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“Running to Stand Still: Change and the Music Industry” and DJ Beatsmith Presents

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Running to Stand Still: Change and the Music Industry

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Those who bemoan the collapse of the music industry are misinformed. As the *Economist* poetically puts it, "The music business is not dying. But it is changing profoundly," ("Having"). The music industry, and specifically the recording industry, has always gone through changes. However, the end goal was always to sell records. As Paula Swatman and others write in *Internet Research*, "The history of the traditional music market is essentially aligned with that of the recording industry more generally," ("The Changing"). In his book The Future of the Music Business, author Steven Gordon implicitly refers to the importance of record sales in the old music industry model when he writes, "…superstars…were selling tens of millions of records. An album may take a million dollars to produce and a couple more million to market and promote. But if a record sold, for example, at $7 dollars wholesale, the payoff for a successful album was spectacularly lucrative," (84). He continues on to note how in the late 1980's, record sales at CBS records exceeded $2.5 billion (84). While neither author explicitly states that album sales accounted for most of the profit garnered by the music industry, I believe that a reasonable person can infer this to be the case from these two examples and practical experience.

Now, as many have noted, the entire business model is changing. Writes Gordon, "Whatever problems the music industry may face at this time, music itself is in fact more popular, more diverse and is being listened to by more people than ever…What the crisis in the recording industry does mean is that the traditional music business is being replaced by something else," (84). At present the music industry's revenue comes from a variety of sources aside from album or single sales (Ripley, "Music Publishing"). As Kathleen Ripley says in her report on the music publishing industry, "…during 2008 and 2009 the music industry became more flexible, adapting its business model in order to meet consumers' rapidly changing needs.

Publishers and labels have adapted by…moving away from digital rights management (DRM), permitting single-song downloads, releasing interactive applications, launching remix contests, streaming music to phones, and allowing video sites like YouTube to monetize infringement," ("Music Publishing"). I aim to examine both the early, record-sales driven era of the music industry, and the new models that are being adopted, in more detail as I continue.

Michael Fink's book, Inside the Music Business, does a nice job of describing the early history of the music industry. Thomas Edison invented the cylinder phonograph in 1877, but his invention was replaced in time by the disc phonograph, invented by Emile Berliner (3-4). The phonograph proved to be the medium of choice until the advent of radio (6). Writes Fink, "On the radio, listeners could hear constantly varying programs without relying on private record collections…In a few short years radio became a giant industry, at first dwarfing and later absorbing the record business," (6). An electrical method of recording was invented in 1924, which resulted in more pleasing recordings (6-7). Fast forward to 1947, when magnetic tape was introduced to the recording industry (12). As Fink states, "…in less than two years tape completely replaced direct-to-disc wax master recording. The advantages of tape were irrefutable: ease of setup, almost unlimited length of record/play time, immediate playback, ease of editing, and the future possibility of multitrack recording," (12). This was followed by the release of LPs, which finally settled into uniform 45 and 33 1/3 rpm speeds (12).

The arrival of TV was the next big development to change the recording industry (13). However, "The onslaught of TV…affected record sales, but not as drastically as had been expected," (13). This is due to the fact that radio stations began utilizing the, "Top 40" format, in which, "Frequency of airplay became one of the intrinsic measures of a new record's success. Radio, which in the early 1920's had nearly destroyed the record business, now owed its own recovery as something of a promotional tool for the recording industry," (14). However, unlike in the present day, the only option for someone to own the song was to legally buy the record. In this way radio served to boost album sales.

While the recording industry continued to undergo changes, the ultimate goal continued to be selling records. Amusingly, Fink's work, written in 1989, espouses the huge effect CD's had on the music industry, which we now know to be relatively short lived. According to Fink, "In the CD's first four years, sales in the United States soared from 800,000 to 53 million units. This momentum increased even more in 1987 and contributed significantly to a total of $5.57 billion sales of all recorded audio products, the highest figure posted since 1978," (26). Again, we see that physical album sales provided much of the music industry's revenue. The medium keeps changing, but the fact that sales of physical copies of music were paramount has not changed. It is true that music videos reached the height of their popularity in the 1980's as well, but they still served as a catalyst for record sales. Writes Dick Weissman in The Global Music Industry, MTV, "…during its heyday in the late 1980s was an important promotional tool for record companies. Music videos were touted as a unique art form, and a few of them…became best sellers on their own and stimulated album sales," (39).

Some may claim that other facets of the music industry, such as concerts, were in fact where the music industry derived most of its income during this period. However, this is not true. Returning to the *Economist*, we see that, "The misery of touring was once a familiar musicians' gripe, inspiring songs from the Rolling Stones' 'Torn and Frayed' to Ice-T's 'Lifestyles of the Rich and Infamous'. But those songs were written in the days when touring was a way of marketing recorded music," ("Having"). So, according to the *Economist*, touring was not a main source of income in itself, but rather a promotional tool for album sales.

So what happened to change the traditional model of record sales? One answer is the rise of music piracy and peer-to-peer file sharing. Writes Gordon, "In the late 1990s, Napster started to gain popularity and users beyond the small group of college students who adopted it in its infancy. It was no big deal until record company executives found out that people throughout the country…were downloading hundreds or thousands of songs for free," (86). The result was, "…an approximate total decline of 25 percent in CD sales," between 1999 and 2005 (Weissman 15).

Gordon lays out nicely the record companies' response to these events in his book. Basically, A&M Records sued Napster, the first P2P file sharing service, and won because, "…Napster was able to control, access, or block infringement by end users," (86). Napster knew who downloaded what material, and because they did not do anything to discourage the downloading of copyrighted works, they were found guilty. However, the next batch of P2P services found a way around this. Writes Gordon, "Just like Napster, these services allow(ed) people to trade music files without paying a cent, but unlike Napster they proved to be more resilient to the labels' legal fire power. This is the reason why: these services did not control a central data base or index where every song was available. Instead they merely allowed people to download software that allows their subscribers to trade files directly with each other," (87). This loophole meant that the record companies were unsuccessful in their litigation (87). They were similarly unsuccessful in targeting individual end-users and the broadband internet providers (87-88).

People are still illegally obtaining music online today. According to a 2010 *Times* article, 50 million people still use Limewire, and BitTorrent, another file-sharing service, "…has an installed base of 80 million users," (Grossman). In addition, according to the IBISWorld report on major label music production, “The IFPI estimates that 95% of music downloaded worldwide online is done so illegally,” (Ripley, “Major Label”). This indicates that these services are not going away. In addition, some claim that music piracy isn’t the real problem. According to Ripley, “Despite popular belief, the greatest challenge facing the industry is not piracy but the associated lower value that consumers now place on recorded music,” (“Major Label”). Why pay for music when it can be obtained for free from so many places?

As one could imagine given the circumstances, major labels are feeling the heat from industry changes. In fact, the major label recording industry has experienced negative revenue growth since 2005 (Ripley, “Major Label”). So what have industry players done to be successful in this new environment? What options exist that haven’t been tried yet? The answer brings to mind the phrase, “The more things change, the more they stay the same.”

For example, physical CD sales still account for 54% of major labels’ revenue (Ripley, “Major Label”). Even after all the advances in technology, and all the new ways record companies are presenting music to the public, the workhorse is still the physical album sales. At the same time, the report notes, “Digital music formats have increased from a negligible percentage of industry revenue in 2003 to comprise 51.0% of total recorded music purchases in the U.S. in 2010…,” (Ripley, “Major Label”). Included in this categorization are digital album and single sales, mobile music downloads, and digital performance rights and subscriptions (Ripley, “Major Label”). Obviously, the major markets are beginning to embrace the digital revolution and use new technology to their advantage. However, “…revenue from digital music sales has yet to come close to recouping the losses from traditional sales,” according to the IBISWorld report (Ripley, “Major Label”).

The use of digital technology is not the only way the major labels have adapted to their changing environment. The IBISWorld report also mentions the increased popularity of "360" deals between the artist and the label (Ripley, "Major Label"). In an article in *Fortune* magazine, A&M/Octone founder and CEO James Deiner explains what is meant by "360," (Kimes 100). According to the article, "…the label takes a cut of all revenue streams, including merchandising, touring, and licensing," (Kimes 100). The upside of this is that, "If you sell 200,000 albums but you also have licensing and publishing, it's the same economics as a gold record," according to Josh Deutsch, quoted in Kimes' article (Kimes 100). So, you can sell fewer records than you would traditionally have to, yet make the same amount of money.

What exactly is licensing, one may ask? Licensing is one branch of the music publishing industry, an industry of companies that, according to Ripley, "…work for musicians, songwriters and composers. They are responsible for licensing the intellectual property of their clients and ensuring that royalties are collected," ("Music Publishing"). According to Ripley, this sector of the music industry, "…is managing to buck the trend of rapidly falling revenue that is occurring elsewhere in the music business, so much so that revenue is expected to grow by 2.0% annually in the five years to 2010 to $4.9 billion," and reach $5.8 billion by 2015 ("Music Publishing"). The biggest source of revenue for the publishing industry is mechanical royalties (Ripley, "Music Publishing"). According to Jay Schornstein, author of a website about music and intellectual property law, "Once a songwriter's composition has been recorded and distributed to the public, copyright registration entitles the songwriter to (mechanical royalties) whenever that songwriter's composition is further recorded…The company putting out the record is required to pay the songwriter a mechanical royalty for each song manufactured," (Schornstein). In other words, any time an artists' original song is remanufactured, for example as part of a compilation, the artist gets money. The next biggest segment of publishing revenue comes from performance royalties, which is money paid to artists' when their tracks are played over the radio, on television, or streaming online (Ripley, "Music Publishing" and Schornstein).

It's not surprising that record companies want a cut of the profits from licensing, considering how successful the publishing industry has been in the past few years. However, it isn't only record labels that are experimenting with new ways to utilize licensing deals, but the artists' themselves. Author Bethany Klein discusses the success of electronic artist Moby due to licensing to advertising in the journal *Media, Culture and Society*, writing, "Moby's success validated advertising as a launching pad for lesser-known or new musicians in both the independent and major music worlds," (463). She claims that this allows artists to become popular in an age where increased homogenization of mainstream radio means that unknown artists have difficulty getting heard (465). Klein continues, writing, "Licensing to advertising is seen not only as a way for reaching the ears of potential buyers, but also a way to reach the ears of radio programmers. As closed off to risks as radio may be, tracks that create a buzz through their…commercials can jump the line and be added to radio playlists," (467). However, Klein states that licensing typically does not help an artist achieve greater success. As she puts it, "The suggestion that exposure can lead to hits relies on the expectation that, through licensing, artists will see an increase in record sales, ticket sales, or other licensing opportunities and radio play…In reality, licensing to advertising does not guarantee any of these benefits and, more often than not, artists see little to no change in record sales and radio play," (473). However, it is important to keep in mind that we are examining licensing as a revenue stream, not as a means of boosting an artist's profile.

Revenue from live concerts appears to be another steady stream of income for the music industry. According the IBISWorld report on US Live Music, Sports and Event Promotion, the industry has experienced positive growth every year except 2010 (Ripley, "Live Music"). Live concerts make up 58.1% of this industry categorization (Ripley, "Live Music"). In addition, the industry is expected to experience roughly 2-4% growth over the next few years (Ripley, "Live Music"). According to IBISWorld, "Consumers' willingness and ability to attend events is heavily influenced by their disposable income. Because events are an affordable luxury compared to vacations and Americans have clearly expressed their love for live entertainment, this industry is expected to thrive as consumer pocketbooks bounce back from recessionary lows," (Ripley, "Live Music"). So it appears that live music will remain a steady positive in the midst of the changes racking the industry.

Digital sales, licensing, and live music appear to be areas that can provide some relief from the economic malaise currently affecting the music business. However, John Gordon has another solution, one that directly challenges the problem posed by the illegal downloading of music. He proposes that it be made legal. Writes Gordon,

> The solution to the music industry's woes is a federal law providing for a statutory license that would legalize the sharing of music online while compensating copyright owners for lost sales. A federal law implementing a statutory license could legalize the transmission of all recorded music for purposes of sharing music over the Internet and downloading permanent, portable copies. Fees would be paid by those directly profiting from file sharing, that is, the makers of CD burners, including computer manufacturers, and the Internet service providers (ISPs) whose subscribers already pay in part for access to such services as Kazaa. As CD sales continued to decline due to an ever-increasing number of households acquiring computers and high speed Internet connections, the amount payable to the fund could be adjusted upwards (93).

Basically, Internet service providers and electronics manufacturers who profit from the illegal pirating of music would have to pay a tax on their products. Users could then download any song legally, and those corporations taxed would pay the artists depending on how many times their songs were downloaded (99). This idea, while not conventional, does have some merit.

Gordon wrote this book in 2005. Unfortunately, as of right now, it doesn't appear to have gained traction.

A second idea that Gordon mentions is for ISP's to charge their users more for special accounts that would allow them to download music without worrying about suffering legal action from the record companies (104). He calls these accounts, "Bandwidth Levies," (104). Writes Gordon, "At least one major ISP, Verizon, publicly announced that they would consider paying such a levy if the record labels agreed to stop suing their customers. The record companies have not publicly supported such a levy to date," (104). Unfortunately, then, this idea appears to be a non-starter as well.

The music industry is undoubtedly not at its strongest. It has suffered from the digital piracy threat because, as Gordon writes, "…the labels were not focused on creating the future… (they) were too busy trying to kill the future," (89). In other words, instead of embracing the new technology that arrived at the beginning of the century, they tried to keep it at bay while continuing with their outdated model of business. However, they appear to have realized their mistake and are now embracing digital means of delivering music to their customers. In addition, they are exploring other ideas, such as "360" deals and licensing, to stay competitive. As long as the industry continues to embrace change rather than forestall it, I believe it will be successful in the future.

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