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# Adding up the music industry for 2008

In the autumn of last year, PRS for Music published Recession and Royalties which asked a timely and pre-emptive question: 'If the UK economy is about to enter a downturn, what does that mean for music?' That paper also provided a simple table showing what's at stake. By adding up the industry for 2007, total revenues came to £3.2 billion with an 80/20 rule in place: eighty percent of revenue came from the consumer, and the remaining twenty percent from business-to-business. That table was an important first stab at working out what music was worth in the UK. Here, we revisit that table to provide a more insightful understanding of how to 'add up the music industry' for 2008.

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Adding up the value of any industry is one thing; knowing where all of its separate parts are and (importantly) how to piece them all together is another. Last year, we added up the various music industry revenues, then adjusted for double counting, and reached a total of £3.2 billion. This was an acceptable and insightful first stab, but admittedly we had only just started trying to calculate the monies generated by live music, made basic adjustments for double counting and hadn't even considered the revenues from advertising and sponsorship. That said, the table provided a concise and simple way in which the reader can understand 'how it all hangs together'. For the music industry's various stakeholders who find themselves in an unprecedented state of transition - that's important.

What that table also provided was an understanding of an eco-system or value chain, which helps counter much of the Armageddon-style hysteria that surrounds the state of the UK music industry. The point being, value doesn't just disappear; rather some will be lost, some will be displaced and some new revenues will enter the industry. With that in mind, some new headline numbers and underlying trends have already been announced for 2008. *PRS for Music* and PPL both announced record breaking gross collections, whilst the BPI reported declines in both retail and trade values, but encouragingly at a slower rate than before. Conversely, by scaling up *PRS for Music* tariff data, we calculated that the value of primary tickets surpassed £900m for the first time ever.

Now, maybe these headlines are telling us something about the underlying trends: a shift away from B2C and towards B2B revenue sources, perhaps? Similarly, the stellar growth of live revenues hints at a 'changing of the guard'; which for many emerging bands leaves behind a model where you would tour at a loss to sell CDs and towards a situation where 'live' related revenues are the main breadwinner. In addition to these headlines and trends, we've also got to contemplate what was lost from the primary market and picked up elsewhere, such as secondary ticketing as well as what was lost completely via illegal P2P file sharing. Finally, we also need to consider the less conventional value streams, such as direct revenues from advertising and sponsorship – something that's never been done before, until now.

So before delving into the details, let's make two announcements straight off the bat. Firstly, the value of music was calculated to be £3.6 billion for 2008. Secondly, this represents an increase of 4.7% on the revised 2007 figure of £3.5 billion. Put more bluntly, the pie just got bigger.

**The Big Number**

**£3.6 Billion for 2008**

**Revenues up 4.7% on 2007**
**B2B now makes up a quarter of the pie**
**B2C revenues skewed towards heritage acts**
**P2P undermining investment in new artists**
**Economic uncertainty for 2009**

### Breaking down the numbers

Now to the detail, laid out in the same easy-to-understand table format as last year. We'll provide a brief overview here, and tackle each cell in turn afterwards, but note that a completely new table was calculated for 2007, which was revised and updated to be consistent with the latest methodology. From the top down, retail value of recorded music fell 6% whilst live revenues grew 13%. In terms of what the consumer spent on music last year, this surprisingly represents growth of 3%.

On the more complex B2B side, *PRS for Music* and the combined revenues of PPL and VPL showed growth of 14% and 13% respectively, after adjusting for double counting. Similarly, publisher direct revenues and record company licensing revenues were both up 7%. Finally, the new addition of advertising and sponsorship was calculated at £89m for 2008. The combined effect grew B2B revenues by 10%. Grouping both sectors together results in a pie worth £3.6 billion in 2008, up 4.7% on the previous year's revised figure of £3.5 billion. Most notably B2B revenues now constitute over a quarter of the overall pie.

## Adding Up The Industry for 2008

**£million (% change on year)**

| | Adjustments | Contribution | YoY growth |
|---|---|---|---|
| BPI retail value of recorded music industry | | £1,309 | -6% |
| Estimated value of the live music industry | | £1,391 | 13% |
| **Business-to-Consumer Total for 2008** | | **£2,701** | **3%** |
| | | | |
| *PRS for Music* gross collections | £608 | | |
| Adjustment for double counting mechanical | -£95 | | |
| Adjustments for double counting live revenues | -£22 | | |
| | | £491 | 14% |
| PPL and VPL gross collections | £140 | | |
| Adjustments for double counting BPI revenues | -£79 | | |
| | | £61 | 13% |
| | | | |
| BPI record company licensing revenues | | £195 | 7% |
| Estimated publisher direct revenues | | £90 | 7% |
| | | | |
| Advertising and sponsorship | | £89 | -1% |
| | | | |
| **Business-to-Business Total** | | **£926** | **10%** |
| | | | |
| **Aggregated total B2B and B2C Value** | | **£3,627** | **4.7%** |

### Recorded Music – signs of the decline levelling off?

The fact retail spending on music fell by only 6% is actually quite an achievement, given the harsh economic conditions and turbulent events on the high street towards the year end. Within the overall figure of £1,309 million, digital grew by almost 50% whereas physical declined by roughly 10%. With a better understanding of both markets, we can revisit the Holy Grail question, which can be broadly paraphrased as 'will the growth in digital revenues be enough to off-set the declines in physical?' Our answer would be that 'it might be ...but be patient!' If one were to project forward current volume and value trends for both sectors, project forward current volume and value trends for both sectors, a 'levelling off' effect might be on the horizon by 2011.

Needless to say, caution needs to be stressed when discussing projections, given the pace of change the music industry is going through: recent history tells us very little about the short term future, never mind three years ahead. We'll come back to this point towards the end, but one trend that is definitely worth following is that digital albums now constitute around half of the digital value pie when viewed on a transactional basis. That's important to consider as we can begin to ask what's driving this trend: is it displacement from physical albums to digital albums, from digital singles to digital albums or is it from P2P to legal consumption?

Looking at the digital market more closely, we can repeat an exercise carried out in the paper titled *Understanding and Interpreting the Digital Market*, and break down the digital pie for 2008. This table begins with our first of three 'known figures': an IFPI digital retail value of £212m which includes ringtones and other ancillary revenues. From here, we can remove VAT at the UK rate of 17.5%, but appreciate that (i) it was lowered to 15% towards the end of last year and (ii) many digital retailers are headquartered outside of the UK. From here, our second 'known' figure is the trade value, which the IFPI report as being £139m, which is 68% of the overall pie. Finally, our third 'known' figure is *PRS for Music* gross collections, which amounts to £22m, of which 58% was distributed as mechanical royalties.

## UK Digital Market 2008: From Retailer to Song Writer

**£million (% change on year)**

| | Adjustments | Contribution | YoY growth |
|---|---|---|---|
| 2008 Estimated digital retail value (IFPI) | | £212 | 51% |
| *VAT based at an estimated 17.5%* | -£32 | | |
| Adjusted 2008 digital retail value - net of VAT | | £180 | |
| Estimated retail gross margin (Pre Society) | -£41 | | |
| Trade value of the digital market for 2008 (IFPI) | | £139 | 64% |
| | | | |
| Then, to be extracted from the retail gross margin | | | |
| | | | |
| *PRS for Music* digital collections for 2008 | | £22 | 51% |
| *Average commission of 12.5%* | -£3 | | |
| 2008 *PRS for Music* net distribution | | £19 | |
| *Of which: performing rights* | | £8 | |
| *Of which: mechanical rights* | | £11 | |

### Live music is growing, unevenly

Make no mistake; the live music industry grew in 2008. More events, more bands, more tickets and importantly, higher ticket prices. Breaking it down to basic supply and demand economics, and given the scarcity embedded in its model, the live music industry is somewhere you really want to be right now. However, the distribution of wealth in live music represents a trend that economists at *PRS for Music* have also established in digital music – a perverse and paradoxical effect of the 'long tail'. We will get to this shortly, but first, the big numbers: primary tickets grew by 13% to £905 million, secondary tickets grew by 4% to £149 million and ancillary revenues grew by 18% to £338m. That gets us to a grand total of just short of £1.4 billion.

Getting to these headline numbers merits some explanation. For the value of primary tickets, we simply divided up the *PRS for Music* tariff receipts by their respective percentages, multiplied by a hundred, factored in VAT and added a prudent booking fee of 10%. Secondary ticketing values were derived by TixDaq, who collect data from all the main online secondary platforms such as eBay, Seatwave and Viagogo. Finally, our estimated ancillary revenues were a combined effort, using a top down approach based on company accounts and a bottom up methodology working with our own live data, Ticketmaster price data and Mintel estimates of 'buy rates' for food, beverage and merchandise. Both routes were strikingly similar, and we took the mid-point into the final calculation.

How do we interpret this buoyant trend for 2009? The first observation is that the artists generating these big numbers can be characterised as heritage acts. Secondly, whilst all major summer festivals for 2009 have sold out, there is a real concern with demand for the 'mid-priced' touring acts. Third, this growing inequality between heritage acts and the rest of the pack mirrors a separate trend identified in digital music, where more choice led to a widening gap between the hits and niches. Combine these three observations and one can see that a 'digital Britain' faces a problem with investment in the creative industries. Sure, recorded is down and live is up – but it's recorded music which makes the primary investment in new talent, and given the damage already done to investment calculations by P2P, therein lies a 'conveyor belt' style question: who's going to invest in the career development of artists to create the heritage acts of tomorrow?

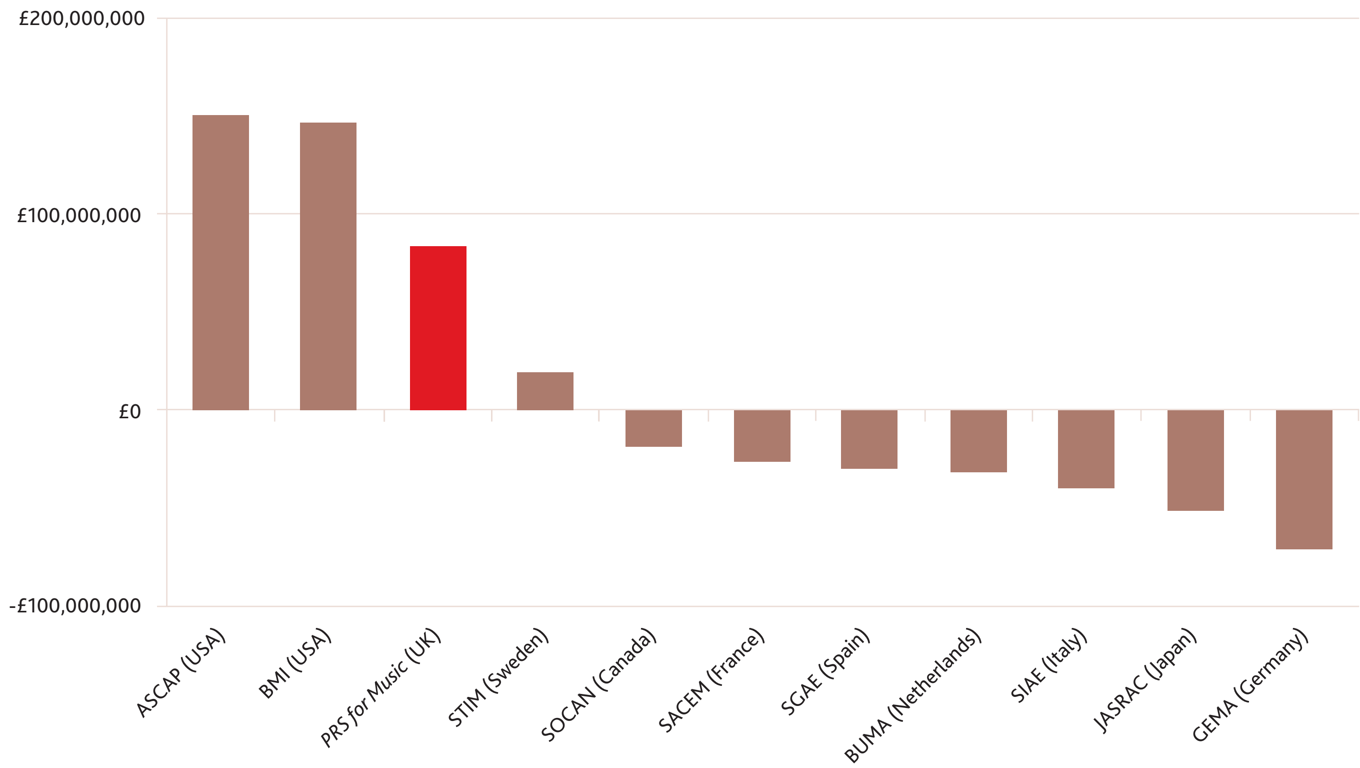
**_PRS for Music_ and PPL – punching above their weight, home and abroad**

The contributions of *PRS for Music* and PPL to the growth of the overall pie are significant. Both have seen public performance, broadcast and online revenues grow significantly, and in the case of *PRS for Music* this has helped off-set declines in mechanical (physical product) revenues. For PPL and VPL revenues, another off-set can be observed as the former grew by an impressive 11%, whereas the latter fell by 8% - and after double counting adjustments - this results in growth of 13%. Whilst the strong domestic performances of each society deserve celebration, the role of international revenues for both camps merits closer attention, not just in its contribution to the overall pie but also in appreciating the outstanding performance of UK songwriters and performers abroad. What's more, that overseas success story continues when you look at the performance of the record labels in North America. Here, we deal with each in turn.

Firstly, international revenues for *PRS for Music* totalled £140m in 2008 whereas PPL, which is relatively new to the world of reciprocal relationships, has sped from zero in 2003 to over £15m in 2008 – encouraging growth for a nascent reciprocal market, and a sign of things to come. [Note: *PRS for Music* has been collecting money from overseas since the early 1920s]. To illustrate the comparative strength of *PRS for Music* repertoire, and offer an indication of PPL's international potential, the chart below ranks the trade balance for the top ten Performing Rights Organisation (PROs) in 2007. Here we take the value of money that comes in from the reciprocal network (exports) and deduct money that flows out to the sister societies (imports). This helps illustrate an important point: the UK is one of only three countries, along with the US and Sweden, who can claim to be a net exporter of repertoire: more money comes in from overseas than gets sent out.

## Society's trade balances: money in (Exports) minus money out (Imports)

**Source: CISAC Accounts 2007**




Arguably, UK artists and songwriters are punching above their weight; the UK music industry can be justifiably proud of its performance and the government should take note. Sure, the physical market is in decline, but not nearly at the same rate of descent as in the US and elsewhere. Similarly, our digital revenues per head of population might not be as large as the US, but it is at least twice that of Germany, France or Spain. With respect to music piracy, the well documented problems persist, and importantly hinder the ability of the legal digital music services to maximise their true potential. That said, the ability of the UK music trade bodies to have a formal dialogue with both internet service providers and the government is encouraging and was even cited by Mitch Bainwol, CEO of the RIAA as 'the direction in which we should all be looking to move in'. There's a lot going on with UK music just now, in terms of licensing, lobbying and collecting revenues, and much of it relates to our performance and influence overseas.

That said: let us not forget the artists who in 2008 brought home numerous success stories, especially from the market that's hardest to crack: North America.

**Success of British artists in the USA and Canada, 2008**

The outstanding performance of UK music abroad was captured in a recent BPI Market Information Report, which provided an analysis of the success of British artists in the USA and Canada in 2008 in terms of album sales, single track downloads and airplay. Key facts:

- In 2008, one in 10 artist albums sold in the USA was by a UK act
- The UK's share of single track downloads was measured at 9.8%
- Coldplay's Viva La Vida was the biggest selling UK artist album in the USA, with sales of 2.1m
- Leona Lewis topped the 2008 download and 2008 airplay charts
- UK artists' share of album sales in Canada reached almost 15%, up from 12.5% in 2007

This overseas performance reiterates the intrinsic value of UK music (see final box), in that the contribution of UK music to the creative economy is not restricted to the domestic market. It also provides a useful reminder of how the interconnected industry hangs together.

For newcomers to the music industry, recall that *PRS for Music* collects for songwriters and publishers, whilst BPI and PPL represent performers and labels. Many of the UK artists listed here, such as Leona Lewis, perform songs written by non-PRS members.

Therefore, while both master and publishing rights are performing well abroad, we must be wary of comparing apples with pears. It can often be the case that an overseas songwriter is penning hits for our UK artists, and hit artists from overseas are performing UK songwriters' works.

**Publisher revenues, direct and increasingly diverse**

Calculating direct publisher revenues is never easy, but our estimate of £90 million is prudent and evidence based; meanwhile the growth estimate of 7% has real meaning. The first thing that needs to be explained is that the standard rule of thumb of 40:40:20 (mechanicals: performance: sync) which is so often used to generalise publisher revenues has long since broken down. Secondly, it would appear that publisher top line revenues are growing, however the revenue mix is obviously changing. Mechanicals share has fallen, the role and relevance of the performing right has therefore grown and traditional sync revenues are not the only 'other' game in town. Third, the combined effect of multi-territorial licensing, advances and equity will make calculating what UK publishers' revenues are worth, and for which time period, increasingly complex going forward.

Beneath these trends are some undercurrents in the publishing industry which are worth flagging up to provide a balanced perspective on this frequently misunderstood sector. Firstly, the amount of revenue available in the buoyant sync market is influenced by supply as well as demand. That means that, even if market demand is strong, should all publishers – large and small – then start focussing their resources on sync revenues, this positive supply side effect will depress price. [Note: obviously if you're publishing one of those few unique songs that can never be substituted, it's value will remain intact]. Secondly, there is increasing evidence of the more 'proactive' US model of publishing being increasingly adopted in Europe, with an emphasis on direct as opposed to collective licensing solutions. Video games, for example, are being licensed directly, offering big returns for big blockbuster acts. Again, the perverse effects of the long tail, with a widening gap between hits and niches, might be rearing its 'head'.

Lastly, commentators often misunderstand the direct and indirect links between record companies and publishers, misleading audiences by simply saying 'the money's in publishing'. There is money in both, with a large part passing from one to the other, which gives rise to a horse and cart scenario: the performance and actions of record companies, and their stakeholders, can also influence the performance and actions of publishers.
A hypothetical example of a downside risk could be the decision to reduce shelf space on the high street, which may eliminate catalogue on which publishers are more focussed. An upside opportunity might be the decision by major labels to throw their weight behind catalogue-orientated digital music services, which might resuscitate that catalogue online. These are all decisions which could be taken beyond the publishers control, hence a balanced outlook for the music publishing requires consideration of internal and external factors.

**Record company licensing revenues, now almost a fifth of total**

Record company revenues, outside traditional unit sales of music, increased by 7% to £195m in 2008, up from £182m in 2007.
This figure is comprised of four sources of revenue: (i) digital licensing such as We7 and Spotify, (ii) sync licensing from the use of sound recordings in film, TV, games and advertising, (iii) PPL and VPL which is reflected in the double counting adjustment and (iv) multiple rights income from '360 degree' deals from direct sales and licensing of recorded music copyrights such as the use of artist logos, merchandise and touring. These additional revenues have shown a second consecutive year of growth and now account for 18% - almost a fifth - of record companies' domestic income.

The most dramatic growth area during 2008 was digital licensing, which includes income from ad-supported models such as Spotify and We7 as well as bundled subscriptions like Comes With Music. Revenues from these new digital business models more than quadrupled in a year to £13.8m in 2008. Broadcasting and public performance licensing collection from PPL also generated strong income for labels of £78.7m – 40% of the overall licensing total and a solid increase of 7% year-on-year. Artist-related income continued to provide a substantial revenue stream of £49.9m during 2008.
In contrast to reports from the publishing sector, synchronisation licence income, from the use of music in films, TV, games and advertising, declined slightly from £23.4m in 2007 to £20.7m in 2008, largely as a reflection of broader economic pressures facing the UK advertising industry.

When combined with the trade value of recorded music, domestic record label earnings amounted to £1,088.6m in 2008. Note that this figure, as with publisher direct revenues, does not include exports from international shipments of physical product.
For clarification, B2C revenues and direct licensing are kept to a domestic base, where as collective licensing revenues from *PRS for Music* and PPL incorporates monies from a reciprocal international network. For the purpose of this paper, this approach not only 'hangs together' the published headline numbers, but is also the most meaningful place to draw the line as to defining UK revenues, something we'll come back to in the conclusion.
That said, there is one further revenue stream through which artists (and their managers) can generate revenues directly, which is advertising and sponsorship, and it is that source to which we now turn to complete the table.

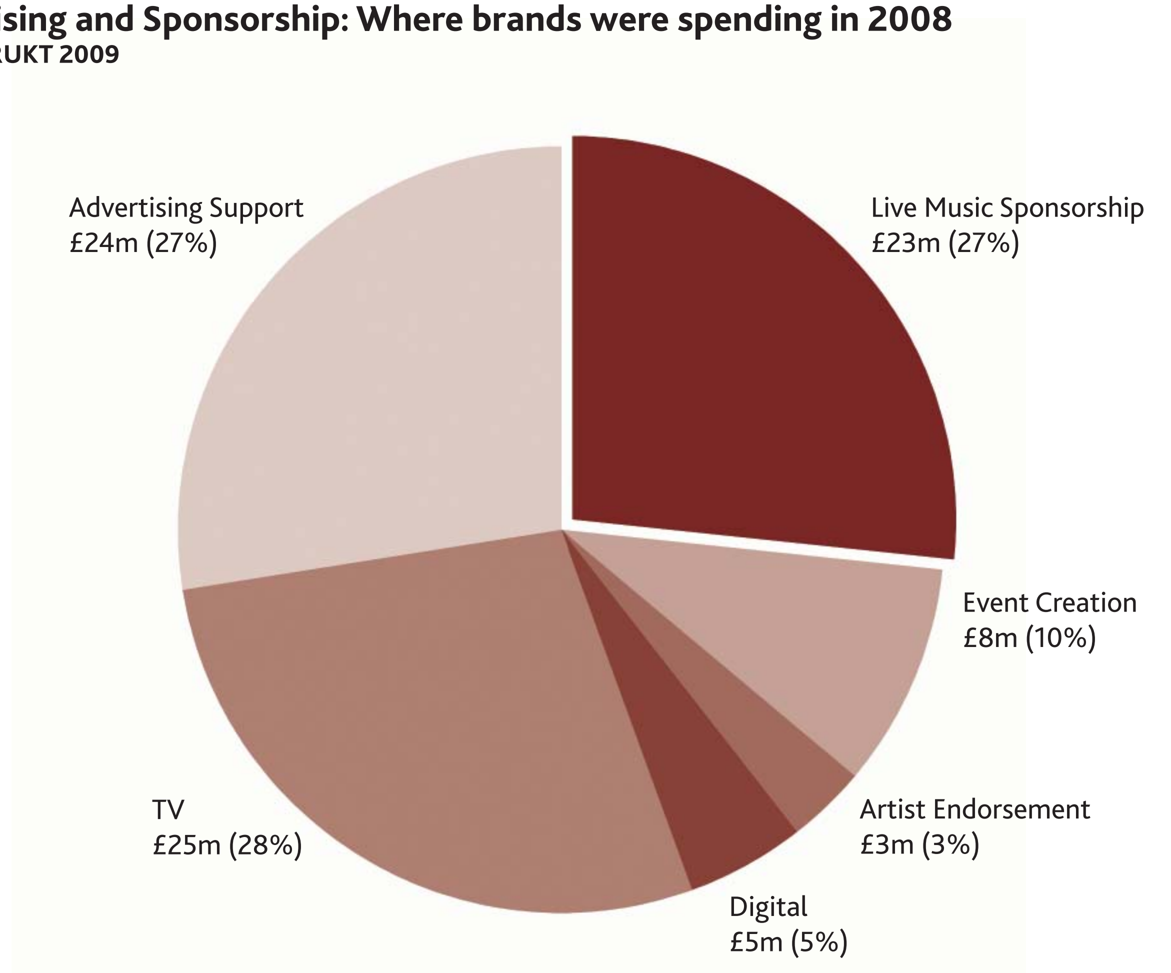
### Advertising and sponsorship

One area of music industry activity that remains off the conventional radar is the revenues generated by advertising and sponsorship. The authors became increasingly aware of this through the impressive work of FRUKT, a music marketing agency, and commissioned them to put a value on this sector for 2007 and 2008 so we could not only complete the table, but also consider whether it was up or down.

FRUKT identified six primary channels where brands can spend their money on music in the UK: (i) live music sponsorship, (ii) event creation, (iii) artist endorsement, (iv) digital, (v) television and (vi) advertising and marketing support. In total, 2008 revenues came to £89m, down marginally on 2007, with the breakdown illustrated in the pie chart below.

## Advertising and Sponsorship: Where brands were spending in 2008

**Source: FRUKT 2009**




Investment in live music platforms has traditionally been a core part of brands' spend in music and still makes up over 25% of total with £23m invested in 2008, although that was down £3m on 2007. This fall is a result of lower income from festival-based sponsorship; however the high-profile naming rights of the O2 venue has minimised the overall effect. Both event creation and artist endorsement showed modest growth, whilst the former is seeing displacement towards advertising support and the latter remains more relevant in US and APAC markets. Digital markets (online and mobile combined) grew by almost 20% in 2008, buoyed by social network partnerships and brands creating their own destinations that link into other live based activity. TV investment grew, with brands co-funding production of music based content for extended usage rights, however this area of investment might be in for a disruptive 2009 as visual content continues its move online. Finally, traditional advertising still dominates the overall picture, with drinks companies tying music activity into their promotional strategy.

Providing a value for advertising and sponsorship should raise some eyebrows, as it's never been done before, at least not in this context. So how should one view a number of £89 million: is it plausible, too high or too low? Opinions will differ on this, but it's worth rearing the long tail's head once again. The sum of £89 million did not reach the entire music industry; in fact the distribution of these proceeds would have reached a select number of mainly established acts; definitely more than double figures but certainly not in the thousands. We've already raised concerns of the live music industry being hit-heavy in its distribution of wealth, and given the fact much of this £89 million is pumped into the live music business, it's not inconceivable that the same 'inequality' effect is kicking in here. Put into plain English, brands investing in music are drawn to it through the potential audience affinity and reach; this means that much of the major expenditure is biased towards the larger priorities and artists, which provide larger fan bases.

### What it all means: and what might the table look like in 2009?

This attempt at adding up the industry offers the reader a meaningful reference point for conducting their own analysis of the market and then building their own evidence base for decision making. It is not exactly timely, as we're past half way of 2009 and still referring to 2007 CISAC numbers for overseas societies! Nor is it perfect; few statistics are – but this work illustrates why we need more timely data and a better understanding of where the imperfections are, and what they mean to the overall picture. That alone raises a thought provoking question: what is the 'UK industry' we're trying to add up? Is it a politically defined border, an economically classified area of activity or a discretionary definition that suits the statistics? Back on street level, if a UK consumer buys a CD from an off-shore web based physical retailer of a Canadian artist recorded and published out of America, with songs written by a Swedish composer – how much of that 'activity' relates to the UK economy? These types of questions are important to ask, but be careful about arriving at the text book answers that the standard economic tools may prescribe. Music, and the creative industries more generally, are not typical 'goods' like manufacturing or services. Furthermore, jumping to conclusions about its contribution to the economy – with terms like Gross Value Added – risks omitting the 'intrinsic value' that music provides (see box).

What this all means, though, is that we've now got a better handle on how the whole music ecosystem hangs together. The work by FRUKT, for example, introduces us to source of revenue which isn't new, but has arguably been omitted from much of the industry analysis to date. That's important, as we cannot be complacent and base analyses around 'known known' market trends and ignore the 'known unknowns'. Similarly, this work gives the reader a better handle on how to ask and then answer the 'Holy Grail' question. As mentioned earlier (though), any projection needs to be treated with caution; but an evidence based projection has to be a better than a thumb in the air forecast. And even if we find ourselves no longer on that projected path, we can use this work to have a constructive debate about current 'events', such as the impact on 2009 of the loss of two prominent high street retailers and dramatic popularity of online streaming services. The former may pull down the value of physical, the latter push up the revenues from digital, but at least we've got a better evidence base to contemplate how the impact of those 'events' might play out on the construction of the 2009 table.

And how might that table look by the end of 2009? Factors outside the industry's control will have a major say, especially as the effects of a 'deleveraging' economic downturn work through the system. Jeremy Fabinyi, Acting CEO of *PRS for Music*, has talked about 'tough times ahead', and advertising revenues are reportedly down double digits in many B2B sectors such as commercial television. That said, the intrinsic value of music itself may be playing a role in helping the industry weather the storm, as all major summer festivals have sold out and recorded music sales have shown some impressive resilience given the conditions. In terms of putting your money where your mouth (or mouse) is, two trends are worth a punt for 2009 though: firstly, B2B's share of the overall pie will grow, and secondly that the wealth gap between hits (often heritage acts) and niches will widen. Ultimately what this all means is that portfolio theory matters more now than ever before or as Jeremy Fabinyi would argue, finding new places and new ways to collect royalties has never been so important.

**Measuring Music's Intrinsic Value**

The "music industry" is an incredibly broad church; ranging from those with artistic talent, who write and perform music, to those who represent, manage and invest in that talent and those who collect royalties on behalf of all the above. An emerging 16-year songwriter, a 57-year-old jazz musician, a major record label and a collecting society like *PRS for Music* are all important parts of the picture.

Into this mix you can add an ever-evolving list of other interested parties, be it retailers, distributors, telcos, tech start-ups, social networks and advertisers, as well as the more traditional promoters, venue-owners and so on.

In short, that catch-all term - "music industry" - conceals a seriously complex interconnected network. And as a consequence, quantifying the true value of music has also proved problematic.

Yes, we can measure tangible sales of CDs, downloads and tickets, but that is only part of the story. A diverse range of additional businesses also derive financial benefit from music, whether directly or indirectly.

We can capture some of the knock-on effects from music. Events such as music festivals have a positive effect on pie-makers and brewers through to hoteliers and tent-sellers to name but a few. The town of Glastonbury benefits to the tune of an estimated £73m per annum as a result of the music festival, whilst T In The Park brings an estimated £18m into the local economy of Perth & Kinross.

Casting our net wider, there are intangible social and cultural benefits, which are much harder to measure. There is something intrinsically good about music. We must, wherever possible, build this intrinsic value into our understanding of the industry and the value it creates.

It is vital that HM Treasury appreciates this intrinsic value when allocating government spending, especially in the context of spiralling national debt. Good health and good education are recognised to have intrinsic value and their funding decisions take this in to account. The same holistic consideration must be applied to music and wider arts funding.

A cost benefit analysis structure that dismisses intrinsic value as 'soft' or 'uneconomic' because a price tag is not attached will lead to a misallocation of resources. Where an activity's benefits are understated, funding will suffer and this has been the experience of many of the UK's creative industries to date.

Music is powerful and it has a deep and significant impact on our national well-being and identity, even if its true value won't always appear on a balance sheet.

**Feargal Sharkey, CEO UK Music**