

Digital Music Report 2012

Expanding Choice. Going Global



representing the
recording industry
worldwide

Contents

Introduction	3	Focus on France	20
■ <i>Plácido Domingo, chairman, IFPI</i>		■ <i>Hadopi: "Positive impact for years to come"</i>	
■ <i>Frances Moore, chief executive, IFPI</i>		■ <i>The independent's view: Innovation and "meaningful sanctions"</i>	
Artist voices	5	Focus on the US	21
Digital Music: Expanding Choice. Going Global	6	■ <i>ISP agreement and strong digital growth</i>	
■ <i>Executive Summary</i>		Focus on South Korea	22
■ <i>Global digital growth rate accelerates</i>		■ <i>A continuing success</i>	
■ <i>The global top selling digital singles of 2011</i>		Developing a legitimate business in China.....	23
■ <i>Access or ownership? You choose</i>		■ <i>Major record companies license Baidu</i>	
■ <i>Global expansion</i>		Protecting content online: Intermediaries step up.....	24
■ <i>Progress against piracy</i>		■ <i>Search engines should link to legal music</i>	
■ <i>Intermediaries have a key role</i>		■ <i>Advertising: Cutting the funds to piracy</i>	
The business models of digital music.....	10	■ <i>Payment providers act on illegal sites</i>	
■ <i>Downloads break through borders</i>		■ <i>Hosting providers: A key partner</i>	
■ <i>Digital album demand alive and kicking</i>		Self-Help: Anti-piracy enforcement and education.....	26
■ <i>The rise of subscription</i>		■ <i>Tackling the pre-release hackers</i>	
■ <i>Subscription reaches new consumers</i>		■ <i>Public education: a long term commitment</i>	
■ <i>Bundling music – a route to the mass market</i>		■ <i>A Guide to Music, Film, TV and the Internet</i>	
■ <i>Internet radio continued to expand</i>		Digital Music Services Worldwide	28
■ <i>Music video meets strong consumer demand</i>			
The art of digital marketing.....	14		
Piracy: Improved cooperation from online intermediaries.....	16		
■ <i>A rigged market</i>			
■ <i>Books feel the impact</i>			
■ <i>ISPs: The needle is moving</i>			
■ <i>Progress in Europe</i>			
■ <i>New study assesses the effect of graduated response</i>			
■ <i>US and New Zealand: ISPs engage</i>			
■ <i>Moves to block "rogue websites"</i>			
■ <i>Evidence of site-blocking impact</i>			

A digital world that rewards artists and creators

By Plácido Domingo, chairman, IFPI



Plácido Domingo. Photo by John Marshall

Plácido Domingo was appointed chairman of IFPI, the organisation that represents the recording industry worldwide, in July 2011.

Domingo is a world-renowned, multi-faceted artist. Recognised as one of the finest and most influential singing actors in the history of opera, he is also a conductor and a major force as an opera administrator in his role as general director of the LA Opera.

I accepted the invitation to become chairman of IFPI in 2011 because I wanted to help improve the very challenging economic environment which musicians – young and old – everywhere face in their careers today.

We all know the music industry is in a period of dramatic change. Much of this is cause for optimism and opportunity, as the Report that follows suggests. Thanks to the amazing technology of the internet, the audience for recorded music is fast-expanding across the world. Artists who might not otherwise find a way to make their music available can take advantage of the new ways to distribute music the internet offers.

At the same time policymakers better understand that the internet does not make music “free”. There is greater acceptance of the need for good and fair copyright laws to stop the infringement of artists’ and producers’ rights. A widening circle of vital partners in the internet world are cooperating in stopping piracy.

As a passionate supporter of the music industry, I welcome these changes. However, it is fundamental that artists and creators, and the producers that invest in them, should be rewarded for their work in the digital environment just as in the physical world. Governments and legislation have an essential role to play. I only have to look at my native Spain – where piracy has had a terrible effect on everyone’s royalties and the labels’ investment in artists – to see the extent of the challenges we face.

A world where copyright is properly respected brings income to artists and producers and investment in artists of all genres. It also delivers jobs, growth and tax revenues. And, of course, it also brings an enormous amount of pleasure to billions of people. As its chairman, I am trying to help IFPI in its efforts to create an environment in which the public can enjoy the benefits from a successful digital music sector.

A handwritten signature in black ink, consisting of a large, stylized 'D' followed by a series of loops and a long horizontal stroke.

Plácido Domingo

Digital Music in 2012:

Optimism Justified. Complacency not Accepted

By Frances Moore, chief executive, IFPI



Looking through the pages of this latest IFPI Digital Music Report, you see a striking paradox: on one hand, there is the innovation and drive of a business that has led the way for creative industries in adapting to the digital age; on the other hand, the extraordinarily difficult environment in which these changes are taking place.

This is the ninth report that we at IFPI have produced documenting the evolution of the digital music sector worldwide. It has been a challenging and often painful transition, but as we enter 2012, there are reasons for real optimism. The digital music business has now reached out to encompass the globe. The largest international legitimate digital music services are present today in no fewer than 58 countries – this number has more than doubled in the last twelve months.

Consumer choice has been revolutionised, as new models for consuming and accessing music are rolled out in new and existing markets. The number of paying subscribers to services such as Spotify and Deezer has leapt in the last twelve months, from an estimated eight to more than 13 million. At the same time, cloud-based services, such as iTunes Match, have become a reality in the marketplace, helping drive the popularity of music downloading.

With a healthy 8 per cent increase in our digital revenues in 2011 – the first time the annual growth rate has risen since records began in 2004 – some might feel tempted to say that a troubled era for the music industry is coming to an end. Such complacency now, however, would be a great mistake.

The truth is that record companies are building a successful digital music business *in spite* of the environment in which they operate, not because of it. Figures in this report show that more than one in four internet users globally regularly access unlicensed sites that contain copyrighted music. This is a startling statistic that captures the challenges we face in developing a sustainable legitimate digital music sector.

We are undoubtedly making important progress in changing this environment, dealing with both peer-to-peer (P2P) and other forms of digital piracy. In the US, music and film companies have agreed with ISPs a new copyright alert system. In France, the Hadopi law has been successfully implemented and research shows it is accepted and having an impact on consumer behaviour.

South Korea, a pioneer of anti-piracy legislation which has required an effective role from ISPs in stopping infringement, is seeing continued market health. New Zealand implemented a new graduated response law in 2011 and surveys show it is already affecting consumer behaviour positively. In Europe, a series of successful court actions required ISPs to block access to The Pirate Bay, prompting substantial reductions in users of that service.

On top of this, there is a “new frontier” in our work against piracy. Cooperation from a far wider circle of technology and business partners, from advertisers to search engines, is now needed to deal with the problem. In 2011, we made significant progress with these intermediaries. A ground-breaking three-way collaboration between payment providers, IFPI and the City of London Police has helped cut funding to 62 illegal websites. That is a positive model that can be extended to new forms of piracy in the future.

The role of search engines in relation to piracy will be a key priority in 2012. Google and other search engines are an important access route for those looking for unlicensed music on the internet. Our industry has stepped up cooperation with search engines in the last year, but a lot more cooperation is needed, such as prioritising legitimate sites in search results and helping prevent the funding of illegal sites via advertising.

The music industry has grasped the opportunities of the digital world in a way few, if any, other businesses can claim to have done.

Despite the challenges ahead, the optimism for digital music going into 2012 is well-justified. The music industry has grasped the opportunities of the digital world in a way few, if any, other businesses can claim to have done. Our digital revenues, at one-third of industry income (and now more than 50 per cent in the US), substantially surpass those of other creative industries, such as films, books and newspapers.

The music business is a dynamic contributor to the digital economy. Yet it can be much more than that, delivering sustainable growth and jobs. This cannot be done through innovation and licensing alone. We need a fair legal environment, effective cooperation from intermediaries and a resolute commitment from governments to use legislation to curb all forms of piracy. These are the priorities we will be pushing for in 2012.

Artist voices



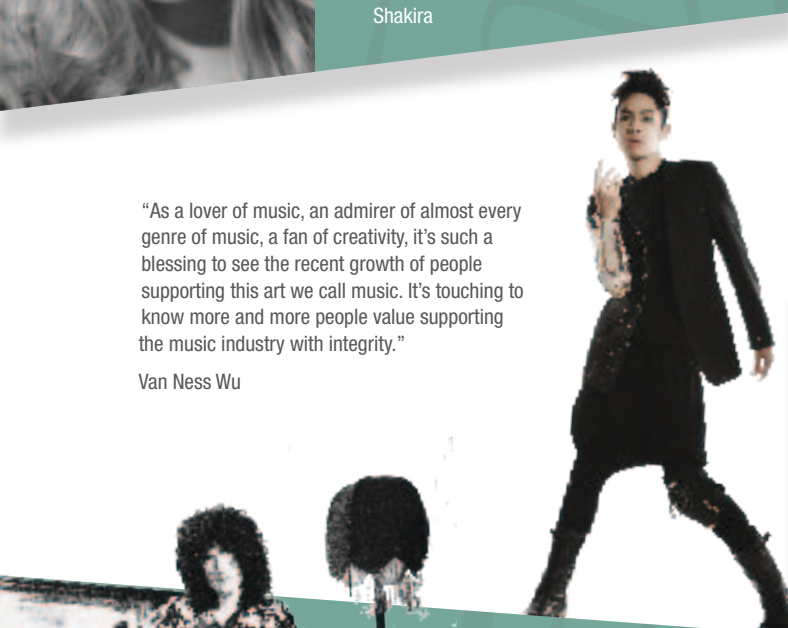
"The creation and recording of a song is the result of the work and talent of many: composers, musicians, arrangers, engineers, assistants, producers. Each day there are more and better digital services to help us enjoy the wonderful music created throughout the world. To consume music legally protects and respects the work of each and every one of the people involved in its creation and recording."

Shakira



"The digital age has brought about a way of consuming music and connecting with your fan base that is unprecedented. Partnering and working closely with digital platforms allows us ways and means of connecting with our fan base which in turn creates greater exposure and generates sales."

Professor Green



"As a lover of music, an admirer of almost every genre of music, a fan of creativity, it's such a blessing to see the recent growth of people supporting this art we call music. It's touching to know more and more people value supporting the music industry with integrity."

Van Ness Wu

"I love the way music turns all these techie devices like PCs, mobile phones and iPads into personalised juke boxes and I love how the internet lets me connect with fans wherever they are in the world."

Natasha Bedingfield



"There has been tremendous growth with new digital channels and streaming services. These new business partnerships have the potential to help turn around our business. We must create an awareness with the public to realise the tremendous damage that has been done to our industry, artists & consumers. We must fight to ensure that the next generation of artists can survive & flourish into the 21st century."

Lee Ritenour, guitarist/artist

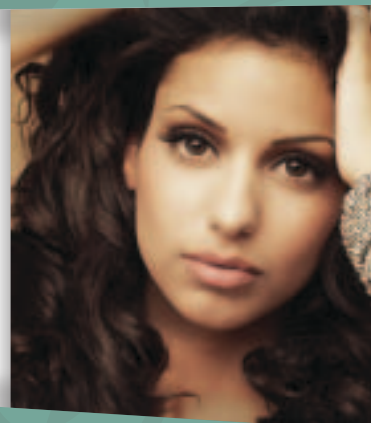


"Music is available to everyone at the touch of a button. Please try and only use those services that actually pay the artists, songwriters and producers, rather than those that don't."

Queen

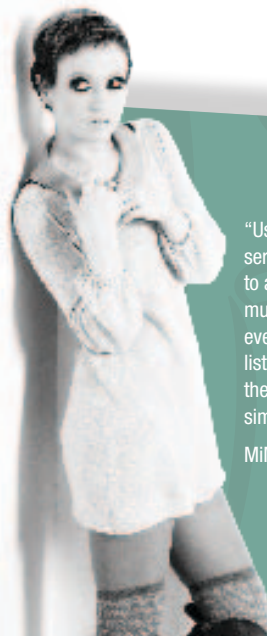
"It's fantastic that fans can listen to all the music they want for a good value-for-money price. This is the future and I am so happy that my music can be listened to in France but also across the world thanks to those new music services."

Tal



"As artists who spend much time on the road we applaud the possibilities available today of having legal and fast access to so many kinds of new, inspiring music."

Frida Gold



"Using many of the new music services allows us all to be able to access a treasure trove of music; new, old, forgotten or even undiscovered. It gives the listener the power to express themselves and explore or simply find old favourites."

MiMi

Digital Music: Expanding Choice. Going Global

Executive summary

The digital music sector is pushing the limits of consumer choice, extending its business models and reaching out to consumers across the globe. Digital channels have overtaken physical formats to become the dominant revenue stream in the world's largest market, the US. And the digital music market is poised to further expand its reach internationally in 2012.

Despite the huge challenges outlined elsewhere in this report, there is a mood of optimism in digital music at the start of 2012. Download services are seeing continued strong consumer demand and are expanding their customer base, particularly in previously untapped developing markets. Meanwhile, a fast-growing number of consumers are using subscription services and other models. "There's a race among the services to go global and plant the flag in new territories," says Stephen Bryan, executive vice president, digital strategy and business development, Warner Music Group. "We're seeing services that are generating revenues and growth. There is high engagement with these services. Consumers love them and spend hours using them."

Global digital growth rate accelerates

Digital music revenues to record companies grew by 8 per cent globally in 2011 to an estimated US\$5.2 billion. This compares to growth of 5 per cent in 2010 and represents the first time the year-on-year growth rate has increased since IFPI started measuring digital revenues in 2004. Digital channels now account for an estimated 32 per cent of record company revenues globally, up from 29 per cent in 2010. Some markets now see more than half of their revenues derive from digital channels, including the US (52%), South Korea (53%) and China (71%). IFPI estimates that 3.6 billion downloads were purchased globally in 2011, an increase of 17 per cent (combining singles and album downloads).

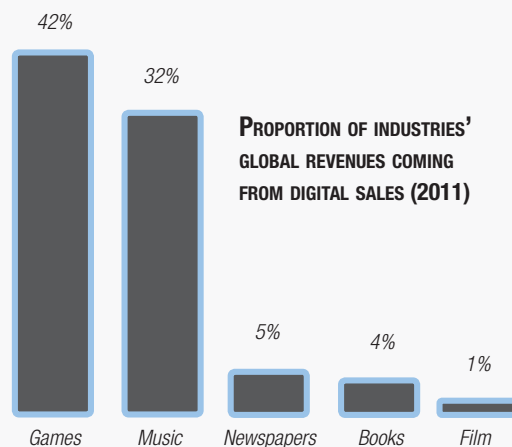
At a time when other creative industries, in particular film, newspapers and book publishing, are only now rapidly shifting to online and mobile channels, the music industry's level of digital penetration still dwarfs that of all other comparable sectors, except games.

COUNTRY	% OF RECORD COMPANY REVENUES FROM DIGITAL SOURCES
CHINA	71
SOUTH KOREA	53
USA	52

Source: IFPI estimates, 2011.

“We have really only scratched the surface of digital music in the last decade – now we are starting the real mining, and on a global scale.”

Rob Wells, president, global digital business, Universal Music Group.







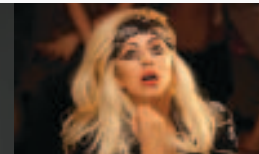
Sources: PWC Global Entertainment & Media Outlook and IFPI. Notes: games includes players' purchases of accessories and additional game content as well as subscriptions. Music share is based on trade revenues. Newspapers include digital advertising and subscriptions. Books excludes audio books. Film excludes online sales and rentals of physical discs.

“There's a race among the services to go global and plant the flag in new territories. We're seeing services that are generating revenues and growth.”

Stephen Bryan, executive vice president, digital strategy and business development, Warner Music Group.

The global top selling digital singles of 2011

The top selling single of 2011 was Bruno Mars' *Just The Way You Are*, which sold more than 12.5 million copies. The combined sales of the top ten digital singles grew by 11 per cent in 2011.

				
ARTIST	TITLE			SALES (M)
BRUNO MARS	JUST THE WAY YOU ARE			12.5
BRUNO MARS	GRENADE			10.2
LMFAO	PARTY ROCK ANTHEM			9.7
JENNIFER LOPEZ	ON THE FLOOR			8.4
ADELE	ROLLING IN THE DEEP			8.2
LADY GAGA	BORN THIS WAY			8.2
PITBULL FT. NE-YO, AFROJACK & NAYER	GIVE ME EVERYTHING			8.2
BLACK EYED PEAS	THE TIME (DIRTY BIT)			7.3
MAROON 5	MOVES LIKE JAGGER			7.0
BRUNO MARS	THE LAZY SONG			6.5

Source: IFPI, 12 months to November 2011. Sales are rounded. Combines all versions of the same song.

Access or ownership? You choose

Certain fundamental factors underpin this growth. First is the continued widening of consumer choice. Digital music is now broadly segmented into two main consumption models - "ownership" and "access". Both took big strides in 2011. Subscription services expanded and linked with new partners to reach new audiences - most notably integrating with Facebook and bundling their services with ISP offerings. Meanwhile, developments in cloud technology are transforming the way fans manage and store their music.

Music companies believe both models - access and ownership - have enormous growth potential. Rob Wells, president, global digital business, Universal Music Group, says: "The fact that these two models of consumption can co-exist speaks volumes about the future. In fact, we have really only scratched the surface of digital music in the last decade - now we are starting the real mining, and on a global scale."

Also driving growth is the global surge in consumer demand for smartphones and tablets. These, along with steadily growing broadband penetration, are a major factor in the increased uptake of both download and subscription services. "The technology infrastructure is being put in place in a way that we have never seen before and that is one major reason why we feel positive about digital music going into 2012," says Edgar Berger, President and CEO, International, Sony Music Entertainment.

Record companies are working with business partners to create products that can offer a better user experience than unauthorised services. Mark Piibe, executive vice president, global business development, EMI Music, says: "We know that some people will migrate from piracy and that others will not, but we want alternatives to be there. We think the presence of access services can expand the whole market."

“We think the presence of access services can expand the whole market.”

Mark Piibe, executive vice president, global business development, EMI Music.

DIGITAL MUSIC TRADE REVENUES BY YEAR			
	2009	2010	2011
TRADE REVENUES (US\$)	4.6 BILLION	4.8 BILLION	5.2 BILLION
GROWTH	10%	5%	8%

Source: IFPI. 2011 figures are estimates.

At the start of 2011, the largest international digital services were present in 23 countries. One year later they are present in 58 countries.

Global expansion

Digital music retailers are fast spreading their reach globally. At the start of 2011, the largest international digital services were present in 23 countries. One year later they are present in 58 countries.

In 2011, iTunes opened for business in 28 additional markets, now reaching more than 50 countries worldwide, including all members of the European Union. Download service 7digital announced in October 2011 that it was launching new stores in Australia, New Zealand, Malaysia and Singapore. This expansion means 7digital is now available in 37 countries worldwide. Subscription services Spotify, WIMP and Deezer are also expanding fast across national borders. Spotify launched in the US and four European markets and now reaches 12 countries. The US also saw the launch of Muve Music in 2011. Deezer opened its service in the UK in partnership with Orange, and plans to continue to expand globally in 2012.

Latin America

In Latin America, iTunes opened for business in 16 countries in December 2011, following its successful establishment in Mexico in 2009.

US-based subscription service Rdio launched in Brazil in partnership with local mobile operator Oi. The BlackBerry BBM music service became available in Mexico and mobile operator America Movil/Carso's Ideas Musik launched in Mexico and Brazil. Other services, including Google Music, are expected to reach Latin America in 2012.

Record companies have also formed innovative partnerships in the region. Universal Music struck a deal with Peugeot in Brazil, that enabled the car manufacturer to offer unlimited music downloads for a year to consumers who bought a Peugeot 207 Magnetico car. It also joined with computer manufacturer HP to offer unlimited tethered downloads for a year and 120 DRM-free downloads to buyers of several laptop models.

Afo Verde, president, Latin Region, Sony Music, says: "Broadband penetration in Latin America continues to grow and the region has become the number two cell phone market in the world, presenting a great opportunity to expand the digital music business. Subscription services are beginning to take root and we anticipate these will perform well, while download services will benefit from the rollout of cloud technology."

Asia

In Asia, South Korea remains the most successful digital music market, with an estimated three million music subscribers. The most popular service is MelOn, followed by MNET. Taiwan has the recently-launched Omusic, an ISP bundled service. KKBOX, a major service in Asia, is present in Hong Kong and Taiwan, offering streaming and download services.

In China, a market currently throttled by piracy, a landmark partnership was announced in June 2011 between three major record companies – Sony, Universal and Warner – and internet search giant Baidu. Baidu, which previously had a licensing agreement with EMI, said it would close its infringing "deep links" service and establish a new authorised digital music offering, Ting, as part of the new agreement.



The digital music market internationally remains extraordinarily diverse. "There isn't one single road map of development for all our markets, and every territory is unique," says Wells of Universal. "The way consumers interact with music varies enormously by market. Every country has different economic conditions, and different levels of broadband and device penetration and digital development."

Record companies are now increasingly focused on new developing markets where digital infrastructure is fast-evolving and there is exciting growth potential, provided digital piracy can be effectively tackled. India, for example, has more than 40 million smartphone users and 14 million broadband connected households (FutureSource Consulting Ltd).

Progress against piracy

Despite the big steps forward of 2011, digital piracy remains a critical barrier to growth and investment by record companies. More than a quarter of internet users globally (28 per cent) access unauthorised services on a monthly basis, according to IFPI/Nielsen.

Digital piracy broadly divides between peer-to-peer and non peer-to-peer channels. Cooperation from a range of online intermediaries is needed in response. IFPI advocates an inclusive combination of graduated response, site blocking and other measures.

"You cannot play down the significance of piracy," says Wells for Universal. "Spain, which should be the powerhouse of repertoire for Latin America and the US Latin market, is effectively a dead market. Yet in South Korea, where we have new anti-piracy laws, the market is surging and now spreading its repertoire far beyond its own borders."

There is important progress on piracy. France has successfully implemented its "Hadopi" law, introducing education and warning measures and the threat of sanctions to help migrate users to legal sites. Research shows this is helping change consumer behaviour, while the number of peer-to-peer (P2P) file-sharers fell by 26 per cent within the space of a year (IFPI/Nielsen).

"Hadopi is our chance to revive French digital music in France," says Yves Riesel, founder of indie label Abeille and specialised digital platform Qobuz.

"It's not the only solution, of course, but along with the efforts of platforms and record producers it has given us a chance to reverse the crisis of the last few years."

Similar positive indications come from South Korea, while New Zealand introduced graduated response legislation in 2011 and in the US a landmark Memorandum of Understanding set out a new programme of graduated response cooperation that will be implemented by most major ISPs in 2012. Meanwhile, draft legislation targeting "rogue" sites is being debated in the US. Evidence of the impact of site-blocking comes from jurisdictions in Europe.

Intermediaries have a key role

The fight against piracy is pushing at new frontiers too.

Other intermediaries, ranging from search engines and advertisers, are increasingly getting involved. A partnership between record companies, credit card companies and law enforcement in the UK in 2011 typifies the widening circle of engagement of these third party "intermediaries."

Search engines are a major channel for consumers to access music. However, many of the top results provided by search engines are linked to unauthorised content. Advertisers can also help restrict the funding of illegal sites. Important steps forward were taken in these areas in 2011, but more cooperation will be needed.

The music industry commits considerable resources to anti-piracy actions and public education campaigns. These are part of an industry digital music strategy that is comprehensive and multi-faceted, combining legal offerings, education and enforcement of rights. In 2011, IFPI was able to secure the removal of more than 15 million infringing links, a 115 per cent increase on 2010.

"The technology infrastructure is being put in place in a way that we have never seen before and that is one largest reason why we feel positive about digital music going into 2012."

Edgar Berger, president and CEO, International,
Sony Music Entertainment.



The business models of digital music

Downloads break through borders

Ten years after the first online stores emerged in the US and Europe, the music download sector continues to expand internationally and improve its offer to consumers. Download stores account for a large proportion of digital revenues and account for most of the 500 legitimate services worldwide, offering libraries of up to 20 million tracks. Many major markets are seeing healthy increases in single track download sales, including the US, up 10 per cent (Nielsen SoundScan); the UK, up 8 per cent (Official Charts Company/BPI) in 2011; and France up 23 per cent (GfK). Consumer demand for iTunes, the market leader, is growing healthily.

Streaming from the “cloud” turned to market reality in 2011, with new systems that enhance the way consumers manage and store their music. Leading the way, Apple launched its **iTunes Match** service in November 2011, offering the opportunity to draw more users into iTunes and drive purchasing. iTunes Match enables users to access their music libraries across the full range of devices they own for a fee of US\$25 a year. The service, licensed by international record companies, effectively upgrades a user's music collection and dispenses with the need for them to physically transfer the music files they have bought across the full range of their families' devices. iTunes Match will be available in the new markets worldwide that iTunes is entering.

New major players are following. Google launched a new music service in the US, **Google Music**, in November 2011 for the Android platform. Consumers can purchase individual songs or albums which are then delivered to the cloud from where they can be streamed to multiple devices.

DIGITAL ALBUM VOLUME SALES GROWTH IN 2011	
US	+19%
UK	+27%
FRANCE	+23%
GLOBAL (EST)	+23%

Source: Nielsen SoundScan, Official Charts Company/BPI, GfK and IFPI estimate.

Digital album demand alive and kicking

Digital was once mistakenly feared to be the killer of the album. However, this has proved far from the case. Digital album volume sales have grown steadily in recent years, with US and UK digital album sales in 2011 up by 19 and 27 per cent respectively. (Soundscan and Official Charts Company). In the US and the UK, digital albums already account for 31 per cent and 24 per cent respectively of all albums sales by volume. Consumer demand for an artist's body of work remains strong in the digital world especially as price competition is often fierce and storage on computers and devices is less of an issue.

Several factors explain the strength of demand for digital albums: strong marketing campaigns, premium offerings that provide additional content and consumer habits. Premium albums often outsell their lower priced equivalents in the first few weeks of release, suggesting many music fans appreciate the extra value offered by these products.

The rise of subscription

Music subscription is transforming the way people experience and pay for tracks and albums. It is also a fast-expanding business model. The number of consumers subscribing to music services globally is estimated to have increased by nearly 65 per cent in 2011, reaching more than 13 million, compared to an estimated 8.2 million the previous year. This supplements the tens of millions of consumers who already use download services. “Subscribing to music used to be quite an abstract concept – but now it has become a practical concept. The mass market understands how it works and consumers see the huge benefits,” says Edgar Berger of Sony Music.

Subscription has caught on exceptionally well in some markets, particularly in Scandinavia. In Sweden, for example, subscription accounted for 84 per cent of digital revenues in the first 11 months of 2011, boosted by its national champion Spotify. Other markets saw sharp growth in subscription revenues, including France which saw an increase of more than 90 per cent in the first 11 months of 2011 (SNEP).

There are around 500 legitimate music services worldwide offering up to 20 million tracks.



ESTIMATED PAYING SUBSCRIBERS TO MUSIC SUBSCRIPTION SERVICES GLOBALLY	
2010	8.2 MILLION
2011	13.4 MILLION

Source: IFPI estimates.

The subscription model saw some high-profile advances in 2011, led by Spotify's move into the US and expansion in Europe to 11 countries. **Spotify** reports it has 2.5 million paying subscribers worldwide, including over 400,000 in the US market since its launch there in July. Spotify sees its expansion in the US as a springboard to international markets. Ken Parks, chief content officer, says: "We were very focused on how Spotify, which had been a European service, would translate to the US. Now, having seen the acceptance in the biggest music market, it gives us a huge degree of confidence and optimism to expand elsewhere."

Deezer is a digital streaming service that was established in France in 2007 and is now expanding globally. Since launching its partnership with Orange in August 2010, it has achieved more than 20 million registered users and over 1.5 million paying subscribers.

Deezer opened for business in the UK in September 2011, in partnership with Orange (Everything Everywhere). In late September, the company announced its strategic integration with Facebook, enabling artists and fans to legally share their music and make new discoveries even more easily.

In December 2011, Deezer announced it was opening for business in scores of countries worldwide over the next six months, whether in telecoms partnerships or as a standalone service. It has already launched in more than 25 countries across Europe. By the end of February 2012, it is expected to be up and running in 80 countries across Africa, Australasia and Latin America, with more countries to follow in June 2012. Mark Foster, managing director of Deezer, UK and Ireland, says: "We think in many countries we will be kick-starting the whole digital music sector and early investment will give us a great market position and ensure we achieve strong early growth."

Music subscription is transforming the way people experience and pay for tracks and albums. It is also a fast-expanding business model.

Subscription is arriving or expanding in other markets too. **Rhapsody** announced in December 2011 that it was the first US streaming subscription service to amass more than one million paying customers. Canada-based **Galaxie** launched a subscription based mobile streaming service, while three new subscription services, **JUKE**, **Rdio** and **Simfy**, advanced the model in Germany and Austria.

Norwegian-based streaming service **WiMP** announced in November 2011 that it had more than 350,000 paying subscribers across Norway, Sweden, Denmark and Portugal. Daily streams rose five-fold in Norway in 2011 and two-fold in Sweden and the second half of the year. WiMP has partnered with Norwegian ISP Canal Digital to offer the service bundled with a TV subscription. In three Scandinavian markets it partnership ISP Telenor and in Portugal in partnership with Portugal Telecom. WiMP plans to launch in Germany, Ireland and Benelux in 2012. Per Einar Dybvik, chief executive of parent company Aspiro Music, says: "WiMP is now targeting roll-out in several new markets, using our experience to turn streaming into a success."

In December 2011, **rara.com** announced the launch of a streaming service in more than 20 countries worldwide, including Canada, France, Germany, Mexico, Spain, the UK and US. The service, powered by Omnifone, is aimed at consumers who still use CDs and want a simple way to access digital music through their internet browser. The ad-free service offers more than 10 million tracks from US\$/€/£4.99 for online access and US\$/€/£9.99 for smartphone access, with lower introductory prices for the first three months. rara.com is pre-loaded on the majority of European HP PCs and is also available on Android, iOS and other platforms.



Subscription reaches new consumers

All players in the subscription business agree the “holy grail” is scale. In 2011, subscription services made groundbreaking moves to achieve mass-market reach, most notably through their integration with Facebook, which has propelled music subscription into the environment of social networks. Under Spotify’s partnership with Facebook, new sign-ups to Spotify come through Facebook and users then share their playlists with friends.

Subscription services have brought huge benefits for consumer choice. These often operate a “freemium” business model, aimed at attracting consumers with a “free” advertising-supported offering before migrating them to the “premium” paid-for service. For such businesses, converting free users to paying subscribers is vital to ensuring their sustainability. The free tier of service is effectively their customer acquisition tool. Spotify is seeing a conversion rate of around 15 per cent internationally, but in some markets this increases significantly. There are added benefits from converting to the premium service: no advertising, the ability to use on a portable device or offline and better sound quality. The service claims particular success converting young fans over to its paid-for option: one-third of its US paying subscribers are under 24.

Subscription services have brought huge benefits for consumer choice...converting free users to paying subscribers is vital to ensuring their sustainability.

Music subscription offers a different model of return on investment for artists and record labels. In the à-la-carte environment, an album or track is downloaded once and paid for. In the streaming environment, a track or album may be listened to hundreds of times, each triggering a payment to rights holders. While the individual payment for a stream is lower than a download, the cumulative payment triggered by a consumer repeatedly listening to an album or track may be higher over a longer period.

Bundling music – a route to the mass market

One key route to the mass market for digital services is “bundling” partnerships with ISPs and telecoms companies. These companies have the commercial footprint and billing structure to enable music services to reach a broad audience. ISPs benefit too, attracting customers, reducing churn (customers joining and leaving) and improving network efficiencies.

Stephen Bryan of Warner Music Group says: “ISPs and mobile carriers are aware they need to offer entertainment content to stay relevant. As they see the economic benefits of offering such content they become more willing to tackle piracy and help develop a consumer experience that is a lot better than piracy.”

ISPs and mobile carriers are aware they need to offer entertainment content to stay relevant.

Two of the most high-profile partnerships launching in late 2011 were Virgin Media’s tie-up with Spotify, and Orange’s coupling with Deezer in the UK, seeking to replicate their joint success in France.

More longstanding partnerships include Spotify and Telia in Finland and Sweden, Telenor and WIMP in Norway, and **Cubo Musica** by Telecom Italia and Play Me in Italy. In Ireland, leading ISP Eircom operates its own dedicated **MusicHub** service, offering subscription and downloads and using its reach as the country’s largest ISP with some 40 per cent of the broadband market.

In the US, **Muve Music** is an example of a new subscription service that is being hard bundled into a wireless rate plan.



The service is operated by Cricket, a leading wireless carrier in the US. For US\$65 a month users can enjoy unlimited song downloads, ringtones and ringback tones and unlimited national talk, text and web access. This plan is offered on an Android Smartphone with no contract.



Since its launch in the first quarter of 2011, Cricket's Muve Music offering has attracted more than 500,000 customers, half of them new to Cricket. Muve Music was built specifically for mobile phone use with customers less likely to have broadband access in the home. It is only distributed through carrier partnerships. By the end of 2012, Muve Music expects to be the number two subscription music service in the US.

Jeff Toig, senior vice president of Muve Music, says: "For the customer segment we target, the mobile phone is central and cash is the primary payment mechanism, while, in contrast, other digital music services have primarily been built for the computer with the credit card as a source of payment."

A different type of bundled service, also aimed at reaching new types of music consumers, integrates the music offering into consumer hardware in the home. Spotify's partnership with Sonos is one of the first deals to give music fans a subscription offering that is geared to provide top-quality audio for people who want to listen to music in the home. Sony's **Music Unlimited** service is based on the population of connected PlayStations and connects to other Sony devices, such as televisions. The service has launched in 17 countries and on Apple devices.



Partnerships between physical stores and digital services have also helped extend the reach of music subscription. Cricket's Muve Music offering is backed by agreements with Walmart and Best Buy that saw these retail giants sell Cricket's phones and sign up customers to its digital service. In Norway, WIMP partnered with physical music store Platekompaniet to sign up customers for its music service offered in partnership with ISP Canal Digital. There is a similar physical and digital tie-up between new music service JUKE and German retail giants Media-Saturn and Media Markt.

Internet radio continued to expand

Internet radio services have long been popular in the US, attracting significant audiences for a more "lean back" non-interactive consumer experience. Pandora continued to grow in 2011, reaching 40 million active listeners in the third quarter of 2011, up 65 per cent on the prior year.

In November 2011, Nokia launched the Nokia Music App with personalised radio features. The app comes pre-installed in the Nokia Lumia 800 phone and enables users to run a personalised streaming service as well as offering the opportunity to purchase downloads or buy live concert tickets. It also offers dozens of stations programmed by music experts. Users can stream any station on demand, or download 15 hours of programming to listen to any time offline.

Music video meets strong consumer demand

Consumers continue to watch music videos in sharply increasing numbers worldwide. The most watched artist on YouTube is Justin Bieber, whose videos have been viewed more than two billion times. His video *Baby* remains the most individually watched music video on YouTube, with more than 690 million views. In December 2011, YouTube announced it would be pursuing a strategy focusing on more prominence for its specialised "channels", including dedicated programming from artists such as Madonna. The service also embraces social networking by integrating with Facebook and Google + so users can see what their friends are watching.



The most prominent dedicated online music video platform is **VEVO**, which provides a revenue stream from premium high-quality videos, original music programming, live events and a forum to break new acts. Across its distribution footprint, VEVO reports it is streaming 3.6 billion videos a month to more than 415 million users worldwide. The fastest-growing parts of VEVO's platform are its mobile and tablet applications which are used by 13 million people. A model that was principally used for marketing purposes has become a commercial proposition.

VEVO generates revenues today through advertising and brand sponsorships. The service has attracted more than 550 advertisers from sectors ranging from automotive to finance. By its second anniversary at the end of 2011, VEVO delivered more than US\$100 million in royalties to rights holders. Its chief executive, Rio Caraeff, says: "VEVO offers the largest premium music video inventory in the world. We want to ensure the music audience is valued by advertisers. Value is created by embracing ubiquity for the audience and scarcity for advertisers."

Integration with social networks is vital for the service. More than 7,500 artists have its VEVO for Artists app on their Facebook pages, helping them power and monetise their videos. VEVO itself has 1.5 million Facebook fans and is working to further improve the embedded experience for users over the next year.

The art of digital marketing

In the digital world, record companies are innovating to reach audiences in new ways.

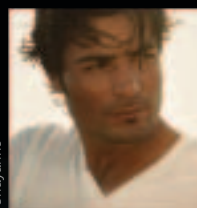
Engaging a new audience in digital: Take That

Many of Take That's fans are women in their 30s and 40s, not typically early adopters of digital music technology. When the album *The Circus* was released in 2008, just 4 per cent of its sales in the first week were through digital channels. Paul Smernicki, director of digital, Universal Music UK, says: "We realised we needed to bring the Take That audience with us on a digital journey."

The band joined online social networks, with their Facebook followers growing in number from around 200,000 to more than one million between the release of *The Circus* and *Progress* two years later. Polydor created an app that was downloaded more than 500,000 times. Digital assets, such as photos, were used carefully. The label built excitement about the first picture of Robbie Williams with the rest of the band before releasing it and encouraging fans to share it online with their friends.

The result was clear, with 20 per cent of sales of *Progress* in its first week of release coming through digital channels. It was notable that *Progress* appeared twice in the iTunes top five, both the original and deluxe versions, with the premium product selling more copies.

Innovative partnerships in Latin America



Chayanne

How do you sell recorded music in markets where there are comparatively few digital and physical stores?

Sony Music Latin America has worked on two initiatives to address that question, creating premium product bundles with Music Ticket + and partnering with Corona Beer in

Mexico to create a dedicated online music channel.

Music Ticket + bundles the sale of tracks and concert tickets. Fans pay a premium for the ticket, and receive a card at the concert which contains a code they can use to download studio tracks from the performing artist.

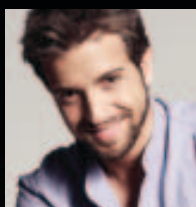
Chayanne, the Puerto Rican singer, has benefited from Music Ticket +, selling more than 350,000 premium tickets during his recent tour of Latin America. This is a significant number of tracks in markets that have been devastated by piracy, with his last album selling around 25,000 copies in Brazil. When fans logged on to obtain downloads after the show, they saw a short film of Chayanne thanking them for obtaining his music legally.

The creation of the Corona Music Channel in Mexico has benefited bands including Pearl Jam, whose album was made available on it for a week before it went on general release. Under the terms of the deal, Corona guaranteed 20,000 copies of the album – a substantial volume for a market where 30,000 album sales achieve a gold record.

Both initiatives are educating music fans about how to obtain digital music from legal sources. Fans also supply their contact details, making it easier for them to be contacted about future albums and concerts.

Working with social networks: Pablo Alborán

Pablo Alborán



Pablo Alborán is a singer-songwriter from Spain. EMI began discussions with him two years ago about how to promote his work in the digital age. Simone Bose, managing director EMI Iberia, says: "Pablo is a very talented artist, with a strong work ethic. We were always clear that we did not want him to do anything that did not reflect his true personality."

The label posted online films of Alborán performing the tracks he was writing in preparation for his debut album, providing fans with a glimpse into the creative process. They also supported his tour across Spain, capturing his performances and posting them online. Kelly Rowland saw the films and said he was an amazing talent, spurring further global interest in Alborán.

Social networks provided vital feedback on the music and this helped to decide which of the 40 tracks Alborán had recorded should appear on his debut album, which topped the Spanish charts for 15 weeks. His follow-up Christmas 2011 acoustic album was made available as a bundle, combining a premium version of the album with additional video footage and a discount on the best tickets for a special Christmas concert.

Bose concludes: "Working with Pablo has helped us learn about how social networks can deliver for our artists, turning theory into practice."

Touching music fans' hearts: Christina Perri

Christina Perri



Warner Australia wanted to build a digital campaign to promote the launch of singer-songwriter Christina Perri's debut single *Jar of Hearts*.

The label decided to build on the incredibly strong message of the song by constructing a microsite that would enable users to anonymously place their stories of heartbreak in a virtual jar, while other visitors to the site could offer personal advice, setting these hearts free.

Integrating the microsite into social networks was crucial for the success of the campaign. As people could see other stories being placed in the virtual jar, they were encouraged to open up about their own experiences. Users directed their friends to the site through links on Facebook and Twitter in particular.

Christina Perri was so struck by the idea that she promoted the microsite through her own online social networks, helping the site gain legitimacy and momentum. Warner Australia also persuaded journalists and media personalities to try the site, offering advice to those who had placed their hearts in the virtual jar. This helped ensure coverage for the story across broadcast, online and print media outlets.

Users could click through to iTunes to buy a copy of *Jar of Hearts*, which plays as a background track while they explored the microsite. Thanks to the digital campaign and offline promotional activity, the single went to number two in the ARIA charts and Christina Perri's album, *lovestrong*, went top five.



Main photo: Take That. Getty Images

Top left: Chayanne. Photo by Ruben Martin

Middle: Pablo Alborán. Photo by Jose Luis Tabueña

Top right: Christina Perri. Photo by Lani Lee

Piracy: improved cooperation from online intermediaries

“Why is the needle in this debate on the move? First, no doubt, because ‘free’ is no longer just a problem for the music industry. Film studios, book publishers and newspapers are all now in the same storm.”

Paul McGuinness, manager, U2

Widespread piracy is the biggest factor undermining the growth of the digital music business. The music industry sees cooperation from online intermediaries, such as internet service providers (ISPs), payment providers, advertisers, mobile service providers and search engines, as indispensable in addressing the problem and significant progress was made with all these parties in 2011.

The vast scale of the problem is widely recognised, as is the recent evolution of new forms and channels. Globally, it is estimated that 28 per cent - one in four - of internet users access unauthorised services on a monthly basis (IFPI/Nielsen). Around half of these are using peer-to-peer (P2P) networks. The other half are using other non-P2P unauthorised channels which are a fast-growing problem. These include blogs, cyberlockers, forums, websites, streaming sites, smartphone-based applications and stream ripping applications. In some countries, the rate of usage of illegal sites is far higher than the global average - for example 42 per cent and 44 per cent respectively in the major markets of Spain and Brazil (Nielsen/IFPI).

PERCENTAGE OF INTERNET USERS ACCESSING AT LEAST ONE UNLICENSED SITE MONTHLY	
EUROPE	27%
GLOBAL	28%

Source: Nielsen/IFPI, November 2011.

Active internet users refers to monthly users of the internet. Unlicensed services refers to selected P2P and non-P2P services that are used to access music and other content.

A rigged market

The result of this activity is effectively a rigged music market. Legal services, whatever their model, incur the business costs of being authorised and paying rights owners, as well as investments to develop secure payment methods and good quality services. This model is unsustainable when facing competition from infringing services that have greatly reduced costs and circumvent the normal rules of commercial business. A commercially sustainable digital music sector needs an environment in which the industry can effectively enforce its rights.

Even in a digital marketplace replete with attractive legal services, illegal “free” continues to be an irresistible magnet for consumers.

Surveys consistently find that piracy undermines the incentive to obtain music using legitimate paid models and depresses spending, even among those consumers willing to purchase music.

Research by The NPD Group during 2010 in the US found that just 35 per cent of P2P users also pay for music downloads. P2P users spent US\$42 per year on music on average, compared with US\$76 among those that pay to download and US\$126 among those that pay to subscribe to a music service. While some P2P users also pay for music, and a few are serious fans who spend a lot, this positive effect is counterbalanced by the far greater numbers of P2P users that spend little or nothing. The overall impact is therefore negative, and this finding is corroborated by a study in Europe by Jupiter Research in 2009.

Books feel the impact

The problem increasingly affects other creative industries, such as book publishers, who are trying to monetise their products in the digital environment. In October 2011, Börsenverein des Deutschen Buchhandels, the organisation representing German publishers and booksellers, reported that 60 per cent of e-book downloads in Germany are illegal. Publishers are warning about the impact this is having on investment decisions. René Strien, CEO for publishing of the major German book firm Aufbau Verlag, says: “In this situation, investing in digital business models is a double risk for my company, which is why having the right legal framework is so essential.”

The music industry advocates a three-pronged approach to tackle online piracy. Providing attractive legitimate services and conducting public education campaigns are two key elements of this approach. The other is the ability of the industry to effectively enforce its rights, ensuring that consumers have an incentive to move from illegal free to legitimate services.

“Many factors have hurt music sales, including the closing of so many record stores. But almost every... study has concluded that file-sharing played a role, and anyone who believes otherwise is running out of alternative explanations.”

Robert Levine, Author of *Free Ride – How the Internet is Destroying the Culture Business and How the Culture Business can Fight Back* (The Bodley Head, 2011).