

# RETHINK MUSIC

## **New Business Models in the Music Industry**

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Authored by the Global Entertainment and Music Business program  
Berklee College of Music – Valencia campus

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## **1. Background on Rethink Music**

Berklee College of Music is pleased to present this paper which provides an overview of the music industry in 2013, examines key current issues, and discusses the consumer's point of view about the consumption of music. The paper has been developed by the graduate music business program at Berklee's Valencia, Spain campus for release at the Rethink Music new business models workshop in April of 2013.

Rethink Music began in 2010 as the result of collaboration between Berklee, Midem, the Berkman Center for Internet and Society at Harvard University, and Harvard Business School. We hosted major conferences in Boston in the spring of 2011 and 2012, drawing over 600 people each year and attracting speakers ranging from the President of the RIAA to the founder of the Creative Commons movement. Separately, we hosted private working group meetings with Berkman in the fall of 2010, 2011, and 2012, which focused on policy issues such as the Global Repertoire Database and easing the licensing process.

This year, Rethink Music will travel globally and will host a number of events around the world. In January of 2013, we hosted the Rethink Music Innovation Summit, a private business models workshop at Midem in Cannes. We are following this event with a public version hosted at Berklee's Valencia campus and another private workshop at SONAR in Barcelona in June of 2013. In the fall of 2013, in conjunction with Instituto Empresa (IE Business School) in Madrid, we will host our first ever Music Venture Day in Berlin.

Our goal has always been to foster real discussion and innovative solutions for the music industry that will benefit all stakeholders, from creators to rights owners to distributors to consumers. We are hopeful that this paper will help frame the issues and provoke discussion during the Rethink Music Valencia workshop and beyond.

## **2. General Industry Overview**

The music industry in 2013 continues to adapt to the seemingly endless digital landscape and consumer consumption patterns. Innovation has widened the horizon of new opportunities for music creators and consumers alike, yet piracy's impact remains deeply felt across the industry. A great deal of consolidation has occurred across all sectors of the business in recent years, but newcomers continue to emerge with attractive value propositions, effectively contributing to the changing methods in which music is produced and consumed. To present a general overview of the current state of the music business, the industry will be discussed in its three major divisions: recording, publishing and live music.

### **Recorded Music**

After over a decade of decline, the recorded music industry is making strides towards recovery and revitalization. For the first time in thirteen years, the International Federation of the Phonographic Industry (IFPI) reported that trade revenue generated from global

recorded music industry experienced a positive annual increase by an estimated 0.3%, reaching \$16.5 billion<sup>1</sup> in 2012, thanks to the impressive recent growth of digital music sector. While this figure is far from the industry's peak annual revenues of \$36.9 billion in 2000,<sup>2</sup> innovation in the music marketplace has spurred a new segment of growth. At least eight of the top twenty markets are expected to see growth in the trade value of recorded music in the next year, including Australia, Brazil, Canada, India, Japan, Mexico, Norway and Sweden.<sup>3</sup> Frances Moore, chief executive of IFPI, expressed this year: "It is hard to remember a year for the recording industry that has begun with such a palpable buzz in the air. These are hard-won successes for an industry that has innovated, battled and transformed itself over a decade."

While global recorded music revenues have far to go in terms of reaching levels last seen in the early 2000's, the digital music sector has witnessed promising and growth in recent years. In 2012, digital music revenues increased 9% to an estimated \$5.6 billion, now accounting for a third of global music industry revenues.<sup>4</sup> Digital channels are increasingly becoming a major source of income for record labels and publishers in a number of markets such as Norway, Sweden, India and the US.<sup>5</sup> In the United Kingdom, digital revenues surpassed physical revenues for the first time in 2012, joining the United States, where 50.3% of total music sales were digital in 2011.<sup>6</sup> This impressive growth can be attributed to continued business model innovation in the music marketplace and the expansion of digital services on a global level. The leading licensed digital music platforms, including iTunes, Spotify, and Deezer, currently offer their services in over 185 countries combined, compared to just twenty countries two years ago.<sup>7</sup> Territories that previously lacked physical retailing infrastructures are now within reach of record labels thanks to the growth of digital music service offerings. Today, there are more than 500 licensed digital music services operating globally, offering over 30 million tracks to consumers.<sup>8</sup> Stu Bergen, Executive Vice President, International Head of Global Marketing of Warner Music Group expressed optimism brought forth by the global reach of digital services: "We have plenty to do and some amazing opportunities ahead of us. Until recently, the vast majority of our revenues came from a handful of countries. Today, digital channels mean we can monetise markets worldwide much more effectively."<sup>9</sup>

Download stores continue to account for the majority of sales in global digital revenues with roughly 70% of total revenues,<sup>10</sup> however the 40% revenue growth rate of streaming services makes streaming the fastest growing sector in the industry<sup>11</sup> and an important source of digital revenues. Subscription rates to digital music streaming services were

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<sup>1</sup> International Federation of Phonograph Industry, [Digital Music Report 2013](#)

<sup>2</sup> International Federation of Phonograph Industry, [Recording Industry World Sales 2000](#)

<sup>3</sup> International Federation of Phonograph Industry, [Digital Music Report 2013](#)

<sup>4</sup> *Ibid.*

<sup>5</sup> *Ibid.*

<sup>6</sup> Brian, Matt. "UK digital music downloads and streaming revenues overtake physical formats for the first time," *The Next Web*, 2012, <http://thenextweb.com/uk/2012/05/31/uk-digital-music-downloads-and-streaming-revenues-overtake-physical-formats-for-the-first-time/> (3 March 2013).

<sup>7</sup> Resnikoff, Paul. "Spotify Is In 20 Countries. Deezer is in 182," *Digital Music News*, 2013 <http://www.digitalmusicnews.com/permalink/2013/20130128countries> (3 March 2013).

<sup>8</sup> International Federation of Phonograph Industry, [Digital Music Report 2013](#)

<sup>9</sup> *Ibid.*

<sup>10</sup> *Ibid.*

<sup>11</sup> "Streaming music revenues up 40% globally in 2012," *BBC News*, 2012, <http://www.bbc.co.uk/news/entertainment-arts-19270362> (3 March 2013).

initially slow to take off, however the number of paying subscribers in 2012 grew to over 20 million globally, a 44% increase compared to 2011.<sup>12</sup> For the first time, overall revenues from subscription music services are believed to account for over 10% of digital revenues.<sup>13</sup> In Scandinavian countries, streaming services account for a bulk of digital revenues. “We do see a similar trend [for sales] across the Nordics, but primarily for Sweden and Norway, where the penetration for streaming services is very high,” Spotify spokeswoman Marine Elgrichi said.<sup>14</sup> Sweden, the birthplace of Pirate Bay and later streaming giant Spotify, has witnessed a positive impact on overall music sales<sup>15</sup> and a drastic decrease in piracy,<sup>16</sup> where legal streaming solutions are most prevalent. This confirms the widely held belief that the recorded music industry needs to create business models that resonate with consumers in addition to focusing on enforcement of copyright law.

While the increase in recent subscription rates are encouraging, they have yet to enable most music streaming platforms to operate as profitable businesses. The challenge of the “freemium” business model employed by leading streaming services is that paying rights holders when their content is streamed can be a burdensome task, particularly when free users greatly outnumber paying subscribers as they currently do. Pandora pays an estimated 50-60% of revenues for content acquisition,<sup>17</sup> while Spotify reportedly pays 70% for content acquisition alone,<sup>18</sup> leaving little room for taking care of other costs, and certainly not a profit. Even with revenues continuously increasing since 2010, Pandora and Spotify have experienced net losses<sup>19</sup> due to these costly operating expenses.

The major challenge subscription music services face today is the difficulty of attracting more paying subscribers to their platforms (Spotify reportedly converts 20% of its free users in to paid users).<sup>20</sup> If these digital music services are able to achieve substantive conversions, streaming could inevitably become a sustainable business model, breathing life back into the recorded music industry. Some services are embracing creative campaigns to help. In late 2012, streaming platform Rdio launched its Artists Program in an effort to reward artists directly \$10 for each new paying subscriber they refer to the service,<sup>21</sup> but the effectiveness of this concept is unclear and currently unique to Rdio. In a world where music services must compete with free, it is evident that streaming platforms must create added value for consumers in their paid offerings if they wish to increase subscription rates. The research presented at the end of this paper aims to evaluate current entertainment

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<sup>12</sup> International Federation of Phonograph Industry, Digital Music Report 2013

<sup>13</sup> *Ibid.*

<sup>14</sup> Billing, Sören. “Swedes prefer streaming to downloading,” *The Local*, 2013, <http://www.thelocal.se/46646/20130310/#.UXFME79kVFQ> (11 March 2013).

<sup>15</sup> Resnikoff, Paul. “Swedish Music Sales, 2012-2012...” *Digital Music News*, 2013 <http://www.digitalmusicnews.com/permalink/2013/20130204sweden> (11 March 2013).

<sup>16</sup> Clayton, Nick. “Piracy Falls, But Not All Musicians Are Happy,” *Tech Europe - The Wall Street Journal*, 2011, [http://blogs.wsj.com/tech-europe/2011/09/30/piracy-falls-but-not-all-musicians-are-happy/?mod=google\\_news\\_blog](http://blogs.wsj.com/tech-europe/2011/09/30/piracy-falls-but-not-all-musicians-are-happy/?mod=google_news_blog) (11 March 2013).

<sup>17</sup> Sisario, Ben. “After a Quarterly Gain, Pandora Warns of a Loss to Come,” *The New York Times*, December 5, 2012.

<sup>18</sup> Houghton, Bruce. “Spotify Asks Labels To Pay Less, Expand Free Mobile,” *hypebot*, 2013, <http://www.hypebot.com/hypebot/2013/02/spotify-asks-labels-to-pay-less-expand-free-mobile-report.html> (12 March 2013).

<sup>19</sup> Pierre, Carl. “Will Music Streaming Ever be a Sustainable Business Model?,” *InTheCapital*, 2012, <http://inthecapital.com/2012/09/09/will-music-streaming-ever-be-a-sustainable-business-model/> (12 March 2013).

<sup>20</sup> “Music Sales Up for First Time Since 1999, Piracy Down,” *TIME*, February 28, 2013.

<sup>21</sup> “The Rdio Artist Program,” *Rdio*, 2013, <http://www.rdio.com/artistprogram/> (12 March 2013).

consumption trends and consumer attitudes specifically towards digital music service offerings, in an effort to provide insight as to how the industry may provide more compelling music solutions to consumers.

## **Publishing**

The music publishing sector was also hit by the downturn in recorded music sales, but after the initial decline, publishers began diversifying revenue channels to encompass deals with mobile partners, app developers, streaming services, greeting cards, film, and other sources outside the traditional model.

As a result, compared to the recorded music sector, music publishers have fared better since piracy began to impact the industry over a decade ago. The major music companies (Universal, Sony, etc.) have publishing divisions accounting for roughly one third of total revenues, typically with much higher profit margins compared to the companies' overall business.<sup>22</sup> By nature of their business, publishers are inherently positioned to generate higher returns on their investments than a record label - they do not have to recoup large costs spent on developing, producing, marketing and distributing an artist's music, and their efforts are typically confined to marketing music in their catalogues to advertisers and broadcasters. Furthermore, while publishers experienced considerable losses in mechanical royalties from physical formats, U.S. publishers have witnessed growing revenues from statutory mechanicals from digital downloads. Even when iTunes, the industry's current largest online revenue source, moved to a variable pricing structure in 2009, publishers maintained relative stability thanks to fixed rates set by the Copyright Royalty Board. The same is mostly true across Europe, even with variable percentage rates for mechanicals.

As consumers drift farther away from physical formats, profits resulting from music publishing for a variety of uses in advertising and entertainment outside traditional deals are making the publishing sector of the larger industry more important than ever, especially within the new media realm. Universal Music Publishing recently inked an innovative deal with Full Screen and Maker Studios, two top YouTube Partner Channels accounting for over 4 billion views a month. The ground-breaking agreement enables video creators working with Full Screen and Maker Studios to legally use songs from the Universal Music Publishing catalogue as samples, soundtracks and covers, and even allows video creators to take part in advertising revenues as a result of those videos.<sup>23</sup> Universal Music Publishing in turn receives the benefit of a higher cost per impression rate from advertising revenues from their music circulating in videos from the two networks, as advertisers often pay a premium to place their content in videos distributed by Full Screen and Maker Studios, whose engaging videos reach valuable demographics.<sup>24</sup> The other two majors have yet to strike similar deals with video distribution networks, however it is likely they will consider doing so in the future as potential revenues are estimated to scale greatly with time.<sup>25</sup> The deal demonstrates the

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<sup>22</sup> Randall, David. "The One Bright Spot In The Music Business," *Forbes*, January 9, 2009,

<sup>23</sup> Van, Alan. "Universal Music Publishing Group Announces Partnership with Fullscreen And Maker Studios," *Maker Studios*, 2013, <http://www.makerstudios.com/company/news/universal-music-publishing-group-announces-partnership-with-fullscreen-and-maker-studios/> (14 March 2013).

<sup>24</sup> Christman, Ed and Pham, Alex. "Universal Music Publishing Inks Deals with Fullscreen, Maker Studios," *Billboard*, 2013, <http://www.billboard.com/biz/articles/news/1538590/universal-music-publishing-inks-deals-with-fullscreen-maker-studios> (14 March 2013).

<sup>25</sup> *Ibid.*

collaborative benefits that can be reached by tapping into popular multi-channel networks on an increasingly prominent medium in entertainment consumption.

## Live

Like the recorded music sector, wide scale consolidation has occurred in live music over the past few decades, leaving a few large players, most notably global leader Live Nation Entertainment. In recent years, Live Nation strengthened its position as the dominant force in the live business by pursuing a vertical integration strategy, acquiring leading ticketing company Ticketmaster and a number of smaller promotion companies, as well as operating roughly 100 notable live music venues around the world.

When the overall music industry's health began to suffer as result of piracy, the growth of the live music sector offset the damage to recorded music revenues. Live concert ticket sales tripled in value in the United States between 1999 and 2009, from \$1.5 billion to \$4.6 billion.<sup>26</sup> In addition to escalating costs resulting from increasingly elaborate live productions, music industry players have become more reliant on live revenues, causing concert ticket prices to significantly rise. In 2008, concert tickets reached peak prices at an average of \$67 in North America, compared to \$26 in 1996, translating to an increase four times greater than inflation.<sup>27</sup> Following the global economic decline in 2008 and lackluster concert sales, promoters lowered ticket prices for the next two years to adapt to changing consumer entertainment patterns. As a result, the live industry benefited from positive regrowth in ticket sales revenues as well as the volume of tickets sold, and promoters began pushing ticket prices up once again to an average of \$68.76 in 2012.<sup>28</sup> Concert industry trade publication Pollstar reported that in 2012 box office revenues for North America concerts totaled more than \$4.3 billion, with a 5% rise in ticket sales totaling 36.7 million sold, compared to 34.74 million sold in the previous year.

It is worth noting that the majority of North America's top 100 grossing tours in the last decade came from relatively older, established acts with a few decades of experience under their belt. Professional services consulting firm Deloitte looked at the highest grossing performing acts in the United States from 2000-2009 and found that 40% of the top twenty lead singers were 60 years old or older, 19% were in their 50's, 35% were in their 40s, and just 6% were in their 30s, while none of the lead singers were under 30 years old.<sup>29</sup> With the live business reliant on just a handful of aging touring acts capable of selling out large concert venues with ticket prices in the triple digits, it may be of some concern to the music industry that in future years newer acts will face the challenge of producing revenues to the same extent of exiting superstars and legacy artists. This is not to say newer acts are not capable of selling out large concerts and touring the globe (*looking at you, Justin Bieber*), but it is likely their active time in the spotlight will be less than artists have enjoyed in the

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<sup>26</sup> "What's working in music: Having a ball," *The Economist*, 2010, <http://www.economist.com/node/17199460> (13 March 2013).

<sup>27</sup> "Concert Ticket Prices Expected To Drop in 2011 After Sluggish 2010", *Billboard*, 2010, <http://www.billboard.com/biz/articles/news/touring/1196169/concert-ticket-prices-expected-to-drop-in-2011-after-sluggish-2010> (13 March 2013).

<sup>28</sup> "Pollstar's Top 200 North American Tours," *Pollstar*, January 7, 2013.

<sup>29</sup> "Keeping the life in live: A&R diversifies," *Deloitte*, 2011, [http://www.deloitte.com/view/en\\_GX/global/industries/technology-media-telecommunications/tmt-predictions-2011/media-2011/d97f8f036907d210VgnVCM2000001b56f00aRCRD.htm](http://www.deloitte.com/view/en_GX/global/industries/technology-media-telecommunications/tmt-predictions-2011/media-2011/d97f8f036907d210VgnVCM2000001b56f00aRCRD.htm) (14 March 2013).

past, as the choices consumers have when it comes to music and entertainment in general continue to exponentially grow and attention spans shrink.

While the concept itself is not new, music festivals have exploded in popularity on a global scale in recent years. As ticket prices for solo concerts continue to escalate, many consumers are willing to spend more in order to have access to a large roster of acts spread over a few days and to immerse themselves in the “festival experience”. Burning Man and Coachella (USA), Big Day Out (Sydney and Melbourne, Australia), Leeds Festival (England), T in the Park (Scotland) and Rock Werchter (Belgium), are speculated to attract between 50,000 and 100,000 music fans each day of operation, while Roskilde (Denmark) and Glastonbury (England) are often estimated to attract between 100,000 and 140,000 attendees daily. Many festivals have expanded outside of their home region, such as Lollapalooza and Sónar (Spain). A slim version of Lollapalooza debuted in Santiago, Chile in 2011 and in São Paulo, Brazil the following year. Already acclaimed as a magnet for the world’s forward thinking electronic and experimental talent in its hometown of Barcelona, Sónar has been focused on international expansion in recent years, hosting frequent events around the world. The festival made its Canadian and American debut tour during last fall’s Sónar On Tour, and will be celebrating its 20th year anniversary with an international run through Reykjavik, Tokyo, São Paulo, Cape Town and culminating in Barcelona. Festivals have become a cultural staple of not only summer but year round entertainment worldwide.

In the United States, major festivals like Coachella, Sasquatch, Bonnaroo and Lollapalooza are witnessing record attendance numbers, often selling out tickets before lineups are announced. Last year, Coachella added a second weekend to its lineup, pulling in a record breaking \$47 million gross. Concurrently with the rise in popularity of music festivals, the number of new festivals debuting every year in the United States is raising concerns about market oversaturation as has occurred over the past few years in the United Kingdom. There, festival-goers had too many choices to choose from with similar lineups and “so-so” appeal, as promoters became occupied with remaining profitable and failed to meet consumers’ expectations. Amidst a shaky economic climate, the UK festival market suffered drastic consequences last year with low attendance numbers and many festivals even closing their doors. (At least a dozen festivals in the UK either went out of business or decided to sit out last year, including popular ones such as Sonisphere UK and The Big Chill, as well as GoGo Festival, LadyRock Festival, Pride House, Trowbridge Festival, Kelvedon Free Music Festival, Harvest at Jimmy’s, & Titanic Lockdown.<sup>30</sup>) “It’s basic economics,” says Dean James, chief executive of Mama Group, a large UK multi-venue and festival operator. “There’s over-supply in the market as anyone with a field thought they could make easy money from a festival, and there’s less demand because of economic conditions and alternative events.”<sup>31</sup>

Amidst troubles across the pond, some promoters believe the festival market in the United States is just getting started. Bob Roux, co-chairman of Live Nation’s North America concerts (which produced 18 festivals in the states last year, including sold out events

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<sup>30</sup> Houghton, Bruce. “The Growing List of Cancelled UK Festivals,” *hypebot*, 2012, <http://www.hypebot.com/hypebot/2012/05/the-growing-list-of-cancelled-uk-festivals.html#sthash.BliG4vNH.dpuf> (12 April 2013).

<sup>31</sup> Spanier, Gideon. “Festivals look beyond music to woo punters in tough times,” *London Evening Standard*, July 25 2012.



Sasquatch, Jay Z's Made In America, and Music Midtown), has expressed optimism for festival development in the States: "Fans are waiting for something in their hometown. You're basically in the very beginning stages of what this is going to look like here in America for the next decade."<sup>32</sup> Other promoters, like Jordan Wolowitz, a partner with Founders Entertainment and promoter of last year's sold out Governor's Ball, warns of too much growth too fast: "It can get to a point where there's over-saturation in the festival market... If too many festivals spring up in the same market, it's a problem."<sup>33</sup>

As more and more festivals begin to sprout up, a key differentiation factor for promoters could be organizing niche festivals and festivals with a multi-dimensional creative emphasis, rather than just music. While oversaturation of the United States' major festival market is likely approaching, there is room for smaller and mid-level niche festivals to develop and grow, such as XOXO in Portland, an arts and technology festival "celebrating disruptive creativity"<sup>34</sup> (funded by a Kickstarter project led by former Kickstarter CTO Andy Baio), Decibel International Festival in Seattle focused on "Electronic Music Performance, Visual Art and New Media", and Northside Festival in Brooklyn, celebrating emerging "music, film, food, ideas and entrepreneurship."<sup>35</sup> Compelling and unique offers will continue to be key for differentiation amongst a growing festival market.

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<sup>32</sup> Knopper, Steve. "Music Festivals Enjoy Record Expansion in 2012," *Rolling Stone*, April 12 2012.

<sup>33</sup> *Ibid.*

<sup>34</sup> "XOXO" XOXO, 2013, <http://2013.xoxofest.com/> (12 April 2013).

<sup>35</sup> "Brooklyn's Northside Festival Unveils 2<sup>nd</sup> Annual Event," *Indiewire*, 2011, [http://www.indiewire.com/article/brooklyns\\_northside\\_festival\\_announces\\_2011\\_lineup](http://www.indiewire.com/article/brooklyns_northside_festival_announces_2011_lineup) (12 April 2013).

## Case Study: The EDM Movement

During the past five years, a seemingly desperate “arms race” has occurred, with many large U.S. conglomerates chasing the ever-growing Electronic Dance Music (EDM) market. This “gold-rush” mentality reached new heights with the recent announcement of the first ever mass market EDM movie from 20th Century Fox and EDM producer mogul Diplo,<sup>36</sup> and the acquisition of Beatport, the biggest online music store and community for DJs, by SFX Entertainment for approximately \$50 million.<sup>37</sup> The SFX move is just another step in the \$1 billion investment plan announced some time ago by SFX’s leader Robert Sillerman, who aims to extend his empire into the EDM industry, which is now worth over \$4 billion per annum<sup>38</sup> and showing huge increases annually in ticket sales and radio airplay. Last year, Live Nation bought Los Angeles-based electronic dance music promoter Hard Events, just a few months after their acquisition of another big popular EDM event organizer, U.K.-based Cream Holdings, promoter of the Creamfields festivals.<sup>39</sup> It is evident that many perceive the growing force of the EDM movement as a road to escape from the darkest era of the music business.

Not surprisingly, with the music business shifting toward live events and festivals, well-known corporate players are seeking a slice of the newly appetising dance music pie. A recent chart ranking the most powerful people in the EDM industry includes Joel Zimmerman from William Morris Endeavour’s new electronic division, James Burton from Live Nation, Robert Sillerman from SFX Entertainment, and Pete Tong from UK BBC Radio1, with Pasquale Rotella, head of Insomniac, operator of the Electric Daisy Carnival and the EDMbiz conference in Las Vegas, at number one.<sup>40</sup>

Further, total EDM festival capacity in the United States has grown by over 45% since 2007,<sup>41</sup> and Europe is also growing via top-line events like Tomorrowland and Time Warp. Emerging events, like the Exit festival in Serbia and BPM in Mexico are gaining strong momentum as well as established dance festivals such as Ultra and Sónar, which now take their festival around the globe, reaching the US, European, South American and Asian markets. Some promoters are now seeking new ways to match the “underground” side of EDM with more traditional pop-music culture; Live Nation Spain launched its Ibiza 123 Rocktronic festival in 2012, pairing pop-rock veteran Lenny Kravitz Chilean with minimal-house DJ Luciano.

As EDM moves into the mainstream, corporate sponsorships, mergers, brand alliances and partnerships have naturally followed, and DJs have suddenly become the new rock-stars - or as Forbes has called them, “Electronic Cash Kings”. Forbes’ chart of annual EDM earnings is lead by Tiesto with \$22 million earned last year, pulling up to \$250,000 per gig, and

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<sup>36</sup> Battan, Carrie. “Diplo Executive Producing Movie About EDM for Fox,” Pitchfork, 2013, <http://pitchfork.com/news/50299-diplo-executive-producing-movie-about-edm-for-fox/> (12 April 2013).

<sup>37</sup> Sisario, Ben. “SFX Entertainment Buys Electronic Dance Music Site,” *The New York Times*, February 27, 2013.

<sup>38</sup> IMS BUSINESS REPORT 2012

<sup>39</sup> Roberts, Randall. “Live Nation’s EDM chief James Barton talk the music’s US future,” *Los Angeles Times*, 2012,

<sup>40</sup> “The 50 Most Powerful People In EDM 2013,” *In The Mix*, 2013, [http://www.inthemix.com/features/54908/The\\_50\\_Most\\_Powerful\\_People\\_In\\_EDM\\_2013?page=8](http://www.inthemix.com/features/54908/The_50_Most_Powerful_People_In_EDM_2013?page=8) (15 April 2013).

<sup>41</sup> IMS BUSINESS REPORT 2012

Skrillex, Swedish House Mafia and David Guetta, respectively at the second, third and fourth spots, earning between \$13-15 million per year.<sup>42</sup>

The majority of dance music festivals now rely on standard lineups of just few big EDM acts, something that has been seen as a detraction from the purity of electronic music itself. For example, Carl Cox, Tiesto and Guetta represent different audiences and genres within EDM, but are often booked as headliners for EDM festivals while many hard-core fans feel these artists should not share the same stage. This “underground” vs “mainstream” battle has continued through wars of words on Twitter and other social media between DJs and producers, with each side questioning the other’s authenticity,<sup>43</sup> and is reminiscent of the 90’s East Coast/West Coast hip-hop rivalry. The recent news of Paris Hilton behind the decks and Justin Bieber announcing a DJ-residency in an Ibiza club for the summer season only fuels the intensity of the debate as some believe EDM is becoming just another pop-trend bubble ready to burst.

As we have seen since the early 70s, the electronic music industry goes arm in arm with technological progress. This factor, along with the boom of online Do-It-Yourself platforms, has made the life of music aficionados simpler than ever, closing the gap between the consumer and the professional, and giving the feel that anyone can be the next big DJ or producer. Equipment to make records is considerably less expensive than even ten years ago; Skrillex has reported that he has made Grammy award winning tracks only with software on his laptop.<sup>44</sup>

Thousands of online courses, specialized schools and conferences are adding to the booming industry at every level, redefining and expanding the concept of music education. Of particular interest are those education-oriented tours around major colleges in the US, like Richie Hawtin’s “CNTRL: Beyond EDM”, in which Hawthins and other notable DJs hosted sessions on technology and music production, allowing attendees to interact and learn from touring EDM professionals.

Perhaps the biggest issue in EDM music today is the lack of professionalism and awareness of legal procedures that part of this culture seems reluctant to fully embrace. As reported by PRS for Music’s director of membership and rights Mark Lawrence at MIDEM 2013, EDM represents up to 20% of UK BBC Radio 1 entire programme (one of the most famous radio shows worldwide), but only only 50% of those songs get remuneration rights (royalties) because of the lack of metadata or mistakes in the playlist sheets. Moreover, the lack of complete and detailed set lists results in another potential huge loss for authors and publishers of those songs; in the case of one big electronic music festival, it has been speculated that up to 100,000€ in royalties fail to find the right pockets.<sup>45</sup>

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<sup>42</sup> Greenburg, Zack O'Malley. “The World’s Highest-Paid DHs 2012,” *Forbes*, 2012, <http://www.forbes.com/pictures/eeel45jfeg/the-worlds-ten-top-earning-djs/> (12 April 2013).

<sup>43</sup> Walker, Peter. “EDM Wars -Storm in a bassbin or impending industry implosion?” *Independent Arts Blogs*, 2012, <http://blogs.independent.co.uk/2012/07/11/edm-wars-%E2%80%93-storm-in-a-bassbin-or-impending-industry-implosion/> (13 April 2013).

<sup>44</sup> “When Richie Hawtin Met Skrillex,” *Mixmag*, 2012, <http://www.mixmag.net/words/features/richie-hawtin-interviews-skrillex> (10 April 2013).

<sup>45</sup> “PRS for Music launches electronic music initiative, Amplify,” *PRS for Music*, 2013, <http://www.prsformusic.com/aboutus/press/latestpressreleases/Pages/PRSforMusicLauncheselectronicmusicinitiativeAmplify.aspx> (14 April 2013).

Further, with much of electronic music born via the creation of new works from existing works, the situation becomes highly complicated when considering copyright law and “what is a derivative work”. In countries enforcing moral rights, the question of whether mash-ups and remixes violate an author’s right to the integrity of his work remains mostly unexplored. In addition, the image of modern “laptops DJs” have led some collecting societies, such as German collection society GEMA, to introduce license fees imposed on DJs who play and store songs digitally, generating criticism of older institutions as not ready to cope with this fast-moving industry. Many German DJs have protested against the new license fee imposed by GEMA, claiming the fees at €0.13 euros (0.17¢) per title or €125 (\$163) for a collection of 1,000 tracks and an additional 500 tracks for €50 (\$65) are too high, pointing out that a typical DJ in Germany (storing some 15,000 digital tracks) would have to pay GEMA about 1,500 Euros (about \$2,000) each year.<sup>46</sup>

In the end, legal issues and missed opportunities can be seen as further incentives to induce new players into the EDM genre, as a perfect place to find and experiment new solutions for the entire music industry. On the other hand, some legacy promoters already feel things are spiraling out of control. Ricardo Urgell for instance, Pacha Ibiza’s long time patriarch, has expressed his frustration with paying escalating performance fees for DJs to play less and less time. Dance producer Deadmau5’s definition of EDM as “minimal effort for maximal profit”<sup>47</sup> couldn’t be more accurate, and is one reason why it is so controversial, so challenging, so unpredictable, and yet so attractive.

### 3. Current Issues

Based on the discussions arising from the Rethink Music Innovation Summit at MIDEM 2013 as well as exchange within our team and other industry executives, we have identified six key current issues to be described in this second half of the paper.

#### The Value of Music

The most common topic arising from discussions about today’s music industry is the value of music in the digital age. The concept of value is most traditionally perceived as a measurement of the benefit an economic actor can gain in exchange for an object or service. With a perspective limited to strictly to economic benefit, one can contend the value of music has drastically declined. At \$16.5 billion, current total recorded industry revenues are far from the heyday of the late nineties, when they clocked in at roughly \$38 billion. Some claim that the value of music is close to if not at zero, as the majority of music consumers are accustomed to free access, whenever they want, through an expanding number of channels, including legal platforms such as traditional radio, YouTube, Pandora and Spotify, or via torrents, peer-to-peer networks and file sharing platforms. A recent study by Nielsen found that portals available to music consumers for free are the most accessed media for music

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<sup>46</sup> Spahr, Wolfgang. “German DJs Protest GEMA’s Proposed Tax on Digital Music Collections,” *Billboard*, 2013. <http://www.billboard.com/biz/articles/news/digital-and-mobile/1556724/german-djs-protest-gemas-proposed-tax-on-digital-music> (14 April 2013).

<sup>47</sup> “Minimal effort for maximal profit”: Deadmau5 talks EDM, Hookers and More,” *FACT Magazine*, 2012, <http://www.factmag.com/2012/11/26/deadmau5-on-edm-minimal-effort-for-maximal-profit/> (11 April 2013).

discovery: 48% of all people say traditional radio is the dominant way they discover music, with 64% of teens reporting they use YouTube to listen to music more than any other source.<sup>48</sup>

A broad perspective takes into account the many types of “currency” that have evolved in the digital paradigm to encompass not just money, but amounts of time, attention, personal data and social participation in music experiences. Music consumers appear to be listening and interacting with music more than ever; the total volume of music purchases reached an all-time high in 2012, totaling over 1.65 billion units, up 3.1% from the previous year thanks to growing consumption of digital formats (digital albums were up 14% and digital tracks up 5%).<sup>49</sup> One study of 500 music consumers found that 45% listen to music over 10 hours a week, while 75% of listeners belong to a social listening site (Pandora at number one, Spotify at number two, and Last.fm number three).<sup>50</sup> Youth in particular are spending more and more time with music - a study of America’s youth found that kids aged 8 to 18 listened to music 2 hours and 31 minutes a day in 2010 on average, compared to 1 hour and 48 minutes a day in 1999.<sup>51</sup> Even when consumers are not paying for their music experiences, they are often giving valuable assets such as personal data, allowing platforms to deliver targeted ads.

Considering these factors, the conversation around music should not necessarily be concerned with the question of whether or not consumers value music in today’s society, because there are many types of currency consumers trade in order to obtain value from music products and services. With this perspective, the value of music for consumers is clearly evident. As in all industries, however, value alone does not guarantee revenue. The question industry stakeholders should ask themselves is how to increase willingness to pay for their offers, because when free offers are perceived to offer the same value of paid offers, willingness to pay is greatly reduced.

Tellingly, a recent study by Nielsen of over 4,000 music consumers indicates their willingness to pay would significantly increase if the industry offered a more engaging set of products and experiences than what is currently available. “Fans want more,” said Barbara Zack, Chief Analytics Officer at Nielsen Entertainment Measurement. “There is an unmet need there. There is a desire to engage at a different level than what they have.”<sup>52</sup> The study concludes that exclusive music merchandise, such as signed posters, limited edition t-shirts, handwritten lyrics, and even direct personal experiences such as a 30-minute Skype conversation with an artist could generate a potential \$450 million to \$2.6 billion in annual incremental revenue.<sup>53</sup> The compelling part about the findings is that exclusive content

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<sup>48</sup> “Music Discovery Still Dominated by Radio, Says Nielsen Music 360 Report,” *Nielsen*, 2012, <http://www.nielsen.com/us/en/press-room/2012/music-discovery-still-dominated-by-radio--says-nielsen-music-360.html> (12 February 2013).

<sup>49</sup> “The Nielsen Company & Billboard’s 2012 Music Industry Report,” *Business Insider*, 2013, <http://www.businesswire.com/news/home/20130104005149/en/Nielsen-Company-Billboard%E2%80%99s-2012-Music-Industry-Report> (10 February 2013).

<sup>50</sup> Monks, Sarah. “Social Sound Bytes: Music Listening & Sharing,” *Lab42*, 2012, <http://blog.lab42.com/social-music-sound-bytes> (14 February 2013).

<sup>51</sup> The Henry J. Kaiser Family Foundation: *Generatio M<sup>2</sup> - Media in the Lives of 8- to 18-Year-Olds* (2010)

<sup>52</sup> Peoples, Glenn. “Nielsen Study: Music Industry Could Add \$450 Million to \$2.6 Billion in Incremental Revenue With Premium Content,” *Billboard*, March 12, 2013.

<sup>53</sup> *Ibid.*

offers as mentioned above are attractive not only to consumers Nielsen calls “Aficionados”, (the most active music buyers (53%)), but even to a sizable percentage of what Nielsen calls “Ambivalent consumers” (22%).<sup>54</sup> Offering exclusive music content and related goods is not a revolutionary idea, as independent musicians have found direct-to-fan strategies offering expanded music offers via crowdfunding platforms such as PledgeMusic and Kickstarter to be extremely successful. (As of this writing, Kickstarter alone has successfully funded 10,797 music projects, with roughly 10% raising under \$1,000, 72% raising \$1,000 to \$9,999 and the remainder of projects raising over \$10,000).<sup>55</sup> Considering their sizable ownership and considerable influence in producing and marketing the work of their artists, major labels stand to greatly benefit from developing their own mixed bundle offers and exclusive offers that could satisfy music consumers’ increasing demands for a better music experience.

### **Balance Between Majors / Independents**

With three major labels controlling almost 90% of the global recorded music market in 2013,<sup>56</sup> the music business is often labeled an oligopoly. Universal, Sony, and Warner are not only responsible for the majority of the industry’s recorded music revenues, but wield substantial power as gatekeepers to mass media such as television, radio and other distribution channels through equity stakes in powerful media conglomerates and music startups. Independent labels are often subject to the terms established by the majors with distribution outlets, if not considerably dependent on them for distribution; according to a recent report by the Consumer Federation of America and Public Knowledge, independent labels now rely on the majors for the distribution of over 60% of their content.<sup>57</sup>

New services find themselves in a weak position when negotiating licensing deals with the majors, as failure to contract with one of the three powers would inflict gaping holes in a music offer that would not go unnoticed by consumers. Digital services often find themselves in a tight bind, often settling by granting the majors large upfront payments, escalating licensing rates, stakes in equity, and other various demands.<sup>58</sup>

Despite their overwhelming influence in the production and distribution of recorded music, major labels are balanced out, at least in the U.S., by the collective strength of the independents, who are estimated to claim roughly a third of U.S. album sales in 2012, more than any single major label.<sup>59</sup> In many international markets there are successful standout independent labels such as XL Recordings (UK) and Avex (Japan), which compete with the majors to a certain degree. Further, independents are recognized for influential contributions to entertainment culture, such as through their prominent successes at the

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<sup>54</sup> *Ibid.*

<sup>55</sup> “Kickstarter Stats,” *Kickstarter*, 2013, <http://www.kickstarter.com/help/stats> (19 March 2013).

<sup>56</sup> “The Nielsen Company & Billboard’s 2012 Music Industry Report,” *Business Wire*, 2013, <http://www.businesswire.com/news/home/20130104005149/en/Nielsen-Company-Billboard’s-2012-Music-Industry-Report> (17 March 2013).

<sup>57</sup> Resnikoff, Paul. “Report: Indie Labels Are Now Heavily Dependent on Major Label Distribution,” *Digital Music News*, 2012, <http://www.digitalmusicnews.com/permalink/2012/120615indies> (17 March 2013).

<sup>58</sup> Robertson, Michael. “Why Spotify can never be profitable: The secret demands of record labels,” *Gigaom*, 2011, <http://gigaom.com/2011/12/11/why-spotify-can-never-be-profitable-the-secret-demands-of-record-labels/> (17 March 2013).

<sup>59</sup> “Indie Label U.S. Sales Market Share Grows to 32.6 Percent; Indies Remain #1 Sales Sector,” *American Association of Independent Music*, 2013, <http://a2im.org/2013/01/07/indie-label-u-s-sales-market-share-grows-to-32-6-indies-remain-1-sales-sector/> (18 March 2013).

music industry's most esteemed awards night, the Grammys. At the 2013 Grammys, independent labels and artists were recognized with 50% of all nominations for the third consecutive year in a row, winning 36 of 79 non-producer awards, including Best Album awards in 18 genres and the Academy's most prestigious award, Album of the Year, for Mumford and Sons.<sup>60</sup>

The rise of the independents is also noticeable in their recent presence in top slots of the Billboard's Hot 100 chart. For the first time in nearly two decades and the only second time ever in history,<sup>61</sup> independent artist duo Macklemore and Ryan Lewis claimed the number one spot on America's defining singles chart with their alternative bargain-hunting hit "Thrift Shop" earlier this year. Shortly after, "Harlem Shake", the bass-thumping jam that inspired a worldwide Internet meme hit the top of the chart after the inclusion of YouTube streaming data in the chart's methodology. Billboard was in discussions about adding YouTube to the Hot 100 formula for almost two years, but after the song gained a worldwide audience with rapid speed after the meme began, Billboard updated the chart's methodology immediately.<sup>62</sup> This modification demonstrates the changing notions of what it takes to have a hit, acknowledging the reality that artists can find success without the assistance of a major label if they manage to produce and distribute a consumer hit.

Many new artists and small labels find joining distribution and aggregation networks such as CD Baby and TuneCore beneficial in placing their music in the world's leading digital music platforms such as iTunes, Spotify, and Amazon MP3. Other independents forgo do-it-yourself (DIY) distribution, due to the weak bargaining power accompanying the individual negotiation rights, in favor of a collective bargaining strategy. Many digital music services wishing to license a breadth of independent repertoire turn to the Merlin Network, the largest global rights agency for independents. This non-profit organization represents over 12,000 independent labels, aggregators and right representatives,<sup>63</sup> including world leaders XL Recordings, Rough Trade, Warp Records, Beggars Group and Sub Pop, viewing itself as the fourth major, seeking to "represent its members in new media deals that can't be easily negotiated locally or individually or are not covered adequately by existing arrangements."<sup>64</sup> The impressive scope of rights represented is the reason why Merlin Network claims it is the "most efficient means for digital music services to license repertoire from the largest and most compelling basket of independent rights in the world."

Stepping back and looking at the whole picture, the majors appear to be in control of the industry as always, but there's never been a better time to be an independent. With large and often rigid organizational structures, majors struggle hardest to adapt to the changing playing field of the music business. Their marketing and distribution muscles are undeniably larger than any independent's, and many artists continue to sign with them for that reason,

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<sup>60</sup> Houghton, Bruce. "Independents Continue Grammy Winning Streak," *hypebot*, 2013, <http://www.hypebot.com/hypebot/2013/02/independents-continue-grammy-winning-streak.html> (17 March 2013).

<sup>61</sup> Feeney, Nolan. "Macklemore's 'Thrift Shop' Is First Indie Hit to Top Charts in Nearly Two Decades," *TIME*, 2013, <http://newsfeed.time.com/2013/01/25/macklemores-thrift-shop-is-first-indie-hit-to-top-charts-in-nearly-two-decades/> (17 March 2013).

<sup>62</sup> Sisario, Ben. "What's Billboard's No. 1? Now YouTube Has a Say," *The New York Times*, February 21, 2013.

<sup>63</sup> "Merlin: Global Rights Body for Independent Music Grows to 8% Share of US Market," *Merlin Network*, 2007, <http://www.merlinnetwork.org/download.php?type=file&id=f1226665186> (19 March 2013).

<sup>64</sup> "Welcome To Merlin," *Merlin Network*, 2013, <http://www.merlinnetwork.org/home/> (19 March 2013).

which may very well be appropriate considering an act's genre and ambitions. On the other hand, thanks to technological improvements and the Internet, independents have all the tools enabling them to produce, market, and distribute professional sounding and looking content, giving artists the opportunity to ignite their own careers from their bedroom. Considering the drastically varying needs of creators, one can reach the reasonable conclusion that there is a place and purpose for entities of all sizes in the industry.

## **Copyright Law / Licensing**

Copyright law serves as the backbone of the recorded music industry, as it grants authors certain exclusive rights to their creative works for a period of time. The idea of copyright was conceived in the early eighteenth century as a mechanism to control the production of printed materials. In the early years of the music industry, copyright law was leveraged to protect the exclusive right of authors to copy their works, such as sheet music, and later, sound recordings. Copyright law allows authors or owners of creative content to exploit their assets as they choose, and enables the music industry to profit from its endeavors.

In today's digital age, where copies are so easily generated, many are questioning a copy-based system of rights and argue that perhaps a "use-based" system of rights might be more appropriate. Further, music in 2013 is a global commodity, but there is a lack of both a detailed global copyright system (the Berne Convention offers some out-of-country protection for creative works but licensing regimes are country-by-country), as well as a centralized, authoritative database identifying musical works and the owners of the rights associated with these works. This presents a problem for music industry stakeholders and anyone wishing to license musical works or otherwise do business with the industry, as all parties would benefit from a streamlined identification and licensing regime. As it stands today, it can be an arduous and frustrating undertaking to identify rights owners of a certain musical work, sometimes without fruition or certainty that the information obtained is correct.

Change to this process may be around the corner with the development of the Global Repertoire Database (GRD), whose stated mission is to provide single, comprehensive, and authoritative representation of the global ownership and control of musical works. The creation of the GRD is spearheaded by a collaborative international effort of the Global Repertoire Database Working Group (GRD WG) formed in late 2009, led by representatives from the following 14 organizations:

- ECSA (European Composer and Songwriter Alliance)
- ICMP (International Confederation of Music Publishers)
- CISAC (International Confederation of Societies of Authors and Composers)
- Sony/ATV Music Publishing/EMI Music Publishing
- Universal Music Publishing
- Warner/Chappell Music
- APRA (Australasian Performing Right Association)
- GEMA (Gesellschaft Für Musikalische Aufführungs- und Mechanische Vervielfältigungsrechte)
- PRS for Music
- SACEM (Société des Auteurs, Compositeurs et Editeurs de musique)
- STIM (Sveriges Tonsättares Internationella Musikbyrå)
- Apple



After publishing a Recommendations Document naming Deloitte as the database's project manager and the International Copyright Enterprise (ICE) as its technology solution,<sup>65</sup> the GRD WG initiated the first of five development phases in October 2012, expecting to deliver the database by 2015.<sup>66</sup> Over 100 individuals from almost thirty companies worldwide are reported to be involved in completing this work.<sup>67</sup> The GRD's goal of providing a single, authoritative database listing all global musical works and who controls the rights to these works and/or their administration is the most ambitious, complex endeavor the music industry has ever set out to achieve. In theory, the GRD would allow people to do business much faster, as Thimo Prziklang of GEMA noted at the GRD conference during MIDEM 2013: "The world repertoire of music will be there in its final state. It will be one place to go to find out about mechanicals and sync rights."<sup>68</sup> The GRD WG has some challenging issues to deal with before the completion of the GRD, including sorting out conflicting data from publishers, collecting societies, and other sources, as well as financing, governance, and data correction. Nevertheless, the parties involved appear to be optimistic about the progress of the GRD.

While establishing an authoritative database of the ownership of musical works would be an impressive feat for the music industry, the industry seems to be also struggling in finding a balance between licensing content at rates which new services can afford to pay and maintaining value in their rights. Even though digital music services have been heralded by many as the hope of the music industry, they often face severe costs in licensing content, one reason why many eventually fail. Startups often find themselves under the mercy of the three major labels since a failure to obtain licenses from all three would translate to an uncompetitive offer in the marketplace. To make things even tougher, startups must manage to strike deals with independent labels as well to make their offer competitive with existing services. "The most truly successful have one thing in common (be they iTunes or Spotify on the legal side of the fence, or BitTorrent or Pirate Bay on the other side); they offer a truly comprehensive repertoire from all labels — major and independent — to an ever-increasing and loyal client base," says Charles Caldas, CEO of Merlin. For startup services "looking to attract the digitally active, early adopters (the key demographic you need to build hype so that you may ultimately reach a broader market), you need to recognize that Arcade Fire, Grizzly Bear and the National are more likely to be at the top of the search lists, not Gaga or Maroon 5."<sup>69</sup>

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<sup>65</sup> "Background to the GRD," *Global Repertoire Database*, 2013, <http://www.globalrepertoiredatabase.com/index.php/background-to-the-grd> (19 March 2013).

<sup>66</sup> Pakinikis, Tom. "Global Repertoire Database 'first release' now scheduled for 2015," *Music Week*, January 28, 2013.

<sup>67</sup> "Global Repertoire Database makes strong progress with plans for 2013 well underway," *PRS for Music*, 2013, <http://www.prsformusic.com/aboutus/press/latestpressreleases/Pages/GlobalRepertoireDatabasemakesstrongprogresswithplansfor2013wellunderway.aspx> (19 March 2013).

<sup>68</sup> Skates, Sarah. "Global Repertoire Database On Track for 2015," *MusicRow*, 2013, <http://www.musicrow.com/2013/01/global-repertoire-database-on-track-for-2015/> (19 March 2013).

<sup>69</sup> Caldas, Charles. "Why do so many digital music services fail?" *Gigaom*, 2012, <http://gigaom.com/2012/03/17/why-do-so-many-digital-music-services-fail/> (21 March 2013).

The United States' leading Internet radio service, Pandora, claims it pays out 50% of its revenues towards music licensing fees,<sup>70</sup> leaving it struggling to pay its bills.<sup>71</sup> Spotify, considered by many to be the most promising streaming service, pays out 70% of revenues in licensing costs<sup>72</sup> and has yet to emerge from the red, posting a reported \$37.5 million net loss in 2010 and a \$59 million net loss in 2011<sup>73</sup> (2012 numbers have not been released). While Spotify CEO Daniel Ek recently stated he believes his service's freemium business model is sound,<sup>74</sup> the world's most widely used streaming service could experience serious difficulties if it fails to improve its 20% conversion rate of free to paid users.

These problems faced by new startups in the digital music space to license their services reflect the often wary approach major labels have in dealing with newcomers wishing to do business. Starting with the introduction of Napster, change in the digital sphere has generally been regarded by major labels with great caution. It now seems that most are now recognizing the opportunities to generate new revenue streams through new outside partners under certain parameters.

Some music services work around huge licensing costs by taking advantage of open API initiatives or piggybacking on existing services' licenses through an API. Music-related APIs (application software interfaces), allow new services to build on the host's existing proprietary technology and licensed repertoire to access a plethora of music-related data, as long as they follow certain parameters specified by the host of the API. Rdio, Spotify, The Echo Nest, Soundcloud and Deezer are just a few of many well-known music services who now offer their own APIs to developers available for use under specific conditions. Some creative uses of music APIs include Richseam ([www.richseam.com](http://www.richseam.com)) and Tastebuds ([www.tastebuds.fm](http://www.tastebuds.fm)). Using a combination of data from the Songkick, The Echo Nest, DBpedia, Last.fm and other APIs, Richseam enables the discovery of music through collaborations and connections between artists of interest. Tastebuds utilizes the Last.fm, Music Brainz, and Yahoo Query Language APIs in order to deliver a music-orientated dating service.

Also, in late 2011, The Echo Nest announced a first of its kind API partnership with a major label, EMI Music. Called OpenEMI, the partnership granted The Echo Nest's B2B music intelligence platform the right to host and manage a first of its kind developer 'sandbox' of data from EMI's catalogue, giving developers the opportunity to take part in "creative briefs" and collaborate on building apps around EMI artists such as Gorillaz, Pet Shop Boys, Professor Green, Chiddy Bang and many more.<sup>75</sup> OpenEMI also includes music from the

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<sup>70</sup> Cheredar, Tom. "Pandora pleads for lower music royalties at congressional hearing," *VentureBeat*, 2012, <http://venturebeat.com/2012/11/29/pandora-congressional-hearing/> (21 March 2013).

<sup>71</sup> *Ibid.*

<sup>72</sup> Resnikoff, Paul. "Spotify: We Pay 70 Percent to Rights Owners," *Digital Music News*, 2012, <http://www.digitalmusicnews.com/permalink/2012/120630spotify> (22 March 2013).

<sup>73</sup> Wauters, Robin. "The royalty squeeze: Why Spotify booked a \$59m net loss on \$244m in revenue in 2011," *The Next Web*, 2012, <http://thenextweb.com/insider/2012/10/05/the-royalty-squeeze-spotify-booked-a-59m-net-loss-in-2011-on-244m-in-revenue/> (21 March 2013).

<sup>74</sup> Kafka, Peter. "Spotify's Daniel Ek on Profits, Label Deals and Angry Musicians: "We're Soing Really, Really Well," *All Things D*, 2012, <http://allthingsd.com/20121206/spotify-daniel-ek-on-profits-label-deals-and-angry-musicians-were-doing-really-really-well/> (22 March 2013).

<sup>75</sup> "EMI Partnership," *The Echo Nest Developer Center*, 2013, <http://developer.echonest.com/sandbox/emi/> (23 March 2013).

iconic Blue Note Records label, thousands of tracks from EMI's catalogue, and access to The Echo Nest's own five billion music data points and developer tools. Developers are invited to submit application concepts to EMI and The Echo Nest for approval, and authorized applications (both free, ad-supported offers and paid offers) are released under a revenue sharing agreement between developers and rights holders, with EMI handling the licensing, clearance requirements and marketing,<sup>76</sup> circumventing issues that often otherwise cause headaches without this kind of partnership. "Application developers are the future of the music business - they are the creative architects reshaping the role music plays in our lives," said Jim Lucchese, CEO of The Echo Nest. "We surveyed our community of 10,000 application developers to understand their biggest challenges in building commercial music applications. Music licensing difficulties were the number one problem developers faced, with assistance in marketing applications coming in at number two. By taking on responsibilities around licensing and putting EMI's marketing muscle behind these applications, OpenEMI is directly addressing these pain points and fostering a more collaborative environment between the established music industry and its future."<sup>77</sup> Since the traditional music industry has historically focused its efforts on resisting innovations in technology rather than considering how it might serve as a tool to improve their existing business, OpenEMI is a unique initiative from a major label actively seeking outside collaborations to create exciting digital offers for consumers.

More recently, Gracenote and MediaNet also released their own APIs. "What's interesting now is that there is this whole ecosystem of APIs out there that makes it possible for you to stitch together your own music service," said Paul Lamere. "You can get local concert listings from Songkick, lyrics from Lyricfind, photos from Getty Images, artist bios from Gracenote and personalized recommendations from The Echo Nest."<sup>78</sup> The recent growth of available tools at the fingertips of developers everywhere has tremendous implications for innovation in the digital music space; by building on these open-ended resources, it is possible to launch a music startup without enduring the burdens associated with negotiating licensing for a brand new service.

## Music and Brands

The relationship between music and brands is not a new development for the music business, but it is becoming increasingly important as the industry continues to develop and experiment with alternative revenue streams. The mutual benefit of a music-brand partnership typically garners the artist a boost in income, investment from the brand, or other conveniences such as free products or services, while the brand stands to potentially gain increased awareness and legitimacy amongst the artists' fans. Brands have long licensed popular music for advertising campaigns and other promotional efforts, but the types of partnerships now occurring are continuing to diversify outside traditional boundaries. One notable trend is appointing well-known artists as brand ambassadors with fancy titles; in the last year alone, corporate marketing-related roles have been appointed to Alicia Keys (for

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<sup>76</sup> "The Echo Nest and EMI Music Team for 'OpenEMI' and App Innovation," *PR Newswire*, 2011, <http://www.prnewswire.com/news-releases/the-echo-nest-and-emi-music-team-for-openemi-and-app-innovation-133141733.html> (23 March 2013).

<sup>77</sup> *Ibid.*

<sup>78</sup> Pham, Alex. "Can APIs Solve Music's 'Crisis of Innovation'?" *Billboard*, March 14, 2013.

BlackBerry), Beyonce (for Pepsi), Taylor Swift (for Diet Coke) and most recently, Justin Timberlake (for Bud Light Platinum, not to mention his co-ownership in Myspace).<sup>79</sup>

Much of the discussion around brands and music is concerned with the question of whether the two are complementary. This year at SXSW, brand and label representatives from the likes of Nike, PepsiCo, and the Beggars Group assembled to discuss the relationship between Music and Brands in a panel titled “The New Vibrant Ecosystem of Brands and Music”. Panelists agreed there is no “one size fits all” model for brands working with artists and bands. Complementary partnerships are borne of common goals, such as Converse’s open-to-all, free of charge Rubber Track recording studio. Known as the go-to sneaker brand of choice for punks and rockers for decades, the brand opened recording studios to support independent and developing acts, strengthening their image as an alternative, youthful company.

Despite the potential of music-brand partnerships, questionable motives can appear to have a parasitic effect. Bob Dylan’s notorious appearance in a Victoria’s Secret commercial drove fans to question the activist’s intentions, with many writing him off as now longer a symbol of rebellion. Long time brand ambassadors The Black Eyed Peas are so intertwined with corporate partners that they’ve been labeled “The Most Corporate Band in America” by The Wall Street Journal.<sup>80</sup>

## Monetization

Monetization is a word on the tip of everyone’s tongues in the music industry of late, as artists, managers, record labels, investors and outside parties continue to experiment with new business models. The following are three approaches to monetizing music in an age where it pays to be creative in diversifying revenue channels.

### YouTube Music Videos - Official & User Generated

It is no secret that music consumption is shifting to online and mobile formats, with music videos on YouTube, the world’s third most popular website,<sup>81</sup> driving a sizeable portion of this traffic. Nearly 40%, or 384 billion, of YouTube’s trillion-plus views come from music videos, a figure that Digital Music News claims is larger than Spotify, Rhapsody, Grooveshark, Rdio, MOG, Deezer, and eMusic combined.<sup>82</sup> A study by comScore found that Americans streamed 43.5 billion videos in 2011, a 44% increase from 2010, while 105.1 million Americans watched videos online each day in 2011, a 43% increase from 2010.<sup>83</sup>

Monetizing YouTube Videos isn’t a new concept, as labels and other copyright holders have had the opportunity to join YouTube’s Partner Program and Content ID system to generate revenue from advertisements since 2007. Content ID allows copyright holders to upload

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<sup>79</sup> Zmuda, Natalie. “More Than a Pitchman: Why Stars Are Getting Marketing Titles” *Advertising Age*, 2013, <http://adage.com/article/news/timberlake-beyonce-marketing-titles/239712/> (24 March 2013).

<sup>80</sup> Jurgensen, John. “Black Eyed Peas: The Most Corporate Band in America,” *The Wall Street Journal*, April 16, 2010.

<sup>81</sup> “Youtube.com Site Info,” *Alexa*, 2013, <http://www.alexa.com/siteinfo/youtube.com#> (26 March 2013).

<sup>82</sup> Resnikoff, Paul. “YouTube Music: It’s Bigger Than Pandora, Spotify, Rhapsody, & Grooveshark Combined,” *Digital Music News*, 2012, <http://www.digitalmusicnews.com/permalink/2012/120501youtube> (26 March 2013).

<sup>83</sup> ComScore 2012 U.S. Future in Focus

reference files of their content to YouTube, which compares these official videos to user-uploaded videos. Following a match, YouTube notifies the copyright holder and gives them the choice to block, track or monetize the content. When Content ID was first unveiled, most copyright holders used the fingerprinting tool in efforts to curb piracy and block unauthorized videos, typical of the general defensive stance associated with the legacy music industry when music began appearing online. In recent years, however, there has been a huge shift amongst major companies and independents alike in utilizing the tool for monetization and marketing. Content ID Senior Product Manager David King has said that by now most rights holders prefer to use the service to monetize their content, and those that do witness their overall video views more than doubling.<sup>84</sup> The most successful story of monetization capabilities is YouTube's most viewed video of all time and viral meme "Gangnam Style", by South Korean Rapper Psy, which has generated over \$8 million alone in advertising revenue. Of the estimated \$0.65 generated for every view of a video uploaded to YouTube containing the song, roughly half of the revenue goes to Psy and his record label after paying the creator of the user-generated video.<sup>85</sup>

INDmusic, a Brooklyn based startup, has also received a lot of media attention after maximizing the monetization of Baauer's viral hit "Harlem Shake". The company services copyright holders by assisting in identifying videos missed by YouTube's Content ID system, effectively garnering the copyright holder a higher CPM (cost per thousand viewer rate) than copyright holders may be able to achieve on their own.<sup>86</sup> The company also embeds links on user-generated videos for viewers to buy the song from a number of digital download outlets, further boosting an artist's revenue.

### Unique Experiences

Consumers are presented with a seemingly never-ending array of options to access music, often with little differentiation from one another. In both recorded and live music, there is an abundance of choice but scarcity of unique appeal or feeling of true connection with artists. As mentioned earlier, research indicates stakeholders in the music industry could considerably increase revenues provided they offer consumers a more engaging set of experiences. One way to do this might be to offer branded music applications containing exclusive content and/or tailored playlists and more from an artist, as a number, including Quincy Jones, Tiësto, Rancid, and others, have recently done via Spotify.<sup>87</sup> These apps produce positive results for all parties, as they provide participating artists' fans a more intimate digital experience and produce additional revenue for the artists all while enabling the music service to offer more value to listeners in its in-house app environment.

Stageit, winner of MIDEM 2013's startup competition for the category "Direct to consumer sales & content monetisation", offers music consumers an even more engaging way to

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<sup>84</sup> Gannes, Liz. "From Monitor to Monetize: The Evolution of YouTube Content ID," *Gigaom*, 2009, <http://gigaom.com/2009/09/28/from-monitor-to-monetize-the-evolution-of-youtube-content-id/> (25 March 2013).

<sup>85</sup> Mims, Christopher. "Google: Psy's 'Gangnam Style' Has Earned \$8 Million On YouTube Alone," *Business Insider*, 2013, <http://www.businessinsider.com/google-psys-gangnam-style-has-earned-8-million-on-youtube-alone-2013-1> (25 March 2013).

<sup>86</sup> Hampp, Andrew. "'Harlem Shake': The Making and Monetizing of Baauer's Viral Hit," *Billboard*, February 15, 2013.

<sup>87</sup> Buskirk, Eliot Van. "Spotify's First Artist Apps: Disturbed, Quincy Jones, Rancid, and Tiësto," *Evolver.fm*, 2012, <http://evolver.fm/2012/06/27/spotify-s-first-artist-apps-disturbed-quincy-jones-rancid-and-tiesto/> (29 March 2013).

connect with the music and artists they love. Self-dubbed as the “venue for live and interactive virtual concerts providing fans with a front row seat to a backstage experience”, Stageit provides a platform for artists to perform concerts online, giving them control over the duration and price of the show. Once a show is fully funded, fans can interact with both fellow fans and the performing artist through the chat window and the artist’s Tip Jar. Since the platform’s inception two years ago, indie and well-known artists alike have performed on the platform, including Jimmy Buffett, Indigo Girls, Jason Mraz and many more.<sup>88</sup> These unique, non-archived performances are why Stageit has been so popular with fans, who pay on average \$12 a head to attend, twice as much as they did a year ago.<sup>89</sup> The company is expected to report roughly \$1.3 million in revenues for 2012.<sup>90</sup>

Branded music apps and interactive non-archived, one time live shows are just two examples of how artists and industry stakeholders can expand their revenue channels utilizing finished creative content. There also lies a great opportunity to monetize the creation process itself. Some artists are now offering limited “seats” in the studio while they record, often for upwards of \$1,000 per day. Merge.fm now offers an online example of this concept too, giving fans access to an artist’s creation process in exchange for \$1.99 to \$4.99 as specified by the artist.<sup>91</sup> The service is free to musicians and offers them 85% of revenues received on their behalf. Artists benefit by receiving valuable feedback from fans before releasing finished work, having the ability to host remix competitions, and using the site to collaborate with other songwriters and producers. In an increasingly transparent and social world where fans want to feel apart of the music experience, the idea of giving them the opportunity to become involved in the process begets an interesting potential scalable revenue stream.

### Simplifying Social and Mobile Commerce

To fully take advantage of growing revenue channels today and in the future, artists and music industry stakeholders should be greatly concerned with optimizing their social and mobile commerce strategies. The value of social commerce is expected to more than triple from \$9 billion to \$30 billion globally by 2015,<sup>92</sup> while half of all web sales are expected to occur on social media channels by 2015.<sup>93</sup> While consumers are engaging with social media on desktops and mobile devices more than ever, a key consideration should be the simplification of purchasing experiences, ideally allowing fans to purchase music and music related goods directly in-stream without redirection to an outside website. Social commerce platforms such as TopSpin, Moontoast, and Chirpify are giving clients the ability to offer their customers just that, paired with rich analytical tools.

Chirpify, for example, allows customers to purchase in-stream on Facebook, Instagram, or Twitter by merely leaving a comment with the word “buy”. The customer’s registered credit

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<sup>88</sup> Satariano, Adam. “Evan Lowenstein’s Stageit, a Live Music Site,” *Businessweek*, February 9, 2012.

<sup>89</sup> Greenburg, Zack O’Malley. “From Pop Star To Startup Boss: The Story of Stageit’s Evan Lowenstein,” *Forbes*, December 24, 2012.

<sup>90</sup> *Ibid.*

<sup>91</sup> “Frequently Asked Questions,” *mergefm*, 2013, <http://merge.fm/pages/faq> (27 March 2013).

<sup>92</sup> Anderson, Matt, Brusa, Jennifer, Price, Jerrell, and Sims, Joe. “Turning ‘Like’ to ‘Buy’ – Social Media Emerges as a Commerce Channel,” *booz&co*, 2011, <http://www.booz.com/global/home/what-we-think/reports-white-papers/article-display/turning-like-social-media-emerges> (28 March 2013).

<sup>93</sup> Murphy, Samantha. “50% of Web Sales to Occur Via Social Media,” *Mashable*, 2012, <http://mashable.com/2012/11/01/facebook-sales/> (28 March 2013).

card preference or Paypal is then automatically charged for the transaction over the Chirpify platform, while the customer goes about doing whatever they were doing before. Clients can also use the platform in the same manner to conduct sweepstakes or giveaways and to offer coupons. Direct-to-fan expert Amanda Palmer and her use of Chirpify exemplifies the huge boost in potential revenue through an in-stream commerce platform. After Palmer tweeted about a new t-shirt available for \$20 via Chirpify, the shirts sold every thirty seconds, resulting in upwards of \$5,000 in revenue from one tweet.<sup>94</sup> Other well-known artists have used the platform to date as well, including Green Day, ASAP Rocky, and Tim McGraw, as well as major brands such as Adidas, Puma, Taco Bell, and the Portland Trail Blazers.<sup>95</sup>

## Direct to Fan (D2F)

Over the past few years, it seems as if one cannot navigate the music industry space without encountering discussions over D2F strategy. With a dark shadow cast on the industry's traditional revenue sources, proponents of the D2F strategy point to an expanding number of channels empowering content creators to reach fans and supporters directly and independently.

Whether an artist is looking to launch a crowd-funded campaign, simply host and share their audio, open a personalized music and music merchandise web store, or secure distribution to the leading digital music stores, artists have an array of tools available for them at reasonable cost. Music and merchandise platform Bandcamp proudly proclaims artists have made over \$36 million using its site,<sup>96</sup> while leading crowdfunding platform Kickstarter reports it has successfully distributed over \$64.6 million to music related projects.<sup>97</sup> A number of high profile success stories employing the D2F strategy have emerged as textbook examples supporting the tactic, such as Amanda Palmer's eyebrow-raising \$1.2 million Kickstarter campaign<sup>98</sup> and Radiohead's 2007 self-released success *In Rainbows*. In the *In Rainbows* example, the band urged fans to "pay what you want" for digital copies of their new album and sold 122,000 copies in the first week alone,<sup>99</sup> reaching Billboard 200's number one spot the following week. Trent Reznor (Nine Inch Nails) is also heralded as a champion of the D2F strategy, successfully connecting with fans while giving them reasons to buy on a number of occasions such as the Nine Inch Nails release of *Ghosts I-IV* under a Creative Commons license. With *Ghosts I-IV*, the band offered the album at a number of price points, including a limited 2,500 copy run of the \$300 "Ultra-Deluxe Limited Edition" signed boxset by Reznor himself, which sold out in less than thirty hours, making the band \$750,000.<sup>100</sup>

Despite the hype about the benefits of utilizing a D2F strategy, it does not appear to be a

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<sup>94</sup> Chapman, Lizette. "Chirpify's Tweet-Sales Potential Could Make Shirt Sale Look Like Chump Change," *The Wall Street Journal*, 2012, <http://blogs.wsj.com/venturecapital/2012/08/28/chirpifys-tweet-sales-potential-could-make-shirt-sale-look-like-chump-change/> (30 March 2013).

<sup>95</sup> "The Social Commerce and Payments Platform," *Chirpify*, 2013, <https://chirpify.com/> (30 March 2013).

<sup>96</sup> "Bandcamp," *Bandcamp*, 2013, <https://bandcamp.com/> (30 March 2013).

<sup>97</sup> "Kickstarter Stats," *Kickstarter*, 2013, <http://www.kickstarter.com/help/stats?ref=footer> (30 March 2013).

<sup>98</sup> Peoples, Glenn. "Amanda Palmer Q&A: Why Pay-What-You-Want Is The Way Forward, and More," *Billboard*, January 28, 2013.

<sup>99</sup> Cohen, Jonathan. "Radiohead Nudges Blige From Atop Album Chart," *Billboard*, 2008, <http://web.archive.org/liveweb/http://www.billboard.com/articles/news/1046867/radiohead-nudges-blige-from-atop-album-chart> (30 March 2013).

<sup>100</sup> Rosoff, Matt. "Update: NIN grosses \$750,000 overnight," *CNET News*, 2008, [http://news.cnet.com/8301-13526\\_3-9886395-27.html](http://news.cnet.com/8301-13526_3-9886395-27.html) (30 March 2013).

one-size-fits-all solution for the music industry. Critics point out the fact that the majority of the artists who have found immense fruition in D2F efforts undeniably have benefitted from a strong fan base originating from development at a major label, because major labels often have relationships and expertise that cannot be matched by any DIY tool. (Even Trent Reznor, despite DIY success, recently returned to a major label (Columbia) for his new project.) Without that boost of awareness from a previous relationship with a major label, it is no surprise that the majority of artists still struggle to get by. A recent survey by the Future of Music Coalition estimates the average gross estimated music income to hover around \$34,455, a figure suggesting musicians make \$5,000 less annually than the average American when compared to the US Bureau of Labor Statistic's per capita personal income estimate for 2010 of \$39,945.<sup>101</sup> Many musicians are concerned with consumption methods growing in popularity, such as streaming and associated royalty rates due to them through streaming channels, and the search for creative revenue streams continues.

## 4) Business Model Approach

Imagining new business models for the music industry is a central focus at this year's Rethink Music Valencia workshop, as it is crucial to reinvent ways of doing business to remain competitive and successful in a changing landscape. In this section the business model concept will be discussed, followed by brief descriptions of business models of some of the most successful companies currently doing business in the music industry.

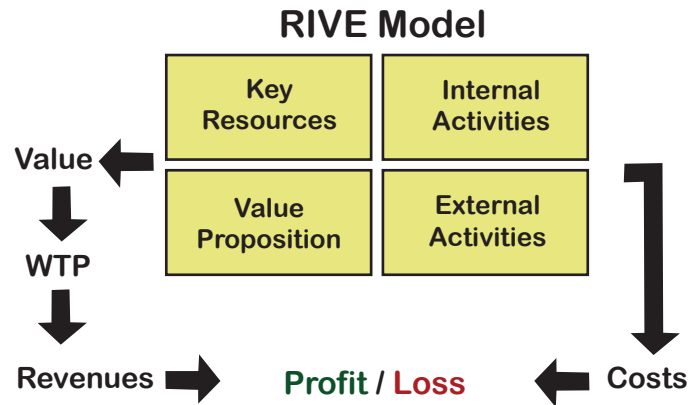
### a) Concept

There are many interpretations of the business model concept; however, its core function is to describe the set of choices a firm makes that determine its ability to create value and generate profits. Business models can be complex to explain, as they encompass many kinds of choices. Successful business models have a few notable qualities. First, all choices are consistent and contribute to a larger story that makes sense. Second, successful business models are designed to address concerns of all stakeholders, and effectively create value for all partners. Without creating value, firms cannot generate profit. If clients appreciate the value generated by a business model, their willingness to pay (WTP) increases, which in turn generates revenue. One way to conceive of a business model is through the RIVE model, as originally conceived by Dr. Emilien Moyon. The RIVE model explains a business model in four interrelated sections - resources, internal activities, external activities and value proposition. Resources can be considered as anything the firm contributes towards delivering its value proposition, its central offer to consumers and customers. (Often, the value proposition is different for the consumer and the customer, who are not always the same parties). Internal activities are activities the firm performs within the company, whereas external activities are activities the firm chooses to outsource, a decision that is often made when a job is too costly or inefficient to perform within the organization. Below is a visual representation of the RIVE model:

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<sup>101</sup> Houghton, Bruce. "Average Musician Grosses \$5490 Less Than Average American," *hypebot*, 2012, <http://www.hypebot.com/hypebot/2012/12/average-musician-grosses-5490-less-than-average-american-chart.html> (15 April 2013).





Choices on the left side impact the value created by a firm and willingness to pay (from either consumers and/or customers), resulting in revenue. Choices on the right side impact a firm's costs, and the difference between these two sides result in a firm's ability to make profit.

### b) Application to specific examples

To identify elements of success in current music offerings, below is a brief discussion of the business models of three of the most prevalent companies in the music business space today: iTunes, YouTube and Spotify.

#### iTunes Store (est 2003)

Apple's iTunes Store has found immense success since its debut a decade ago - in 2008, it became the top music vendor in the United States,<sup>102</sup> and the top music vendor in the world in February 2010.<sup>103</sup> The success of the iTunes store is rooted in a successful business model built around a simple yet compelling value proposition: a comprehensive digital catalogue of the world's music available to consumers in an extremely convenient way. The iTunes Store was the first digital music store at the time to offer a unique pricing model, allowing consumers to purchase and download individual songs a-la-carte, rather than full albums, meeting a growing demand among digital music consumers. Furthermore, the physical constraints of a brick-and-mortar store limited retailers to stocking only the most popular titles, whereas the iTunes Store benefits from stocking a wide range of offerings, from hits to the most far-out niche titles, taking advantage of the comparably far cheaper digital shelf space associated with an online marketplace.

The key resources include patents on its software and other intellectual property, staff (including but not limited to lawyers, programmers, designers, and testers), and most importantly, a strong existing brand and customer loyalty. External activities include actual music recording production and preparations necessary to create a finished product, which

<sup>102</sup> "iTunes Store Top Music Retailer in the US," *Apple*, 2008, <http://www.apple.com/pr/library/2008/04/03iTunes-Store-Top-Music-Retailer-in-the-US.html> (16 April 2013).

<sup>103</sup> "iTunes Store Tops 10 Billion Songs Sold," *Apple*, 2010, <http://www.apple.com/pr/library/2010/02/25iTunes-Store-Tops-10-Billion-Songs-Sold.html> (16 April 2013).

is delivered to the iTunes Store by the label or sound recording owner or administrator. Internal activities include managing legal relationships with labels and sound recording owners and administrators, while maintaining and improving software, technology and database design in order to ensure seamless integration with all of Apple's products and services.

The iTunes Store's comprehensive catalogue in addition to its seamless integration with the Apple products and services has made it the of the most successful music retail storefront in the post-Napster age, and the number one source of revenue for the major labels. Their customer-pleasing interface and pricing structure is now the industry standard, which many other digital stores seek to replicate.

### YouTube (est. 2005)

The world's third most popular visited website<sup>104</sup> and second largest search engine (after parent company Google)<sup>105</sup> is quickly becoming the most popular music streaming service – 64% of teens listen to music through YouTube more than through any other source, while 7% of all people do the same.<sup>106</sup> Like iTunes, YouTube's value proposition is simple - it is a free and easy way to share and access the largest collection of videos. The "free" quality of the video streaming platform has led it to gain an impressive volume of consumers, thus making it an extremely attractive platform for advertisers. The company recently announced that ads on the streaming platform show a higher ROI compared to TV ads for brand advertisers.<sup>107</sup> YouTube makes the majority of its revenue from advertising, based on a CTR (click through rate) where better alignment of the ad with the viewer demographic results in a higher payout per click. On the cost side of the equation, expenses come through internal activities such as paying partners, typical operating expenses (salaries, rents), technology, and network maintenance. External activities include actual video generation, which is done free of charge by the platform's extremely large user base. So far, YouTube has provided extensive value to both consumers and customers, fortifying its position as the premier video streaming site for consumers, content creators, and advertisers alike.

### Spotify (est. 2008)

With 24 million active users and 6 million paying subscribers,<sup>108</sup> Spotify is quickly becoming the most popular on-demand and download music streaming service. The key driver of its business model is its value proposition similar to both the iTunes Store and Youtube: it offers

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<sup>104</sup> "Alexa Top 500 Global Sites," *Alexa*, 2013, <http://www.alexa.com/topsites> (16 April 2013).

<sup>105</sup> Schonfeld, Erick. "ComScore: YouTube Now 25 Percent Of All Google Searches," *TechCrunch*, 2008, <http://techcrunch.com/2008/12/18/comscore-youtube-now-25-percent-of-all-google-searches/> (16 April 2013).

<sup>106</sup> "Music Discovery Still Dominated By Radio, Says Nielsen Music 360 Report," *Nielsen*, 2012, <http://www.nielsen.com/us/en/press-room/2012/music-discovery-still-dominated-by-radio--says-nielsen-music-360.html> (16 April 2013).

<sup>107</sup> Lawler, Ryan. "YouTube Has Found Its Business Mode, And Is Paying Out Hundreds Of Millions Of Dollars To Partners," *TechCrunch*, 2012, <http://techcrunch.com/2012/07/19/youtube-business-model/> (16 April 2013).

<sup>108</sup> Sawers, Paul. "Spotify now has in excess of 24 million active users, with more than 6 million paying subscribers," *The Next Web*, 2013, <http://thenextweb.com/insider/2013/03/12/spotify-now-has-in-excess-of-24-million-active-users-with-more-than-6-million-paying-subscribers/> (16 April 2013).

a breadth of music at the touch of the fingertips, either for free (supported by advertising) or with added benefits available through reasonable subscription plans. To date, Spotify primarily makes its revenue from advertisement fees and subscription fees. To offer its extensive music catalogue, it maintains key resources of licensing agreements with rights owners, and patents on its software and platform. The company's costs include internal activities such as operating expenses (salaries, rents), bandwidth costs, and network maintenance, and external activities include licensing agreements (the bulk of their costs), development of software and APIs to be used by third party developers, and partnerships with telecommunications providers and automakers. As mentioned earlier, Spotify has yet to achieve profitability; however, many in the industry believe the streaming service's "freemium" business model will lure its growing free user base to paying subscription plans that could prove the model to be sustainable and lead the recording industry in its recovery.

The business models of the companies discussed above are successful in that they offer compelling value propositions to all or some partners, but there is room for innovation and improvement thanks to flourishing opportunities brought forth by the digital realm. To identify some of these opportunities, we sought to identify consumer expectations regarding music services so that we may draw conclusions as to how the industry may imagine new business models for the future of the music industry.

## **5) Research**

### **a) Purpose of Research**

As consumption continues to shift online, there is a lot of discussion in the music industry about rethinking traditional business models, particularly within the hardest hit sector of the industry, recorded music. Digital music services have been praised by many for their potential to rejuvenate revenues, and have gained substantial interest from consumers as well as investors in the past five years. Despite their popularity, digital services have yet to generate substantial profits that would restore the industry to its former glory. Our research seeks to provide insight as to how digital music services could enhance their offers to consumers and potentially increase their willingness to pay. To do so, we conducted a consumer survey to compare general entertainment consumption habits with music consumption habits, and in particular, assess music consumers' attitudes towards current digital music services. We hope to shed some light on opportunities for the industry to improve music consumers' experience with digital music offers that may in turn increase their willingness to pay for them.

### **b) Methodology**

#### **i. Sampling**

The survey was administered by utilizing web survey tool SurveyMonkey, with settings constraining respondents from completing the survey more than once. We felt using the Internet was the most relevant method to circulate our survey because it enabled us to

extend our reach to a larger audience than physical constraints allow, therefore comprising a more representative sample of music consumers all over the world. From February 28th, 2013 to April 12th, 2013, invitations to partake in the survey were sent out on social networking website Facebook, Twitter, to individuals in the Berkman Center and Rethink Music databases, on the Rethink Music Valencia website and on the Berklee Valencia website.

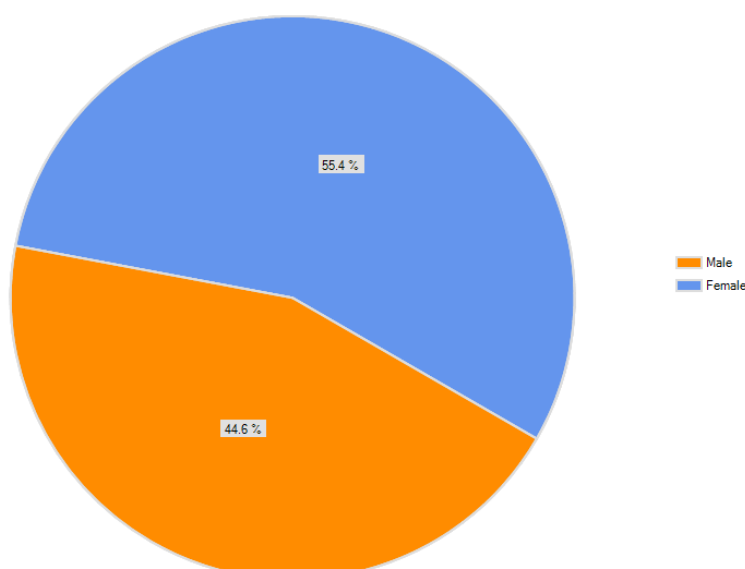
## ii. Survey Design

The final survey was a result of a combination of insights, the first being an initial pilot survey, developed in the fall of 2012, serving as an exploratory investigation aiding in crafting an optimal methodological framework. Furthermore, ongoing conversations amongst Berklee Valencia's Global Entertainment and Music Business program graduate students and faculty as well as a cross-departmental focus group staged at Berklee Valencia were also instrumental in developing the research question and survey design. (The cross-departmental focus group was comprised of members from each of Berklee Valencia's graduate programs - Global Entertainment and Music Business, Contemporary Studio Performance and Scoring for Film, Television and Video Games - as well as undergraduate students in the Global Studies program visiting from Berklee's main campus in Boston.) The goal of the final survey was to present concise, unbiased questions with simple language so that respondents understood what was being asked and retained interest throughout the survey.

The first few questions of the survey were constructed to determine participants' willingness to pay for general entertainment activities in relation to their willingness to pay for digital music offers. (Willingness to pay is most often thought of as the maximum amount of money a person would be willing to pay in order to receive a good or service.) Subsequent questions were designed to identify main methods of music consumption, assess participants' satisfaction with current digital music offers, and identify qualities of participants' ideal digital music service. The final survey was comprised of thirteen questions including multiple choice, rank order scale, and ten-point Likert scale format. Piping logic was employed to route participants around questions that did not apply to them. Based on common answers from the pilot survey, a number of questions on the final survey were supplied with possible answers for participants to choose from (such as in Question 4 and 5). For the question "Imagine a feasible digital music service that would fulfill your expectations", we felt it was important to leave an empty essay box for respondents to fill with their own

unbiased ideas, rather than suggest various features to choose from.

Figure 1: What is your gender?



## c) Results

A total of 553 participants attempted the survey of which 419 fully completed it.

After filtering out the 134 incomplete surveys, the final sample was narrowed to 419.

Of the data from the final sample, **Figure 1** depicts the proportion of males to females who took the survey, with 55.4% being female.

**Figure 2** depicts the age distribution of respondents, showing the majority of respondents belonging either to the 18-24 years old (32.5%) or 25-34 years old (32.9%) age groups. Regarding respondents' country of origin, entertainment consumers from thirty-six countries completed the survey.

Figure 2: What is your Age?

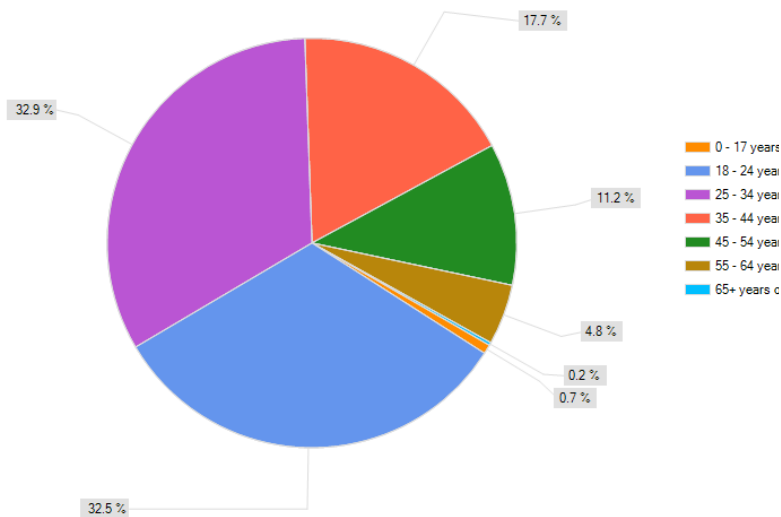
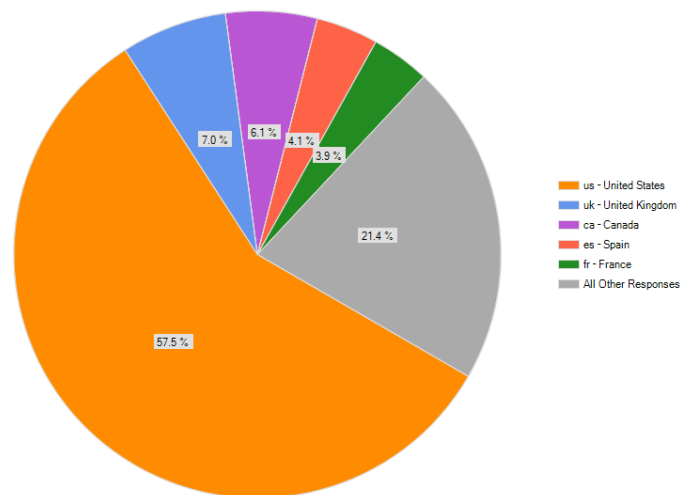
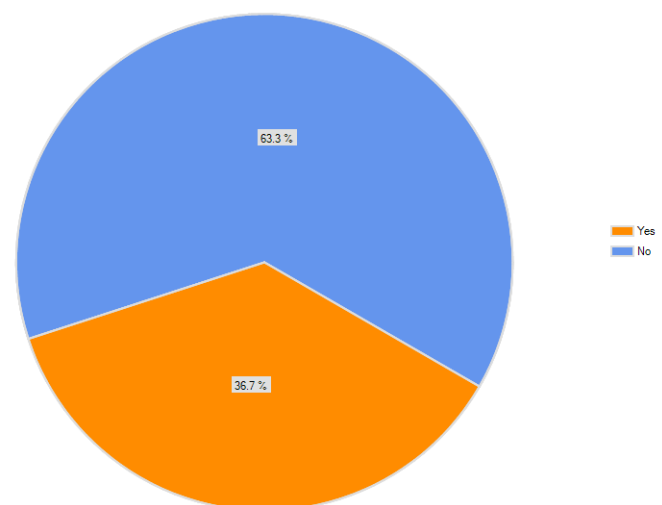


Figure 3: What is your country of origin?



**Figure 3** depicts the breakdown of respondents' countries of origin, the top five countries represented were the United States (57.5%), followed by the United Kingdom (7%), Canada (6.1%), Spain (4.1%) and France (3.9%), with all other countries represented by the remainder of respondents (21.4%). The majority of respondents in the survey sample (63.3%) indicated they are not musicians, as shown in **Figure 4**. The distribution of respondents balanced out across genders, age groups and country of origin affirm efforts to have a representative sample of music consumers through the survey's diffusion via the Internet.

Figure 4: Are you a Musician?



The first few questions of the survey were concerning the participants' general entertainment consumption patterns. We wanted to gauge consumers' overall entertainment subscription

trends and willingness to pay for various types of entertainment in comparison to digital music subscription services.

Figure 5: Do you currently pay for any entertainment subscription services?

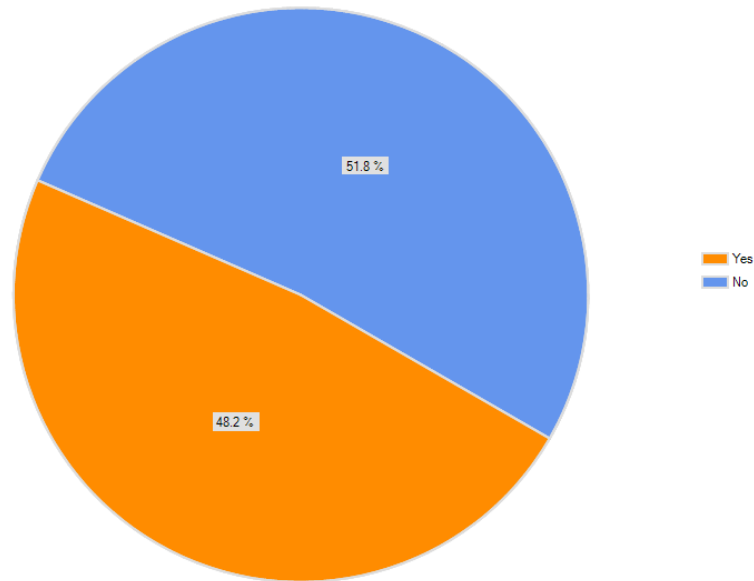
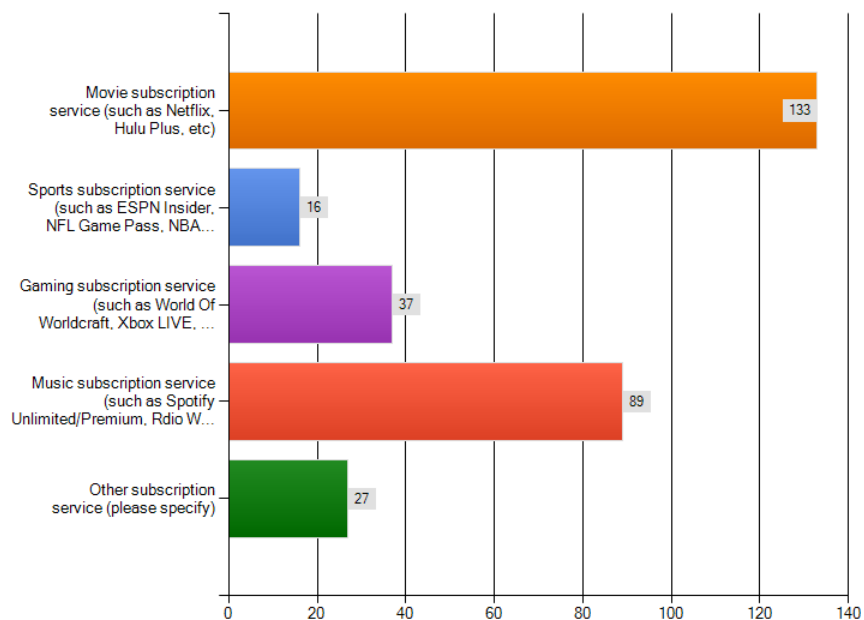
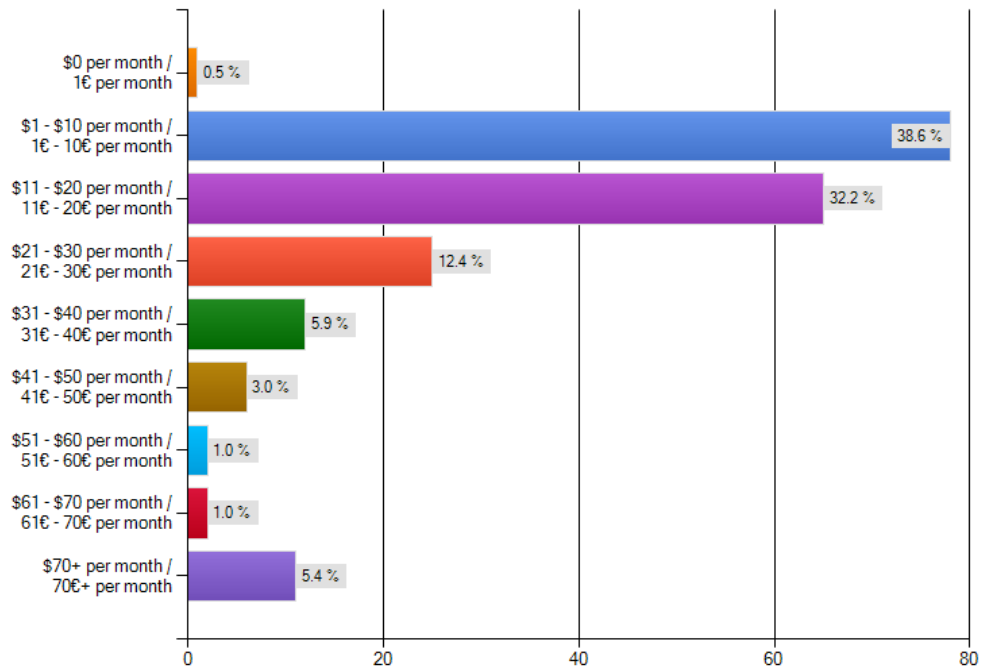


Figure 5 shows almost half of respondents (48.2%) indicated they currently have entertainment subscriptions. Figure 6 shows movie subscriptions are the most popular entertainment subscription service amongst all survey respondents (31.74%), followed by music subscriptions (21.24%). Less popular subscriptions include gaming subscriptions (8.83%), subscriptions other than the categories provided (6.44%) and sports subscriptions (3.82%), also seen in Figure 6.

Figure 6: What entertainment subscription service(s) are you currently paying for?

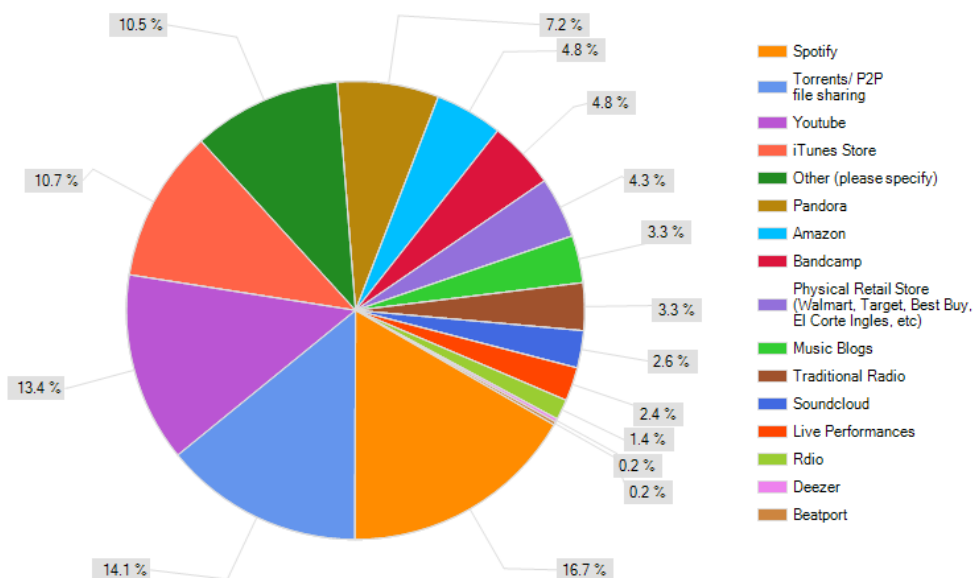


**Figure 7: How much a month are you currently paying for all your entertainment subscription services combined per month?**



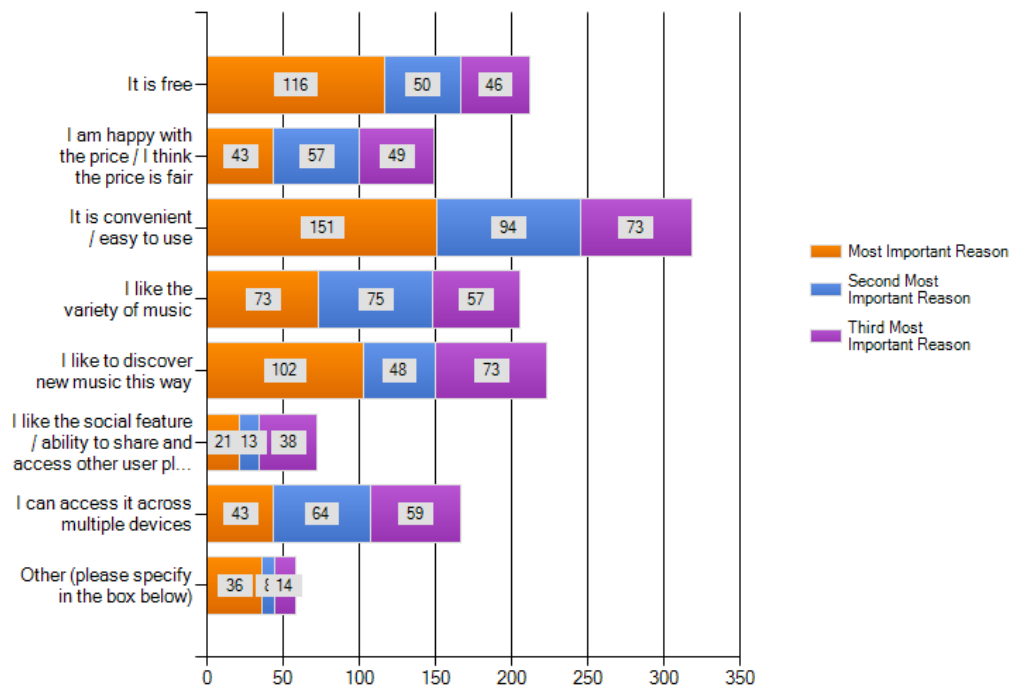
Of the respondents that indicated they currently pay for entertainment subscription services, the majority of respondents were paying either \$1-\$10 per month / 1€ - 10€ per month (38.6%) in total for all their subscriptions, or \$11-\$20 per month / 1€ - 20€ per month (32.2%), as illustrated in **Figure 7**.

**Figure 8: What is the number one way you get music?**



In response to our question about how respondents most often access music, Spotify was ranked as the number one method (16.7%), followed by Torrents / P2P file sharing (14.1%), and YouTube (13.4%), followed by the iTunes Store (10.7%) close behind. The full breakdown of the various ways respondents indicated they most often get music from is shown in **Figure 8** on the previous page. It is interesting to note that no one method commands more than 20% of the results, suggesting there is no dominant leader in the delivery of recorded music to consumers.

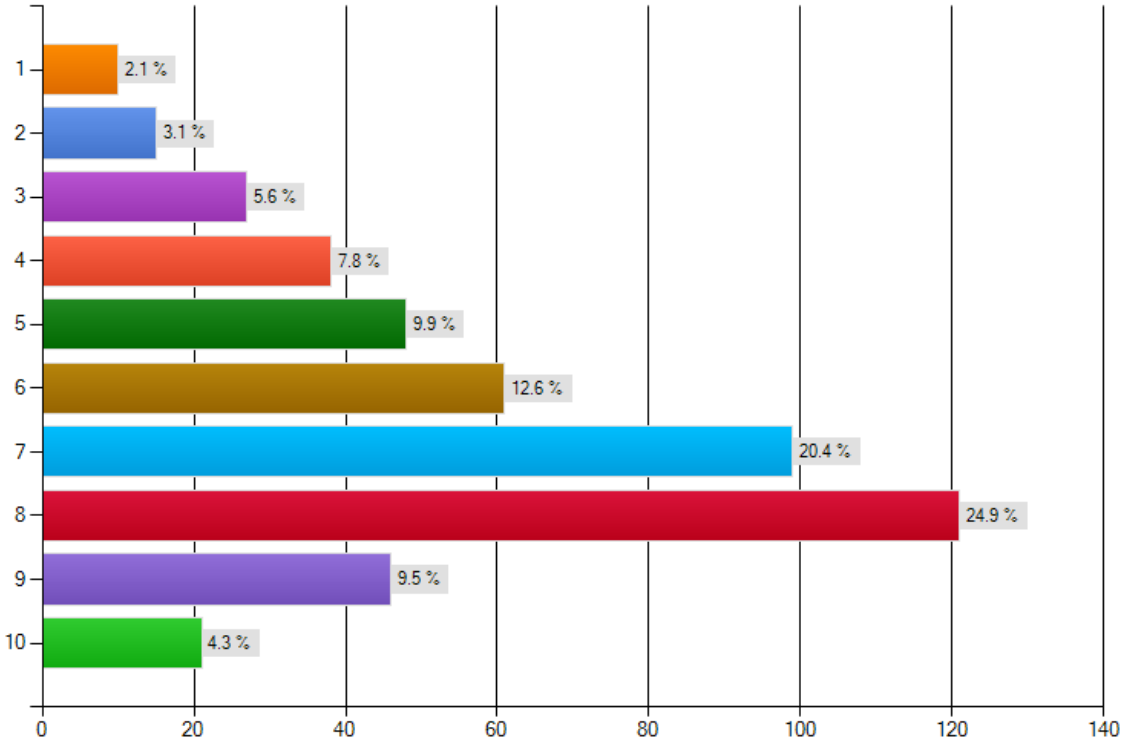
**Figure 9: Using the answer you selected above, please rank the top 3 reasons why you like to get music this way. Please do not select the same answer more than once.**



**Figure 9** depicts respondents' top three reasons behind why they like to get their music from their number one source they indicated earlier in the survey. "It is convenient / easy to use" was most often cited as the number one reason (25.81%) why respondents like to get music from their top source, followed by "It is free" (19.83%) and "I like to discover music this way" (17.44%).



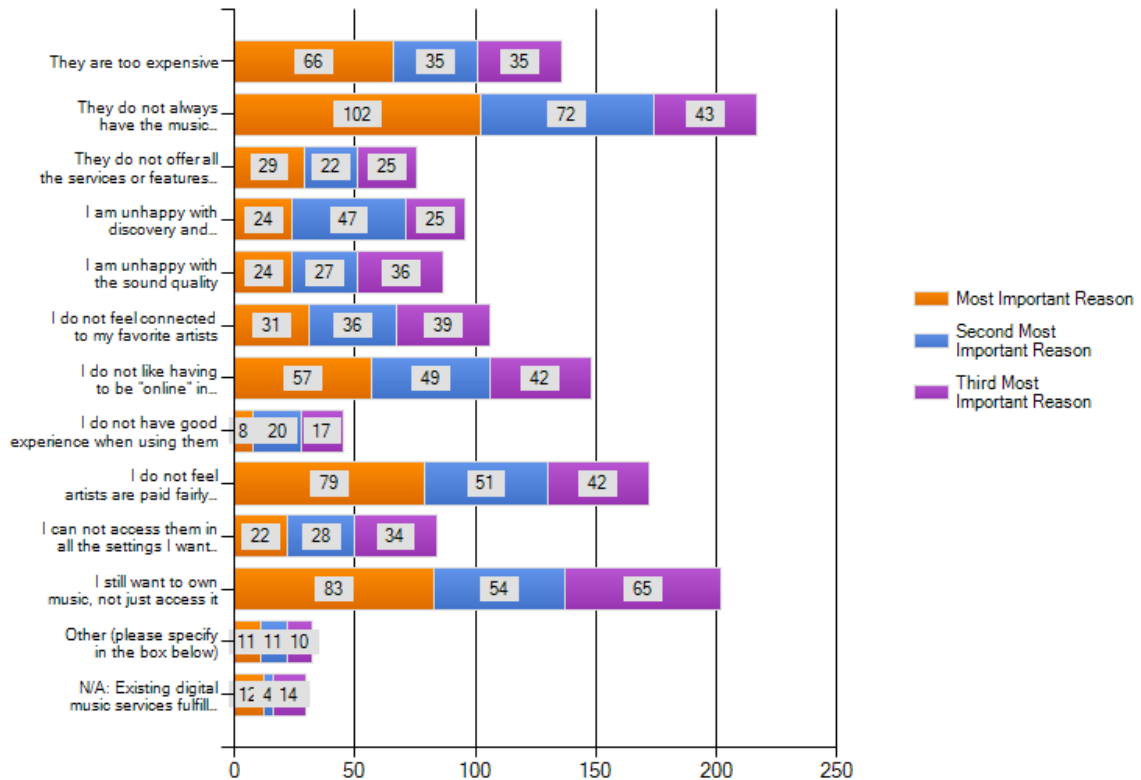
Figure 10: How much do existing digital music services fulfill your expectations? Choose a number: 1 being they do not fulfill your expectations, 10 being they match your expectations to the fullest. ("Digital music services" include many platforms, such as Pandora, Spotify, iTunes Store, Amazon and so on.)



Respondents were also asked to indicate how much existing digital music services fulfill their expectations. **Figure 10** depicts the distribution of satisfaction ratings of existing digital music services, showing ratings of 8 (24.9%) and 7 (20.4%) being most popular on a scale of 1 to 10, with 10 as completely fulfilling expectations. The average fulfillment rating was 6.51.

Respondents that did not indicate existing digital music services fulfill their expectations to the fullest were asked to select the three most important reasons why this was the case, as featured in **Figure 11**; “They do not always have the music I am looking for” was most often cited as the number one reason (19.03%), followed by “I still want to own music, not just access it” (15.49%), and close behind was “I do not feel artists are paid fairly” (14.74%).<sup>109</sup>

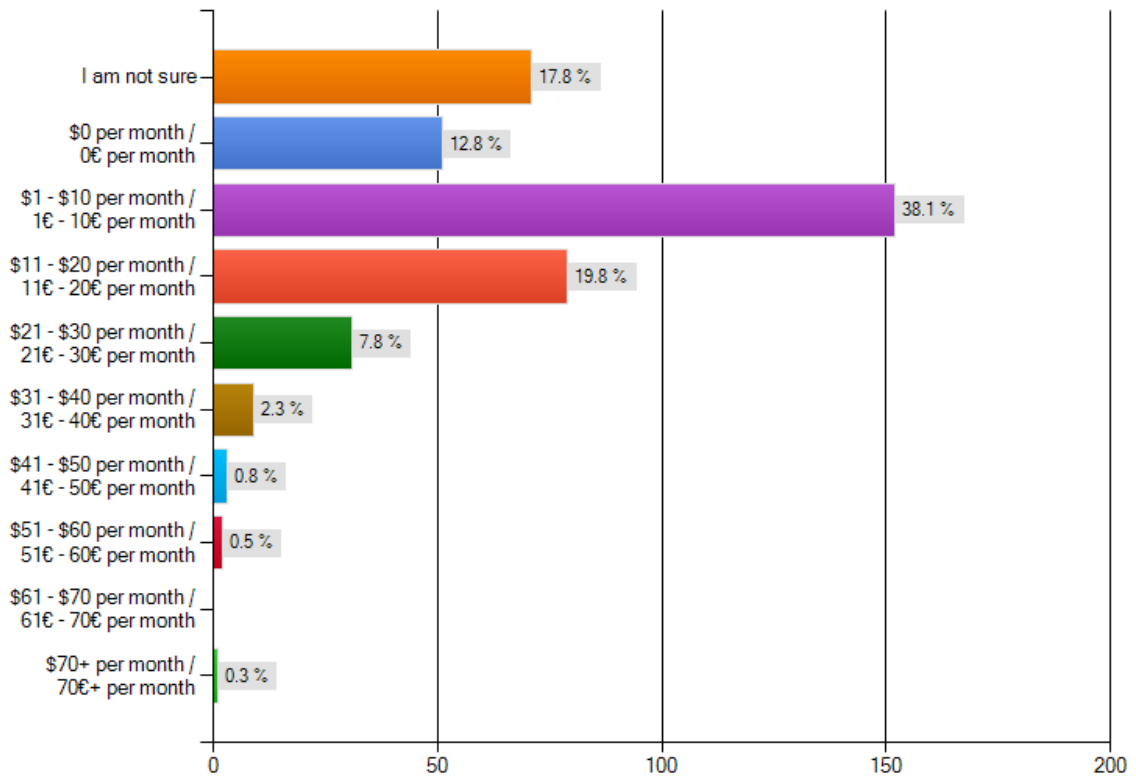
**Figure 11: Please select the three most important reasons why existing digital music services do not totally fulfill your expectations.**



Finally, participants were presented with an essay box and asked to “Imagine a feasible digital music service that would fulfill your expectations”. **Figure 12** on the following page displays 38.1% of respondents indicated they would be willing to pay either \$1-\$10 per month /1€ - 10€ per month for their ideal digital music service as described, followed by 19.8% indicating they would be willing to pay \$11-\$20 per month /11€ - 20€ per month for their ideal music service. In total, the results suggest **nearly 70% of respondents are open to the idea of paying a music subscription fee**. 400 responses were recorded describing various qualities respondents consider desirable in a digital music service, bringing forth many intriguing viewpoints. Many of the central themes are described below in the next session, Discussion.

<sup>109</sup> When computing these percentages, votes falling in the “N/A” category were not counted.

**Figure 12: Based on your idea of an ideal music service as you indicated above, what is the maximum amount of money you would be willing to pay per month for this service?**



#### **d) Discussion**

##### Easy And Free – The Way They Want You To Be

When framing the topic of research, the original stated focus was to identify possible improvement areas for digital music services in an effort to potentially increase consumers' willingness to pay for them. Our assumptions about how to improve revenues for digital music services were challenged when survey results indicated the top three dominant methods consumers use to access music - Spotify, Torrents / P2P file sharing and YouTube - are either natively free or have a free option. With much of the discussion amidst the music industry focused on new monetization strategies, the survey results suggest the emphasis may not be best placed on increasing consumers' willingness to pay for digital music offers. Respondents indicated convenience and being free as the most important influences attracting them to their dominant method of accessing music; therefore, making services easy to access and free (or "feels like free") while finding alternative revenue streams may be a more viable, pro-active approach for services without a compelling paid offer. For services choosing to operate on a business model relying on subscriptions, it is imperative to offer compelling, irresistible value in paid offers in order to successfully draw and retain music consumers' interest and patronage.

## Improve The Experience - It's Common Sense

In a world where consumers are accustomed to having access to music for free at the touch of their fingertips, but are also often overwhelmed by the sheer number of choices available to them, digital music services must be perpetually concerned with improving music consumers' experiences in order to differentiate themselves and attract a larger pool of users. As mentioned in the results section, the most popular ratings respondents indicated for fulfillment of their expectations of existing digital music services were 8 (24.9%) and 7 (20.4%), on a scale of 1 to 10. When considering the bigger picture however, the average satisfaction rate is much lower, at just 6.5. Considering this moderate satisfaction rate and results suggesting there is no dominant leader in the delivery of music to consumers, there is considerable room for services to improve customer sense of fulfillment and to increase the share of users that use their service as their number one method to access music.

There are a number of approaches services can consider to improve customer fulfillment in providing music solutions. A wide range of feedback was received regarding qualities an "ideal music service" would have, yet a few popular themes emerged. Some comments related to enhancing user interface and features: "...Way better filtering and music organization options. Way better recommendation algorithms... Smart separation of artists with the same/similar name. Automatic notices of catalog updates for artists in playlists." Others commented on music discovery related to regional/geographical trends. "Music preferences integrated city-by-city with local music and venues." Others suggested ways to make services feel less "cold" and feel more like a natural listening and discovery experience: "A service that did not feel like a service, rather a portal to your own curated music collection. Included album art, liner notes, and other experiences that made music consumption feel more tangible (like own a record collection & all its artwork) rather than just streaming mp3s in the service client's environment." Another respondent expressed desire for the in-store browsing experience to be replicated: "...No one's done it, but it doesn't seem impossible to replicate the corner-of-your-eye 'ooh, what's this?' moment on-screen...."

A second theme that emerged highlighted the importance of a more fluid music experience. Many referred to better connectivity and compatibility with outside networks - "Can pull in my musical preferences across devices and sites/platforms.... blogs, youtube, tweets, etc"; "Better linking with artist websites, current artist news and touring information". Others want improved integration with the overall social music ecosystem - "...Well linked to other services and shops, like concert tickets distributors"; "Integrating all parts of an artist into one place. Download music, stream music, buy show tickets, read their blogs, etc., all in one place...". The apparent demand for a music platform offering a seamless experience of music discovery with an integrated storefront offering music goods and services suggests a compelling consideration for existing and future digital music services.

Another theme arising from the suggestions pertained to all around flexibility, specifically related to pricing, formats and device compatibility. Many advocated for pay-what-you-want models and expressed yearning for access to higher quality music (often referring to streaming and downloading legal music at 320kbps) across multiple devices.

Finally, a considerable number of comments referenced artist compensation. Many respondents expressed a desire to “pay artists directly” or give them “the majority of money”. One could interpret an interesting paradox emerging from the survey results; consumers value digital music services that are free or give them the option to pay what they want, but they also are concerned about artists being paid fairly. One respondent made an interesting comment related to price and the compensation of artists, stating that the price of music should “...be both low enough to encourage people to abandon torrenting but high enough that artists get a fair share of the profits.” A future analysis could be conducted to determine the feasibility of a digital music service with a business model that could both deter people from torrenting and compensate artists fairly. Considering many music consumers’ general impression (fueled by a plethora of stories in media) that artists are not paid fairly, it would be in the best interest of digital music services to employ a transparent business model that gave music consumers confidence the service compensated artists fairly: one respondent urged “A service that allows a connection to the musician; that allows the listener help the musician; a service that concentrates on the music BEFORE the profit model (and thus makes the listener WANT to pay); a service that also provides information to the musician in a statistical manner; and a model that is ethical to all parties. Yes: this is realistic & possible - it just requires a desire to make it happen.”

Without improving the consumer’s experience and taking advantage of opportunities to differentiate, digital music services run the risk of becoming a past “flavor of the month”<sup>110</sup> and being put aside once a new service comes along offering a more compelling value proposition, although some consumers will be reluctant to rebuild a music library in another service. With so many competing channels offering access to music and reports of technology giants Apple and Google (via the YouTube brand) on the verge of entering the subscription streaming game as soon as this year, existing and future music services need to focus efforts on making their offers irresistible to music consumers. This will be the most prevalent challenge facing digital music services once the major smartphone manufacturers begin shipping devices bundled with their own pre-installed streaming services. Offers from Apple and Android (Google) will be more convenient to use and the profitability of the services would be largely irrelevant due to the muscle of the larger companies.

### Music vs. Movie Subscriptions

As the business of both music and film is rooted in the basis of copyright and both have faced similar issues with online piracy, one may wonder why the movie subscription business has found more success than the music subscription business (31.74% of survey respondents indicated they pay for a movie streaming service, compared to 21.24% indicated they pay for a music streaming service.) Below are three possible reasons contributing to the higher success of movie subscription rates over music subscription rates.

1) The experience of film often tends to be more of a novelty and generally a more communal form of entertainment - people often get together to watch something, be it family

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<sup>110</sup> Flores, Joey. “Why Music Startups And Ad Networks Suffer From ‘Flavor Of The Month Syndrome’,” *hypebot*, 2012, <http://www.hypebot.com/hypebot/2012/10/why-music-startups-and-ad-networks-suffer-from-flavor-of-the-month-syndrome.html> (17 April 2013).

or friends. A subscription service positively affects the social viewing experience as groups of people can choose together from a variety of options what to watch without entering a rental or retail store. Contrast this with a music subscription, where there is not much community value added by having a subscription. It may be a less special experience to sit with your friends in the living room and listen to music on a paid subscription account, or while you cook dinner in the kitchen. Music consumption tends to be far more frequent and less novel of an experience when a subscription is involved, thus contributing to peoples' lower willingness to pay for them in comparison to movie subscriptions.

2) Due to technological developments and subsequent effects on music consumption habits within the last fifteen years, many creators and consumers alike have decided that "music is (or should) be free". With the advent of Napster in 1999, consumers began experiencing music for free for a few impressionable years, while record labels shuffled their feet failing to provide an *attractive* legal alternative to appease consumers' demands for digital music. The release of Apple's first generation of the iPod in 2001, the first widespread commercially successful portable media player, further encouraged consumers' appetite for digital music. Finally in 2003, Apple launched the iTunes Store (originally known as the iTunes Music Store), providing a legal and convenient way to download music. By then, however, illegal file sharing had taken its toll, and consumers became accustomed to accessing music for free. As a result, more content creators began releasing their music for free due to a perception that music consumers are unwilling to pay for it, and would either illegally download it or not hear it at all. This in turn has perpetuated consumers' assumption that "music is (or should) be free", and continues to influence creators to offer their music for free or at a price specified by the consumer because its perceived value is at or close to zero. Movies, on the other hand, are generally perceived to have a higher value; not often do you hear "movies are (or should) be free". This may result from the nature of movies as a comparatively far more expensive form of entertainment to create and distribute, even with advances in technology within the past two decades. (It is extremely difficult to create and distribute a professional-looking and sounding movie with an amateur budget and relatively inexperienced personnel.) Music, on the other hand, can be produced at a professional-sounding level by nearly anyone with a limited budget and barebones equipment in their bedroom.

3) Movie subscriptions and rentals have existed for far longer than music access models. Video rental stores opened in the 1980's, allowing consumers to become accustomed to the concept of renting content. In the late 1990's, Netflix began as a DVD-by-mail subscription service (with the intention of becoming a streaming service as bandwidth grew), further entrenching this mindset. Conversely, music subscriptions did not launch until the early 21<sup>st</sup>-century, and did not become mainstream until 2011 when Spotify's integration with Facebook raised the awareness level. Therefore, the public has generally not had as much time to accept and adopt the subscription model for music.

In perspective, movie subscription services could be more popular than music subscription services because of a higher perception of value and/or due to a longer uptake period; music consumers may be less likely to consider a paid digital music solution due to a vicious cycle perpetuated by consumers and creators alike that music is essentially free and far cheaper to produce and distribute than in the past. For subscription rates to music services

to improve, the consumer must see significantly added value to the music experience from the subscription.

### **e) Conclusion**

A complex challenge is at hand in the digital music paradigm to find business models that satisfy all parties involved. Rightfully so, all music industry stakeholders want to be compensated fairly, while a growing proportion of consumers increasingly demand a better music experience, and expect music to be available in a wide range of formats, easy to access across multiple devices, and free. As circumstances in the music ecosystem are incredibly varied and diverse, there may not be a paramount solution for the entire industry, but the ongoing facilitation of ideas and concerns is indispensable in working towards desirable circumstances for everyone. Technology and platforms will continue to improve, and hopefully alongside them, consumer satisfaction.

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