere	2,836,000
I have less disposable income	2,185,000
I can't afford them anymore	2,641,000
I wasn't aware how much I was spending on these services	939,000

Source: PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q36. What reason/reasons can you attribute for using these services less or stopping using them altogether? Base n=1,446.

This latter point suggests PRS pricing is not reflective of changing market dynamics, such as the impact of free alternative content on the internet, and changes in consumer expenditure via their mobile device. And explains why a number of PRS categories have been classified as high risk.

For instance, monthly average revenue per user (ARPU) for 2014 revealed that the average "adult" user spent £1.39 per month, yet a video clip would cost £6. Similarly, one of the PRS services experiencing growth, "games (or apps) charged to my bill", had a monthly ARPU of £0.62 in 2014, yet service providers are maintaining subscription models charging £4.50 per week. Regardless of whether the service has been classified as growth or high risk, pricing models reflect a short-term ambition targeting a minority of users.

The PRS industry should set two clear targets in the near term. Research suggests that, firstly, a reduction in pricing is needed to encourage a greater percentage of the PRS user base to increase their expenditure. And secondly, by conveying a clearer pricing strategy for consumers will help alleviate any fears associated with using PRS. These are moves which could potentially offset, or at least slowdown, the decline in users that the PRS industry is experiencing.

While greater clarity of pricing is anticipated with changes to non-geographic call services (NGCS) covering 09 numbers in July, the PRS industry should continue to explore means of making PRS pricing for both voice-based and mobile-based services more transparent – and understandable – for the consumer.

<sup>35</sup> Street research; see Methodology





## 6. Regulatory developments

The anticipated release of Payment Services Directive II (PSDII) in July 2015 is expected to accelerate operator billing activity in the UK, when updates to the existing Payment Services Directive from 2007 will be unveiled by the European Commission (Directorate General Internet Market).

The growth of operator billing has effectively stalled as Level 1 providers used 2014 and the first quarter of 2015 to explore the opportunities and their intentions for mobile payments. Both opportunities and intentions are expected to become considerably clearer following the outcome of PSDII. The current PSDII proposals will likely limit mobile payments to €50 per transaction and € 300 per month for the exemption to apply.

But for companies exploring the opportunity of expanding beyond digital goods and services into physical and quasi-physical goods and services, they can currently become an Authorised Electronic Money Institution (EMI) by applying for an e-money license. As of the end of 2014, two Level 1s in the UK held e-money licenses.

In addition to the two e-money licences already acquired, the research revealed that other established Level 1 providers had either started the 18-month authorisation process for an e-money license, or were delaying the process until the opportunity surrounding physical and quasi-physical goods and services becomes clearer.

Consequently, the industry expects an escalation in activity surrounding operator billing, and the broader introduction of physical and quasi-physical goods toward the end of 2015 as the Level 1 providers start revealing their mobile payment strategies. By which point a clearer understanding of the mobile payments landscape is expected.

It has been suggested that companies without an e-money license could potentially partner with companies holding an e-money licence as a means of gaining FCA authorisation for the sale of physical and quasi-physical goods, as a cost-effective way to meet compliance regulations without the cost of acquiring an e-money licence.

Whether companies holding an e-money licence would be prepared to concede competitive advantage to rival companies is unlikely in the short-term, but could be a possibility longer term as the market unfolds. But any such development would be dependent on whether it meets FCA requirements.

## 7. Collaboration

Since late 2013, PhonepayPlus has been actively collaborating with industry, following a period when relations became increasingly strained. During this time, there have been a number of public examples of industry and regulator collaboration. This includes changes to introduce regular text payments in the charity sector, including the advent of "SKIP", cooperation to stifle the significant threat posed by affiliate networks in 2013, to tackle the issue of re-direct, and the formation of the Rapid Response Unit in 2014 in conjunction with AIME and the Mobile Broadband Group, to counter the imminent threat posed by serious non-compliant activity.

The Rapid Response Unit has been formed to address issues that emerge, calling on the relevant industry expertise to identify the solutions to address this and deploy quickly, rather than apply what has been described as the enforcement took kit. Once the issue has been resolved the Unit disbands.



PhonepayPlus acknowledges that the best way of keeping up with developments in the marketplace is by working with industry. When appropriate, the regulator will meet with industry and work through the issues as part of an informal process to present policy solutions.

In a broader context, PhonepayPlus has also supported AIME, the Mobile Broadband Group, and the UK Treasury, on Payment Services Directive II (PSDII).

This period of heightened collaboration has been heralded by both the industry and regulator as making significant steps in the right direction, with on-going progress anticipated throughout 2015 based on proportionate collaboration.

## 8. Future of payments

### Making operator billing appeal to the blue-chips and merchants

The rise of smartphones has created the opportunity for mobile payments and opened the door for sections of the PRS industry to look to diversify or expand into the sale of physical and quasi-physical goods charged to a phone bill. As the next bastion of growth for the PRS industry, operator billing – excluding PayforIt – could result in companies competing for revenue across other industries, as opposed to competing for revenues within a declining and isolated market.

The promise of revenue generated from physical and quasi-physical goods that is fundamentally remodelling the PRS landscape. A growing number of Level 1 companies operating within PRS with a long-term strategy are focusing on the operator billing opportunity, which may result in these companies reducing their role in traditional PRS, in order to pursue a truly scalable operator billing model beyond the limitations of digital goods and services.

The dilemma facing the majority of companies within the PRS industry, as they readily admit, is that they cannot identify exactly what the operator billing opportunity is, what exactly the products and services will be, and when exactly it will become commercially viable. All they know is that operator billing represents a vast opportunity and will ultimately become a mainstream payment mechanism, not only for digital content and services, but for physical and quasi-physical goods also. Not surprisingly, there is an abundance of optimism surrounding operator billing throughout the PRS industry.

*The short and medium-term prognosis of UK Phone-paid premium rate services* report by Deloitte and commissioned by PhonepayPlus, published in November 2014, claimed operator billing has the potential to generate a total addressable market for digital goods and services of £500 million by 2019.

One service touted as being ideal for operator billing is car park payment, which was as industry estimated to be worth in excess of £3 billion<sup>36</sup> in 2012. If operator billing could account for 10%, this alone would represent a £300 million opportunity.

Parking is one industry already linked with the frictionless payment process associated with operator billing, other sectors and services include toll roads, vending machines, take-aways, and ticketing. Additional areas raised by industry cover electric car charging, hiring of rental bikes (such as Boris Bikes), and Father-to-child airtime credit payments. The industry also believes services will be launched addressing the health and education sectors.

<sup>36</sup> Source: the British Parking Association in 2013; [http://www.britishparking.co.uk/write/documents/library/reports%20and%20research/bpa\\_uk\\_parking\\_sector\\_report\\_awweb.pdf](http://www.britishparking.co.uk/write/documents/library/reports%20and%20research/bpa_uk_parking_sector_report_awweb.pdf)



A growing trend in recent years has been for major Level 1s to remove services associated with non-compliant activity from their clientele. This departure from mainstream PRS was based on the belief held by the Level 1s that major blue-chip organisations and merchants would not work with companies involved in non-compliant activity. And the same beliefs are once again being applied by the Level 1s with regard to operator billing and the opportunity of enticing the very same merchants and blue-chip organisations.

Sections of the industry believe like-for-like comparisons between PRS and credit cards will potentially be avoided provided adult, competitions and digital content are extricated from PRS to ensure non-compliant activity does not prevent the widespread appeal of operator billing to blue-chip organisations and merchants. A possible remedy for this dilemma is PayforIt.

### **PayforIt**

PayforIt was expected to become the consumer-facing brand that presented operator billing as a viable alternative to existing payment mechanisms such as PSMS within PRS, but also as a possible contender for quasi-physical and physical goods. During 2014 it has become apparent that PayforIt's appeal is unlikely to extend beyond the PRS industry, inadvertently becoming sidelined as the de facto payment platform for traditional PRS.

### **Mobile operators**

Mobile operators have already commenced making significant strides to become competitive in the quasi-physical and physical goods and service space by agreeing to a reduced transaction fee of 9.9% for operator billing at the start of 2014. Toward the end of the year that figure is believed to have dropped further to around 7-8%. Mobile operators<sup>37</sup> have said that they will assess their transaction fee on a case-by-case basis, with a view to reducing the fee below 7% provided it is a volume-based proposition. Nevertheless, operator billing is unlikely to match the 1-3% of the debit and credit card providers.

Out-payment terms will also prove a considerable hurdle in attracting blue-chip organisations. Under the PRS Code of Practice, mobile operators cannot make an out-payment before 30 days, whereas merchants are accustomed to 3 day out-payments from credit and debit companies, for example, even as quickly as 24 hours in some instances.

## **9. The threat of competing payment platforms**

### **New players, established authorities**

New entrants into the PRS space, such as Google, view operator billing as a good alternative payment mechanism to credit or debit cards. The company is already experiencing significant revenues from app and in-app purchases in developing markets from the unbanked, and is starting to make significant revenues in the UK - taking a share of the £68.44 million (excl VAT) generated by operator billing (including PayforIt) in 2014.

Apple is believed to be exploring operator billing, but is likely to launch in developing markets and not in the UK where 99% of its iTunes accounts have credit or debit card details<sup>38</sup>. Nevertheless, the Apple effect could potentially educate mobile users about alternative payment platforms when ApplePay is launched in the UK. However, there is a fear that ApplePay could educate consumers about the merits of contactless payments, like mobile wallets and near-field communications (NFC), and not operator billing.

<sup>37</sup> Source: Industry research

<sup>38</sup> Source: Industry research



Credit and debit cards are already having a negative impact on PRS. For certain sectors, such as gambling, flirt and chat, and tarot and horoscopes, daily payments capped to £30 are seen as too restrictive, and has prompted the transition of heavy users from PRS onto credit cards. The latter has stolen a clear march on operator billing. At Mobile World Congress 2015 in Barcelona, innovative products and services predominantly identified as ideally suited to the frictionless payments of operator billing, such as parking, bike hire, toll road payments and so on, are being developed to accept card payments. The companies innovating in these sectors have not considered the option of operator billing.

At present, the opportunity for operator billing is being stifled by an abundant lack of promotion by the industry. The mobile operators will play a central role in establishing operator billing as a rival payment mechanism to debit and credit cards. But as mobile operators highlight, the issue they face at present is that operator billing is used by adult services, which they cannot promote to their customer base. However, when Google Play introduced operator billing, mobile operators distributed a promotion to all Android devices, and a similar initiative will occur with Microsoft and its respective device owners.

There have also been calls by premium rate service providers for mobile operators to explore enabling mobile withdrawals rather than just deposits, trying to bring the service in-line with existing e-wallet solutions<sup>39</sup>.

### 10. Consumer appeal of operator billing

Operator billing presents the PRS industry with an opportunity to evolve an already established and widely used payment mechanism into a projected multi billion pound industry.

Digital content and services paid for via PRS continues to appeal to 16.5 million users, as of the start of 2015. But the ability to convert the mobile device into a payment mechanism for physical goods and services is transformational and understandably has captured the attention of the PRS industry.

The potential of PRS is that all of the 48.6 million mobile users in the UK can adopt it to complete a transaction. And there are very encouraging signs emanating from PRS users with regard to the operator billing opportunity.

The consumer survey has revealed that PayPal is the preferred payment channel of PRS users for services, but second was operator billing, ahead of debit card and credit card. Convenience, simplicity and trust were the top three reasons PRS users would use a payment mechanic.

Fig 43: Preferred consumer payment channels

Debit card	4,089,000
Credit card	2,411,000
PayPal	6,500,000
Direct to your phone bill	4,301,000
Virtual currency	502,000
Pre-purchased credit	1,177,000
Other - please specify	270,000

Source: PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q.38. If you could pay for services via any payment channel, which would be your preferred choice? Base n=3,000.

<sup>39</sup> Source: Industry research



When the question specifically related to PRS as a payment mechanism one-third of PRS users claim to have no loyalty to a specific payment mechanism, however, one-quarter of PRS users claim the service is convenient, and from a trusted brand. Less than one-tenth of users said that PRS was the best way of accessing the information or entertainment they were after.

In fact, when specifically asked if PRS users would like to pay for “other transactions” using operator billing, the percentage more than doubled. In total 56% of respondents said they would be interested (17% of respondents) and potentially interested (39%). This would equate to 10.8 million PRS users.

**Fig 44: The potential appeal of operator billing**

Yes	3,318,000
Potentially	7,503,000
No	8,487,000

Source: PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q.40 Would you be interested in using your mobile phone to pay for other transactions that appear on your monthly mobile phone bill, or uses available credit from your pay-as-you-go account? Base n=2,877.

Once again, convenience is the prevailing reason for one-quarter of PRS users attracted to using the mobile phone to pay for transactions. One-tenth claimed to not like having to enter card details. Other reasons included an easy way to keep track of spend, and avoiding the risk of accruing debt with a credit card.

**Fig 45: What is appealing about using your mobile phone to pay for transactions?**

It's easy to keep track of how much I'm spending when paying by mobile	1,607,000
I don't trust other methods/don't want to enter my card details	902,000
It would be more hassle to enter my card details	1,886,000
It's easy and convenient	5,110,000
I prefer not to use a credit/debit card	1,099,000
If things go wrong, I am confident I can get redress	1,109,000
I don't have a 'one-click account' or credit card	715,000
I haven't considered it yet but it could be an option	2,291,000
I pay my mobile phone bill off each month, avoiding the risk of accruing debt with credit cards	1,285,000
Because it's a good way to pay discretely and/or anonymously	1,306,000

Source: PhonepayPlus quantitative consumer survey, December 2014-January 2015. Q.41. What is the appeal of using your mobile phone to pay for transactions? Base n=1,612.

Of the 42% of PRS users which do not find the prospect of operator billing appealing - which equates to 8.1 million people - cited reasons included a preference for other payment methods (17% of total PRS users), a trust of existing methods (15%), and a distrust of using the mobile phone to pay for transactions (12%).



## About mobile squared

mobile squared provides intelligence and insight on the mobile sector. We've been analysing the mobile space for two decades, so our expertise has been earned, not learned. Our instinctive ability to ask the right questions uncovers invaluable nuggets of insight, which we interpret to help shape truly effective strategy for our clients. Our experience is recognised by the industry - we sit on judging panels for the prestigious GSMA Awards, EMMA awards, and the MEFFYs.

For more information go to [www.mobilesquared.co.uk](http://www.mobilesquared.co.uk)



## About PhonepayPlus

PhonepayPlus is the UK's independent regulator of premium rate services (PRS).

Premium Rate Services (PRS) are the goods and services that you can buy by charging the cost to your phone bill or pre-pay account.

They include directory enquiries, voting on TV talent shows, donating to charity by text or downloading apps on your mobile phone.

Our regulation is open, fair, and robust, underpinned by a Code of Practice approved by Ofcom.

As the telecoms, internet and payments sectors continue to grow globally at an unprecedented rate, PhonepayPlus takes action to safeguard consumers and help cutting-edge providers of digital content and services to thrive.

Our vision is that anyone can use premium rate services with absolute confidence in a healthy and innovative market. Within our remit and expertise, we seek a more consistent approach to regulating micropayments that are like PRS.