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Adding up the UK music industry 2010

Prepared by Will Page and Chris Carey, *PRS for Music*.

This is the third edition of *Adding up the UK music industry*, yet it represents an unusual first, with UK music industry revenues falling by 4.8 percent to £3.8bn in 2010. During the year, both recorded and live music saw significant declines in revenues. To interpret this southward trend, demand- and supply-side factors must both be considered. On the demand-side, the tightening squeeze on disposable income is forcing consumers to make tough spending choices. On the supply-side, many major touring acts were not on the road in 2010, and with less supply comes less demand.

This year, we've made significant methodological advances, the most important of which is within the UK music publishing business. We now value UK music publishing direct revenues at almost £250m, a significant upward revision. Consequently, UK music can take some pride in that we are now one of the few – if not only – countries in the world to be able to demonstrate the true value of this fundamental part of the business.

The importance of UK music abroad remains a core focus of this report, as it is where the most potential lies going forward. International revenues remain one of the key drivers of both *PRS for Music* and PPL collections. We consider the success of UK labels and publishers overseas and take stock of *PRS for Music*'s members' ability to outperform the US in exporting repertoire abroad. The fact that music and media are among the few export industries the UK truly excels in is expanded upon in our concluding remarks.

The driving force for this third edition remains the same: the better we understand this complex business, the better it will perform. We are therefore indebted to the collaborative working spirit of the UK music and media sectors for their contributions.

Headlines and footnotes

This report is unprecedented in the music industry as it involves all the major stakeholders putting their cards on the table, so that the seven core revenue streams can be calculated, collated and constructed into one meaningful table. But before going to the table to grab the headlines, it's important to be clear on the footnotes. It's important to recognise what the report is, and what it isn't. The most common question that industry stakeholders ask about UK music is 'how is it doing?' This is a turnover-based question, which seeks to discover whether there is more, less or the same revenue coming in compared to a year ago.

In *Adding Up* we answer this frequently asked question, and do so by focusing on turnover. We do not attempt to present financial accounts that have their own regulated reporting standards. Nor do we attempt to present the value of UK music to gross domestic product (GDP) for inclusion in official government accounts. That is the job of accountants and government statisticians. We focus instead on turnover, which tells us if markets are growing, stagnating or shrinking.

The big numbers for 2010

- **UK music exports continue to grow, outstripping even the US**
- **Total UK music revenues down in 2010, falling 4.8 percent to £3.8bn**
- **Industry adapting to change with growth reported in B2B licensing**

PRS for Music represents over 80,000 songwriters, composers and music publishers in the UK and protects the rights of international songwriters through over 150 arrangements with international bodies.

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Reading beneath the top line

As with last year's report, three questions will punctuate each of the revenue lines.

- How do we accurately define 2010?
- What exactly is the UK music industry and where do we draw the line?
- Are the terms B2B and B2C still the right way to carve up revenues?

Firstly, we take an activity approach to the calendar year. If tickets were purchased for a festival a year in advance, which is often the case, we re-scale the data to ensure that the revenue numbers are reflective of the activity that took place within that calendar year. We also re-work previous years' analysis to ensure that the critically important year-on-year trend is consistent and meaningful to the reader.

Secondly, and perhaps most puzzlingly, how do you define the UK? In the context of business-to-consumer (B2C) revenues, if the US band Bon Jovi sell out the O2 Arena to tourists who have flown in from South East Asia, then is that actually UK revenue? We are asking what activity took place in the UK, and what revenues it produced; therefore this revenue would be included. Consequently, we do not pick up the revenues of UK artists like Coldplay when they tour France, for example. For business-to-business (B2B) revenues, we capture flows into the UK from affiliates (e.g. GEMA in Germany) and net-off money that the UK sends overseas to affiliate organisations (e.g. ASCAP in the US). Importantly, this new exports-minus-imports adjustment better enables us to add the contribution of the UK collecting societies into GDP, and allows other countries to replicate this methodology without double counting.

Thirdly, we maintain a view that the best way to add up the industry is to separate out the revenues into B2C and B2B. The increasing diversification of revenue streams helps illustrate why. Record labels, for example, are moving towards an impressive one-in-three rule where one third of trade revenues come from outside the physical product market. In addition to this, there is a growing B2B revenue stream from licensing activity.

With this clarity on caveats, we can now go back to the headlines and work through the big numbers in this year's table, before distilling each sector down individually.

Adding up the UK music industry

£m	2009	2010	Change
BPI retail value of recorded music	**£1,343**	**£1,237**	-7.9%
Estimated value of live music	**£1,589**	**£1,480**	-6.8%
***PRS for Music* gross collections**	**£431**	**£425**	-1.3%
Adjustment for mechanical revenue	(£89)	(£81)	
Adjustment for live revenue	(£23)	(£20)	
Adjustment for international payments	(£80)	(£85)	
PPL and VPL gross collections	**£66**	**£79**	18.9%
Adjustment for recorded B2B revenue	(£72)	(£72)	
Adjustment for international payments	(£2.7)	(£3.0)	
Estimated record company B2B revenue	**£204**	**£218**	7.2%
Publisher direct revenue (excluding *PRS for Music*)	**£241**	**£242**	0.6%
Advertising and sponsorship revenue	**£90**	**£94**	4.2%
Business-to-consumer total	**£2,932**	**£2,717**	-7.3%
Business-to-business total	**£1,032**	**£1,058**	2.6%
Total B2B and B2C value	**£3,964**	**£3,775**	-4.8%

Are recorded music revenues back on a slippery slope?

While 2009 was the year when UK retail spend stabilised (and trade revenues actually grew), there is an eerily familiar slippery slope feel to the 2010 figures, with the second largest percentage fall in trade revenues since records began . While steep falls in physical revenues continued apace in 2010, there were clear signs that growth in digital revenues slowed across the main international recorded music industry markets, with the IFPI reporting global digital trade value up only 5.3 percent to $4.6bn in 2010. Put more bluntly, global digital revenues are not going to be the '$30 billion dollar baby' people talked about five years ago. Indeed they may stabilise at around $5bn over the medium term.

A global perspective

The IFPI *Recording Industry in Numbers 2011* publication reported an eight percent fall in revenues in 2010, driven by a 14 percent drop in physical off-setting the five percent gains in both digital and performance right revenue. Reading beneath the top line, the top two markets (US and Japan) were responsible for 50 percent of the decline in 2010, compared with 80 percent in 2009. Compounding the overall declines were the UK and Australia, both of which had stabilised back in 2009, before reporting large falls in 2010. Outside of the large established markets, South Korea, India and many Latin American markets reported growth, with Brazil overtaking Spain to claim tenth spot in the IFPI rankings. Indeed, the market in Spain (a western European market with 46m people and an advantageous language) is now so depressed that 3,000 album sales will often get an artist to number one. Should declines continue at their current pace, it is conceivable that Spain could drop out of the top twenty within three years, possibly being overtaken by countries such as India and South Africa – which is a timely reminder of the increasing relevance of these re-emerging markets.

Back to Blighty

Although the southward trend in the UK market has re-emerged, there is some good news that needs to be kept in mind. UK music continues to remain relatively and comparatively strong. In per capita terms, the UK remains one of the top three recorded music markets in the world, towering above the US market, and remains number one in terms of European digital revenues, with Norway a close second. In addition, when artists break big in the UK, their hits sell volumes rarely seen anywhere else. The US act Kings of Leon's *Only by the Night* sold more in the UK (2.6m) than the USA, and is one of five artist albums to have sold more than two million copies in the UK in recent times – alongside Lady Gaga, Take That, Adele and the late Amy Winehouse – a respectable watermark by any standard.

Delving into the statistics, three observations help to form a view of what happened last year. Firstly, the aggregate trade value of physical albums has near enough halved in five years, and now appears to have entered into an accelerating rate of decline. Consequently, the make-up of the recording industry trade revenues is changing faster than anyone could have predicted; in 2009 £1 in every £5 came from outside physical revenues, half way through 2011 and it's now looking close to £1 in every £3.

Secondly, the spiky nature of demand re-emphasises how critical the fourth quarter is to the overall picture, generating 40 percent of total trade value for the year, with physical product still making up three-quarters of that demand. Fourth quarter 2010 was a particular disappointment: the value of sales fell by 16 percent in the final three months of the year, accounting for 60 percent of annual losses. The notable explanations for the disappointing fourth quarter included the exceptionally bad weather (which affected distribution as well as consumption), competition from other media goods such as computer games, ongoing pressure on retail space and the persistent presence of unlicensed digital content on ISP networks.

Thirdly, there are two supply-side developments worth noting: the release schedule may have lacked the strength of the previous year, with half of the top ten selling albums in 2010 being either 2009 releases (Lady Gaga, Michael Buble and Paolo Nutini) or compilations (*Now That's What I Call Music 76* and *77*). Also, new BPI research on breakthrough acts – bands that pass 100,000 album sales for the first time – show that 2010 hit a new low, with only 17 UK acts making it past this watermark, compared to a broadly consistent 25 in recent years.

Before considering the prospects for 2011, it is well worth taking time to ask a question that is incredibly complicated to answer: what is the value of digital in the UK, and to whom? In this instance, we will answer on behalf of music rightsholders.

Firstly, the OCC and BPI estimate the retail value of digital at an impressive £316.5m in 2010, up 18 percent on the previous year. By definition, retail is a B2C value as it captures consumer spend. We can strip off a notional £47m in VAT using a rate of 17.5 percent (it will be lower for many of the transactions which took place) and from the net amount remove the trade value of £215m to show an effective retailer margin. Using these published retail and trade values, VAT works out as £47m, leaving retailers with a margin of £56m. Of course, with a lower VAT rate, retailer margin will widen further.

However, the value of digital music to rightsholders also includes two other revenues. Firstly, there are B2B record label licensing revenues from models such as ad-supported services. Secondly, the authors' value of digital rights in the UK, which is not captured in the trade value as the rights are licensed directly by collecting societies such as *PRS for Music* and SACEM and agencies such as CELAS. In the table below, we accommodate this by adding £12.5m in ad-supported revenues for the labels and £34.2m in songwriter copyright[1]. Consequently, a more specific question is 'how much is digital music worth in the UK to rightsholders in 2010?' The answer is an impressive £260m.

Value of digital music in the UK to music rightsholders 2010

£m		
Retail value of digital music		**£316.5**
Less: VAT @17.5%	(£47.1)	
Retail value less VAT		**£269.4**
Less: retailers' margin	(£56.0)	
Trade value of digital music to labels		**£213.3**
Add in: labels B2B revenues	**£12.5**	
Add in: authors' digital collections	**£34.2**	
Uk digital value of music rights		**£260.0**

[1] The value of songwriter copyright online in the UK was calculated through three steps. Firstly, we took the value of *PRS for Music* online licensing for UK markets. Secondly, we estimated the value of UK online songwriter copyright which was paid through to other licensing organisations such as CELAS and SACEM for transactional UK activity. Thirdly, we scaled UK revenues to reflect non-transactional blanket deals that took place in the 2010 calendar year.

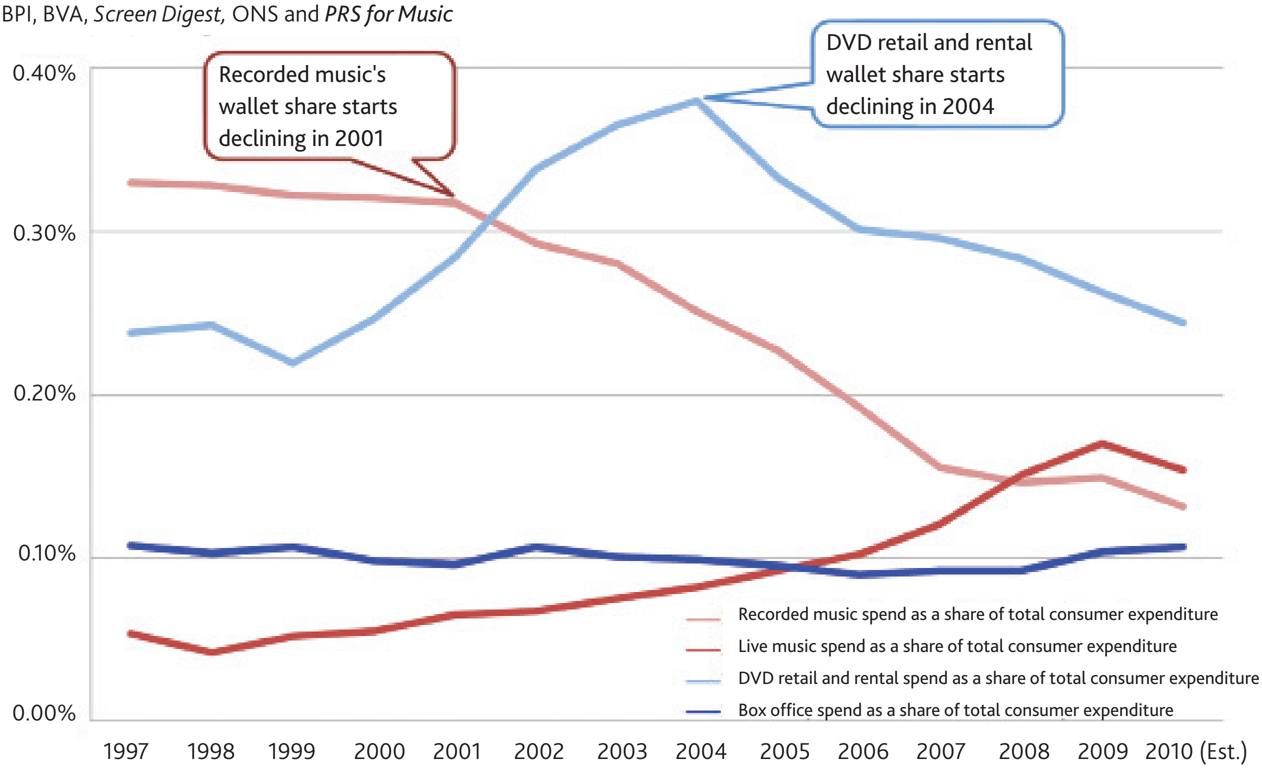
Looking ahead to 2011, the success of Adele is as welcome as it is worrying, as this 23-year-old artist was responsible for almost 10 percent of all artist albums sold in the first four months of the year. While her feats at home and abroad are worth celebrating, what's worrying is the performance of the rest of the market, with continued declines in physical value and modest digital growth. Significant supply-side adjustments are taking place too, with retailers and wholesalers seeking new ways to balance risk in the supply chain. All of this needs to be set against the state of the economy, and the squeeze on consumers' wallets with spending cuts, tax creep and oil prices already compounding an inflationary problem which is eroding earnings and savings. All these factors are likely to force the consumer into some tough choices about their entertainment budget (see box overleaf).

Events up, recordings down

The chart below expands upon a recently published paper titled *Wallet Share* by breaking down the respective shares of total consumer UK expenditure on live and recorded music from 1997 to 2010. In addition, the shares of box office, video retail and rental spend are also plotted. A working hypothesis by economists at *PRS for Music* is that people are spending more of their money on events and less of their money on recordings of events. Put simply, they go to gigs and the cinema more but buy CDs and DVDs less. The dark red and dark blue lines show live music growing consistently and box office spend broadly constant, which means absolute value growth as total consumer expenditure grew throughout this period. The light red line shows recorded music's wallet share declining from 2001, while the light blue line shows DVD retail-and-rental wallet share following a similar path from 2004. Here, it's worth pointing out one blatantly obvious point: both cinema and concerts involve some form of excludability – security guards – which means you have to pay to get in. Since broadband hit critical mass in the UK in 2001, this has not been the case for media files on networks.

Wallet share of events versus recordings

Source: BPI, BVA, *Screen Digest,* ONS and *PRS for Music*



Live music: where supply dictates demand

Live music finds itself in unfamiliar territory in this year's report, having experienced a fall in primary ticket revenue for the first time in recent history. Primary ticket sales fell from £956.9m in 2009 to £843.5m in 2010, a fall of 11.8 percent. The secondary market (those tickets traded on resale sites, such as GetMeIn, Seatwave and Viagogo) grew by £21m, with arenas accounting for the greatest volume of tickets traded. At-the-event spend (often referred to as ancillary revenues), which had grown nearly 60 percent over the previous five years, also faltered in 2010, falling 3.5% to £444m (from a revised £460m) as a result of fewer people going to live events. However, when people did go out, they spent similar amounts to the previous year. Consequently, total live revenues fell from £1.59bn to £1.48bn, down 6.8 percent.

It would be very tempting to look at these numbers and jump towards a knee jerk reaction that the live music bubble has burst. We should not. Instead, we should develop a broader understanding of the dynamics at play in the market. While UK festivals performed strongly, and arenas and mid-sized venues held up, there was a striking decline in the number of stadium gigs in 2010 compared to the previous year. It was this reduction in supply of stadium concerts that accounted for almost two-thirds of the fall in revenue.

From statistics to the reality of bands on the road, this supply-side story is born out in the acts that performed last year. In 2010, a number of stadium- and arena-filling bands were not on tour (Rolling Stones, Coldplay, Take That) and many of those that did tour opted to play smaller venues in order to limit their risk (Kings of Leon and Rod Stewart played arenas rather than stadiums). This risk-averse behaviour is rational in the current economic climate. Last year, we championed the success of music against the rest of the economy, whereas this year it feels as though the economic downturn has caught up with the live music industry, and promoters and bands alike have responded accordingly.

To gauge the performance of festivals and arenas, it's worth looking at the UK market against the backdrop of Europe, as the two are intrinsically linked. Arena tours are rarely confined to the UK only, and many UK festival promoters are now developing events overseas, such as Benicassim in Spain, and are deliberately marketing them to the UK audience. The UK festival market saw its primary ticket revenue increase by nearly 20 percent. This growth was the result of both the increasing capacity of existing festivals and the increasing number of festivals, up 16 percent on the previous year.

A similar growth story can be observed across Europe, with a comprehensive *IQ Magazine* survey finding that capacity of European festivals was up 15 percent and attendances grew by six percent, with sell-outs increasing by 10 percent - a 'build and they will come' success story. A side issue that is clouding this growth story and increasingly gathering the attention of managers is the calendar period in which festivals take place, which has stretched from July to August to a much broader May to October. There is a plausible argument that this is now crowding out the conventional touring calendar for emerging bands, with some fans saying: 'Why would I pay £30 to see you in spring, when I've already spent £200 to see you in the summer?'

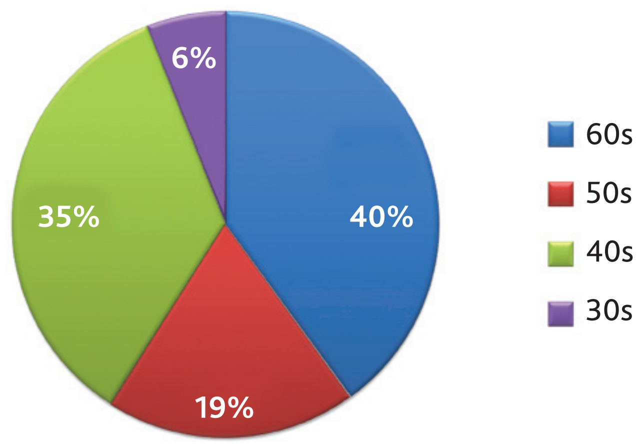
The UK arena market offers a less rosy picture, with *PRS for Music* revenues from arenas falling two percent in 2010. The National Arenas Association's (NAA) report also showed that, while music continued to make up 60 percent of arenas' footfall, music attendances were down 20 percent on 2009, as the volume of shows dropped sharply. Again, the supply-side story can be drawn upon here by pointing out that performances were down six percent. The most striking observation of the NAA report was the dominance of the *X Factor* tour, which had 478,000 attendees – reiterating the importance of hits in a market awash with choice. The European arenas market showed similar trends, with *IQ*'s survey reporting attendances for music events at arenas falling 16 percent on the year while ticket prices grew by two percent.

Looking ahead to 2011, most market players and observers are confident that headline revenues will bounce back, due at least in part to the supply of big bands on tour in the UK. Rihanna, Westlife and Justin Bieber are all noteworthy additions to the 2011 arenas calendar. The impact of Take That touring the UK was visible in the 2009 revenues, and noteworthy by their absence in 2010. They are back on the road in 2011, playing to 1.7m people. While we are not saying that one band makes a market, a tour of this scale really is a 'needle mover'.

Our view is that the live music business is not entering a cycle of boom and bust, but rather showing signs of maturity and cooling to a more sustainable growth path, after a period of unprecedented growth. What this analysis does tell us is twofold. Firstly, that supply dictates demand, and secondly, that demand will be increasingly spiky over time. Looking further ahead, it is right to highlight the aging population of live music performers (see chart below). Deloitte plotted Pollstar's top grossing US tours of the decade by age of lead singer in 2011, finding that 40 percent of the top 20 acts will be in their 60s in 2011. A further 19 percent will be in their 50s and 35 percent in their 40s. Only six percent of the top 20 were in their 30s, with no-one in their 20s appearing. The question is this: against the backdrop of falling record sales, who is putting the time, money and expertise into developing the arena, festival and stadium acts of the future?

Pollstar top grossing US tours of the decade, by age of lead singer in 2011

Source: Pollstar, Deloitte



Collecting societies: growing musical exports, importing collections

The two UK music collecting societies presented a contrasting picture for 2010. *PRS for Music* collections fell for the first time in recent memory but distributions were almost flat – indicating productivity gains. PPL, on the other hand, reported an increase in collections, but the growth in distribution was distorted by a one-off charge resulting from a tribunal decision. It is worth remarking upon the relative stability shown by both societies over the past few years in the face of the deepest recession in a generation. This is a useful indicator of the merits of collecting societies in providing a stable source of revenue for artists, songwriters, labels and publishers.

Firstly, we should explain an important adjustment to these numbers. For both societies, we add international collections, as done in previous reports, but now net-off the money sent to overseas affiliates. So, *PRS for Music* brought in an impressive £170m in international revenues from around the world, but sent out £85m to affiliates such as ASCAP and BMI. In this year's report, we adjust for double counting and include the net amount of £85m. Similarly for PPL, we add in the £32m of international revenues which feature in their gross collections, but net off £3m PPL sent out to overseas affiliates, and therefore report the net amount of £29m.

In 2010, PPL collections grew by 10.7 percent to £143.5m, making it one of the world's largest performance rights societies. Its total distributable revenue was up 33.6 percent to £124.1m, but the sharp rise was due to the fact that 2009's total had been hit by the UK Copyright Tribunal's decision affecting licence fees payments between 2006 and 2009.

Growth was reported across all three PPL revenue streams of public performance, broadcast and international, with the last of these producing the most notable headlines, up 49 percent to £31.7m in 2010. This is a continuation of the £92m success story that resulted from the 52 international reciprocal contracts PPL has established in 28 countries in the past seven years. Going forward, international revenues will remain an increasingly important part of the PPL story.

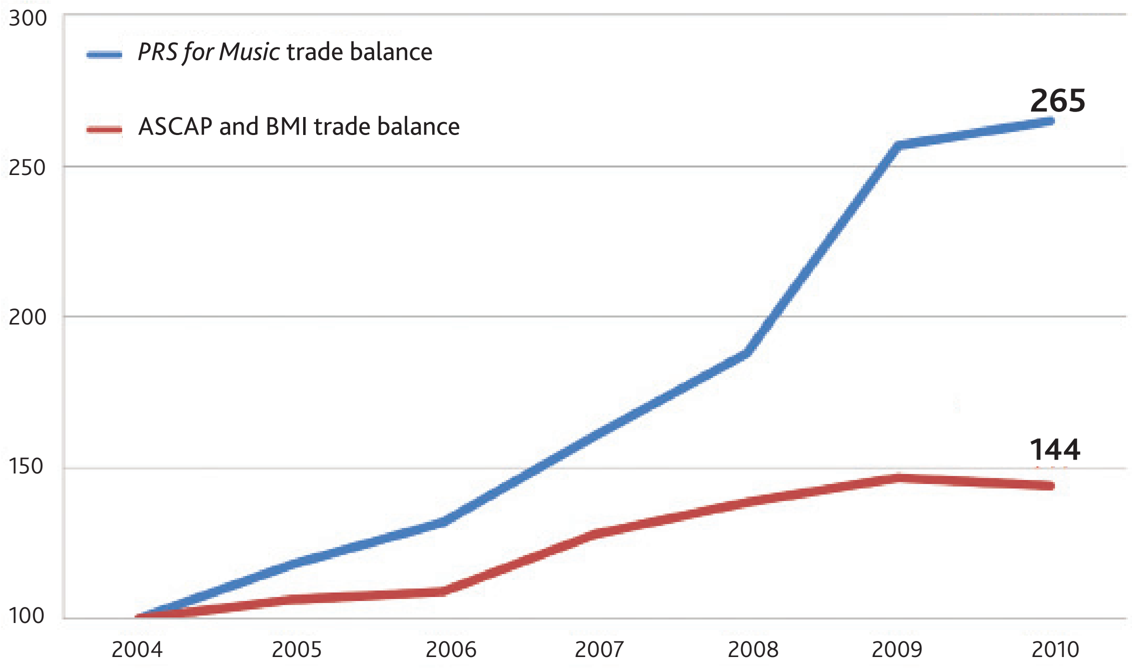
On the other hand, *PRS for Music* collected a total of £611.2m in royalties in 2010, down 1.1 percent on the previous year's record of £618.2m – the first drop in collections in recent memory. An 8.8 percent drop in recorded music sales contributed to the £7m decline in royalties collected. This was offset by a 4.3 percent growth in royalties from digital services, a 1.9 percent rise in radio royalties, and cost savings of nearly 10 percent. As such, net distributable revenue fell just 0.2 percent last year, from £548.8m in 2009 to £547.9m in 2010.

The international success story of *PRS for Music* has been well documented in the past, with the UK being one of only three net exporters of musical repertoire, along with the US and Sweden. Interestingly, in 2010 Sweden sent out more than it brought in, so now we are down to only two.

When we looked more closely at these remaining two net exporters, in particular *PRS for Music* in the UK and the main US societies ASCAP and BMI, we found that *PRS for Music* members significantly outperformed their equivalents across the pond in terms of net trade balance – money in minus money out. The chart overleaf illustrates the index of this trade balance to show the net export growth of the two markets. What is striking is that the relative growth of the UK has significantly outperformed the US, increasing its trade balance 165 percent from $35m in 2004 to $95m in 2010. By comparison, the two US societies have grown their balance by 44 percent from $310m in 2004 to $452m in 2010. It's worth noting that, while this is an index of a net figure, the analysis remains robust when you think comparatively: if you were to multiply *PRS for Music's* money in and money out by a factor of five to reflect the US' greater population, the balance would be broadly similar at $474m. This tells us that whilst all three societies have seen steady growth of 20-30 percent in money sent out to affiliates (imports), *PRS for Music* has almost doubled its incoming revenue (exports), outperforming the US societies by a factor of three.

Index of money in less money out: trade balance of US and UK PROs

Source: CISAC



What the export performance of *PRS for Music* and PPL tells us is that for artists and songwriters, the potential to build upon an impressive international track record is huge. Whether it's the US performance right debate, or the growing importance of markets like Brazil, Russia, India and China (BRICs), the UK as a net exporter is well positioned to benefit from growth in these re-emerging markets. Indeed, given the current economic climate, there may well be more potential overseas than there is back at home – a topic we will return to in our conclusion.

Publisher direct revenues: new insights, significant revisions

Of the seven revenue streams which make up the UK music industry in this annual report, publisher direct revenues have always been the most challenging to calculate due to the lack of existing industry data. Compounding the complexity further is the nature of music publishing itself, which is beyond generalisation as there are so many different players operating in so many different markets, from grand rights to computer games. Reassuringly, this year's *Adding Up* report can offer an important advances in understanding this often misunderstood, yet fundamental, part of the music industry.

By working with the Music Publishers Association (MPA), we were able to survey its membership at a granular level, to appreciate the diverse set of revenues and calculate the value of each. Thanks to the MPA, we are now able to offer a more comprehensive summary of direct publisher revenues, which goes far beyond the 40:40:20 (mechanical:performing:sync) rule of thumb that existed before.

The survey, which was conducted by the MPA and economists at *PRS for Music*, focused on the core membership of the trade body, and breaks down publisher revenues into key streams (e.g. sync, grand rights, print) and then into geography (UK revenues and international receipts). The survey gathered data from the past three years, which allows us to backdate the 2008 and 2009 numbers to produce a consistent year-on-year change for the report.

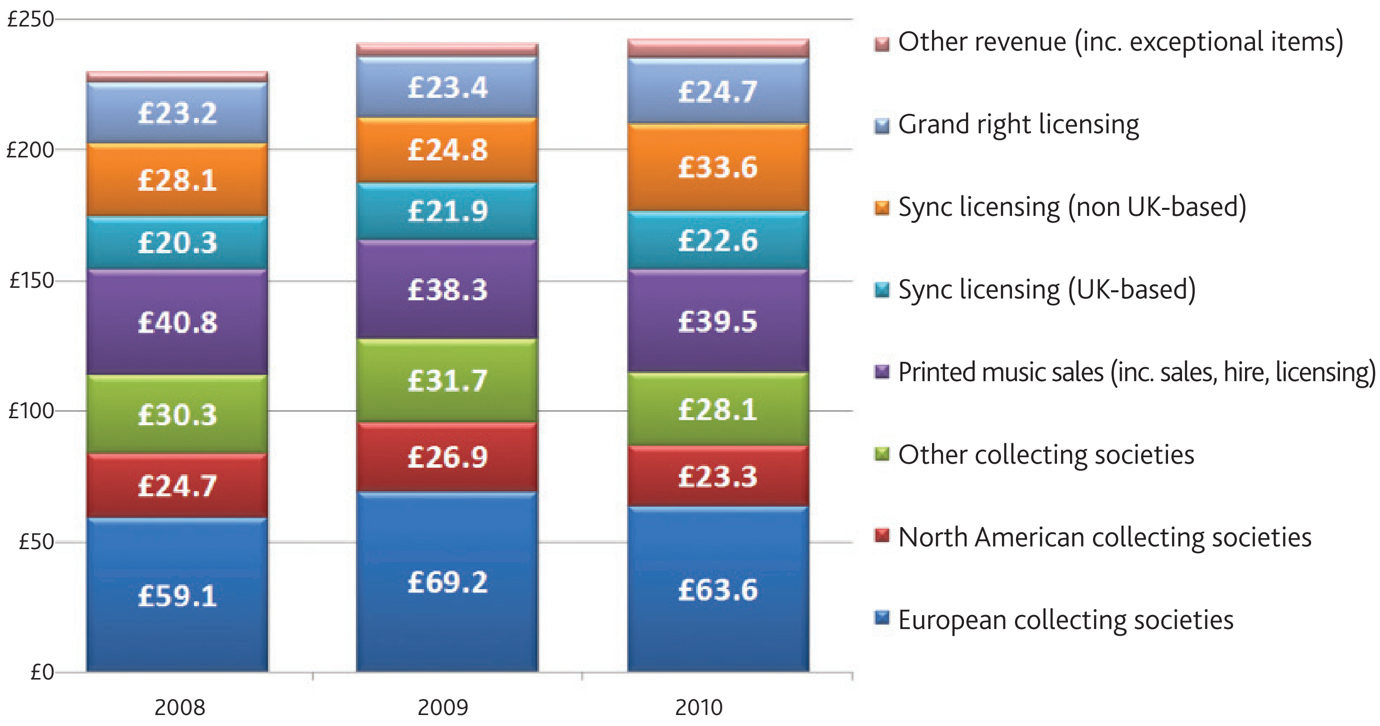
As such, we are able to revise our 2009 valuation of publisher non-society revenues from £103m to £241m. The 2010 figure is broadly constant at £242m, increasing just 0.6%, with growth in sync being offset by falling collections from societies outside the UK. This suggests some stability in the aggregate publisher revenue.

A good proportion of these revenues is derived from the sub-publishing revenue, which in most countries comes through collecting societies such as GEMA or SACEM. A fifth of the revenue is derived from sync licensing income paid to UK publishers. UK-based sync (turquoise area in chart overleaf) captures revenues paid from UK users to publishers for the use of UK originated works and the local publisher share of non-UK originated works. The non-UK based sync (orange area) captures revenue flowing back from overseas for the use of UK originated tracks, net of the local publisher's share. As with other methodology within this work, these actions are taken to allow other countries to replicate this work for their own region without double counting.

Looking beneath the top line, what is perhaps most striking in the chart below is the stability shown in the five publishing revenue streams over the three years. There are some notable winners and losers worth highlighting. Synchronisation of UK works abroad has grown from £25m in 2009 to £34m, while sync within the UK has grown £1m during the same period, again stressing the importance of exports. UK print revenues have stayed remarkably constant over the past three years. Unsurprisingly, mechanical licensing income (which is collected through MCPS and hence excluded) has been on a steep downward trend for the best part of a decade, yet the fact that each of these revenue streams have shown stability illustrates one of the core strengths of the music publishing business: a balanced portfolio with many royalty eggs in several revenue baskets.

UK music publisher revenues excluding *PRS for Music* payments, 2008-10

Source: MPA survey of members and *PRS for Music* calculation (£m)



Record companies: no longer just a wholesaler of music

'We're no longer just a wholesaler of music,' stated Paul Smernicki, Director of Digital at Universal Music Group, in a recent article in *The Economist*. This astute observation acknowledges that, as their traditional business declines, record labels are becoming more skilled at licensing live music and merchandise. The growth in B2B revenues of 7.2 percent to £218.4m, the fourth consecutive year of reported growth, shows that labels are reallocating their resources into B2B markets. Put more bluntly, the growth in this sector illustrates the old adage 'you only get out what you put in'.

To recall, B2B revenues are a combination of the five revenue streams that the BPI previously defined as secondary revenues, along with the additional B2B revenues that arise from ad-funded digital models. Those five revenue streams are comprised of: (i) the £73m in public performance licensing PPL has passed on to the labels, (ii) synchronisation revenues, (iii) premium revenues from covermounts and consumer promotions, (iv) artist-related income from merchandising and touring and (v) 'other income', which refers to record company share of revenue from shows or films, and record company income from music-related TV productions. On this occasion, detailed analysis of company accounts allowed us to estimate the value of these five revenue streams at £206m in 2010, up 6.5 percent on £193.5m in 2009. On top of this is a further £10.8m in ad-funded digital and £1.6m from other digital sources not captured in the retail value of music. As such, B2B revenues total an impressive £218.4m.

This £218.4m in secondary revenue is in addition to the £213m in digital trade revenue highlighted in the earlier table. So, the combined total of label revenue that does not come from the declining physical product market is a healthy £431m, or 41 percent of the total – highlighting the growing importance of diversification to the modern UK record label. This observation may irritate the industry, with many an external armchair critic still touting the observation that labels are dead and therefore they need to diversify. Yet the evidence asserts this has already happened. In fact, we are possibly only one *Adding Up* report away from stating that the majority of record label revenues come from outside the physical product market.

There is a push-and-pull element to what's driving revenues in this sector. The developments in the computer games sector have helped pull revenues forward. Year-end statistics from GfK Chart-Track reveal that unit sales of music games in the UK increased by 13.7 percent in 2010, against an overall decline of 14.3 percent. Hence, the growth areas in computer games are driven by music, such as *Michael Jackson: The Experience*, which in turn drives sync revenues for both record labels and music publishers. Indeed, the developments with Lady Gaga and *Farmville* may well mark a new beginning in this convergence story.

Similarly, developments in merchandising have increased secondary revenues. In the past, a label might acquire a t-shirt manufacturing company with the intention that artist deals would simply encompass merchandise revenues from touring. Now, that t-shirt company will have diversified its product range from hooded tops to high-level fashion and diversified its retail outlets from concert stalls to the High Street and airports. This in turn brings a better proposition to artists, which then allows broader deals to be done, and secondary revenues to grow.

Artists and managers are utilising direct-to-fan tools more, plus they are now able to make better make-or-buy decisions as to what services they acquire and what they can do themselves. This internal competition is forcing the labels to advance their offer in terms of products, services and expertise.

Advertising and sponsorship

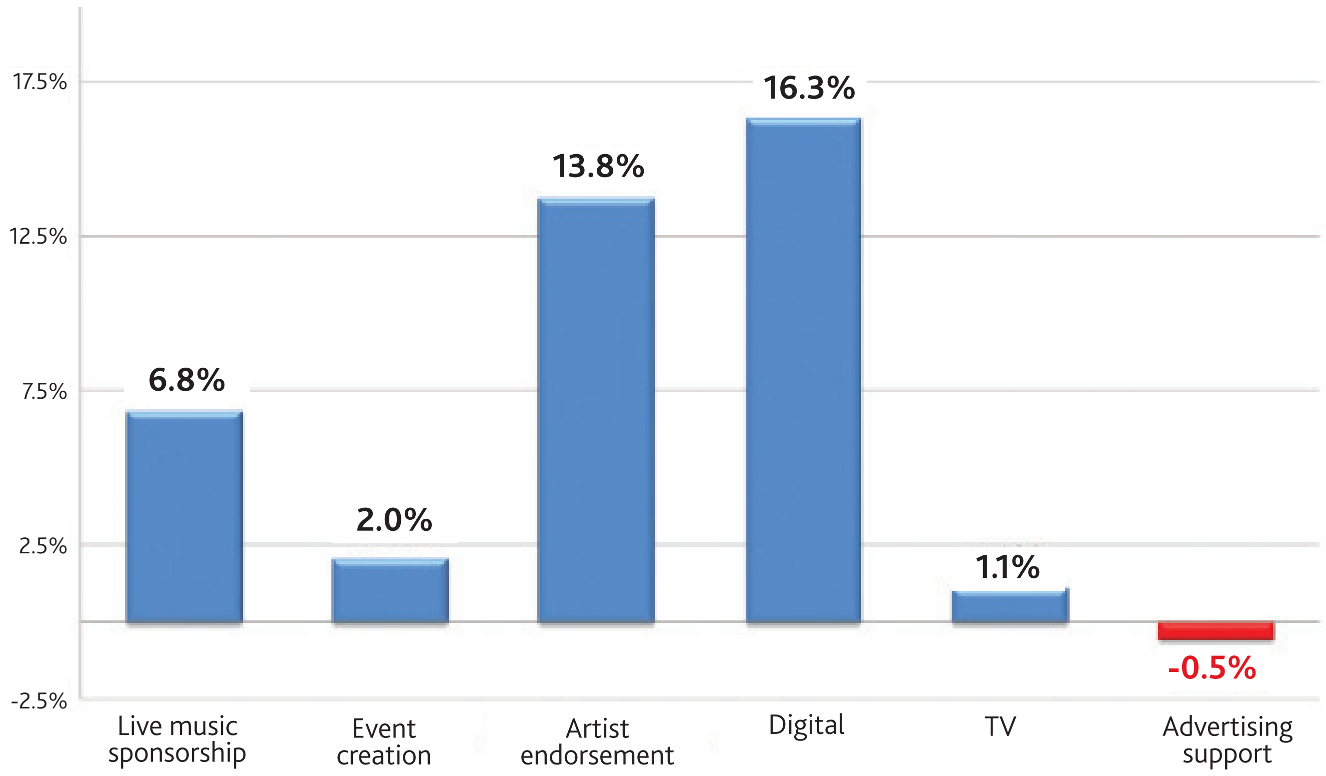
We have continued our partnership with FRUKT Communications to improve our understanding of this unconventional part of the UK music industry. As before, we have identified six primary channels where brands can spend money on music. The table provides definitions for each of the six categories, as well as the headline numbers.

Channel	FRUKT definition 2010	Spend (£m)	Share
Live music sponsorship	The spend on sponsorship rights and direct (e.g. on-site and at event) activation costs for festivals	£32.9	35.1%
Event creation	The creation of custom experiential (e.g. event-based) activity; includes all direct activation costs for event	£8.1	8.7%
Artist endorsement	The use of image rights and appearances of artists to endorse a specific brand/product/service	£3.3	3.5%
Digital	The creation of specific music-focused digital and mobile activities, as standalone platforms or within wider music campaigns	£7.3	7.8%
TV	Sponsorship of existing music-specific or music-focused TV programs and the creation of ad-funded TV activity	£21.8	23.3%
Advertising support	The use of above the line (ATL) advertising and below the line (BTL) promotions to support existing music campaigns (e.g. festival activity, venue naming, custom events, artist endorsements)	£20.2	21.6%
TOTAL		**£93.6**	

The aggregate spend of nearly £94m represents an increase of 4.2 percent, and is largely a result of growing sophistication within the space, as brands become more sophisticated in engaging consumers at events, online and through traditional advertising, competitors and new entrants are forced to move away from simple badging and sponsorship towards more complex multi-channel activations. Furthermore, the growing reach of both festival and digital channels into lucrative 18 to 35 year-old audience means that rights and media owners can demand higher investment rates. The year-on-year movement across the six categories is illustrated in the chart below.

Year-on-year change in music advertising and sponsorship revenues, 2009-10

Source: FRUKT



Breaking down the six categories, Live Nation and AEG are leading the way in live sponsorship for both festivals and venues in 2010. As the consumer value of download promotions and pure content platforms decreases, live music platforms are underpinning the approach of many brands. However, some brands have moved back towards their own event creation, although many of these take the form of limited-scale events and are often used as content creation forums.

Artist endorsements saw a significant increase in 2010, growing 13.8 percent, the second largest increase behind digital. Much of this increase was down to the rise in low- to mid-level artist partnerships, rather than the large scale international deals, which were more prevalent in 2009. Endorsements led from the US are not counted within this sector; however advertising or digital support that originated in the UK is. This sector has seen an evolution in strategy and growing sophistication in approach. Artist partnerships are now spanning across channels, often centred around a launch event and a stream of digital content. At the same time, labels and management are signing and selling artists to brands with a growing level of acumen - artists such as Eliza Doolittle or Pixie Lott are being positioned as both performers and brand advocates.

Digital's growth of 16.3 percent is to be expected. Brands in the UK continue to utilise this as a core communications channel and, with so much music consumption happening online, it's a natural space for brands to sit. Brand-funded TV content focused around music continues to make up a significant proportion of brand spend, just shy of a quarter of the total pie. Growth has slowed due to the lack of a new mass-market vehicle in 2010 (for example *X Factor, Britain's Got Talent*), however both Channel 4 (through *T4* and *4Music*) and ITV (via ITV2 and 3) have continued to attract brands as sponsors of content. Advertising support was the only revenue stream to record a fall in investment in 2010, but a drop of just 0.5 percent is far less than in wider advertising markets.

As with so many other revenue streams covered in this year's report, the supply-side takes priority here. The future path of advertising and sponsorship revenues will depend more on the resources thrown at it than anything else. Encouragingly, the Music Managers Forum has already recognised this and is taking a more pro-active role at engaging UK managers and artists with new and established brands to develop this sector further.

Get small, get abroad

It would be foolish to ignore the obvious trend, which is that physical product took a hammering in 2010 and less money was spent on tickets, and it would be tough for the B2B sectors to grow enough to off-set this downturn. UK consumers spent £215m less on music in 2010 than the prior year – a big dent. Therefore, a succinct summary could be that the big numbers fell and the small numbers grew.

It would be equally foolish for one part of the music industry to publish a strategy for another to follow to reverse these downward trends. With so many complexities and nuances associated with each of the seven revenues streams, it is best left to the experts within them to work out their own road ahead. However, the report does hang together all the different components in such a way that some cross-cutting themes can be put forward. Two key themes deserve a mention here: 'get small' and reduce the transaction costs of managing metadata, and 'get abroad' to maximise the export opportunity of UK music, given the unprecedented changes now taking place in the global economy.

Dealing first with the very unsexy topic of transaction processing and metadata, which is actually the lifeblood of all operational environments, some key points need to be made: in the digital world there is constant change, greater complexity and significantly higher volumes to manage. Business models in the digital world are constantly changing to meet voracious consumer demand. By contrast, for example, the TV broadcasting model didn't change from its inception until the advent of cable and satellite services, and even then by very little. The complexity of arrangements amongst all parties involved in the supply chain are getting ever more detailed as content is sliced and diced to almost infinite levels of granularity. The only way these transaction processing demands can be met is through the development of cross-industry technical standards, deployed right across the supply chain to provide an entirely automated global environment.

Through standardisation initiatives such as DDEX, the Global Repertoire Database and PPL copyright database (with both global initiatives being driven by UK societies), high quality data about musical works and sound recordings will be available to the entire supply chain, and the methods of communication of that data along the supply chain will be automated. This will drive down transaction costs in creating, managing and communicating the data. Now, lowering transaction costs doesn't just cut costs but importantly produces benefits in higher levels of efficiency that speed up cash flow, lower barriers to entry for new legal services and leads to a better allocation of resources - away from managing data and toward monetising it.

There is an old expression about North Sea oil which is that it takes two barrels of oil to get one barrel out of the pump. Current transaction costs in the digital music supply chain often feel like that too. Instead of costing the industry money, metadata should be standardised in such a way that it enables the industry to deliver greater efficiency gains.

The second recommendation is to 'get abroad'. The earlier case studies of *PRS for Music* as well as PPL and MPA illustrate the potential, but do not take account of the changing market. Take the BRIC economies of Brazil, Russia, India and China, which leading investment banks estimate will equal the G7 in terms of economic power by 2028, if not a whole lot sooner. Currently, the performing right collections of these four countries are equal to those of Spain. The risk is that there are two different trajectories; economic growth and intellectual property growth – with the former significantly outpacing the latter. Global organisations like WIPO need to rethink IP in this context, and UK music needs to rethink its export strategy, given the geopolitical rebalancing taking place within these re-emerging economies.

An excellent piece of BPI research underlines the importance of looking beyond borders. According to the BPI, UK artists' share of global sales is estimated to be 11.8 percent in 2010, with one-in-ten sales in the US being a UK act and up to one-in-five in markets like Germany and Australia. BPI also commissioned Ipsos MORI to put a series of statements to the public about the success and importance of British music, with 83 percent of people feeling proud of British music's achievements. As the excellent BBC documentary *Made in Britain* has shown, the list of goods and services that we truly excel in exporting is becoming increasingly limited and is centred on ideas and intellectual property. Therefore it makes sense to work on re-positioning the UK music industry for the changes taking place in the global economy, to maximise the potential of its songwriters and artists in markets that may have been ignored in the past but simply cannot be overlooked anymore.

BBC Introducing new artists at home and abroad

Andy Parfitt is Controller of BBC Radio 1, Radio 1Xtra, Asian Network and Popular Music

On a freezing evening at the end of 2009 I made my way to The Flowerpot, a classic Kentish Town music venue. My job that night was to explain to an audience of journalists, politicians and opinion formers what BBC Introducing had been doing throughout the year, and why they might be interested.

Readers of this report will probably already know that BBC Introducing is a service for unsigned artists, which allows them to upload tracks to the BBC so that they can be listened to and assessed by a range of producers and presenters, providing them with an instant and steady stream of burgeoning UK talent. Being 'spotted' can result in a BBC session on BBC local radio, Radio 6 Music, a playlist slot on Radio 1 – even a performance on a BBC Glastonbury stage. It is a remarkably simple but powerful idea that is the modern day equivalent of sending a demo cassette to John Peel, or loitering outside the Radio 6 Music studios ready to thrust a CD into a presenter's hand.

The evening at The Flowerpot started with my short speech and was followed by live performances from some bands that had recently uploaded their tracks – also, amazingly, on the bill that night – in this tiny pub – was Florence and the Machine, one of the few international breakthrough acts to have made an impact in the US, and contributed significantly to both the recorded and live revenues laid out so clearly in this report.

Why was Florence Welch here sharing the small stage with Out Like a Lion, a West Country indie-pop outfit playing their first ever gig? As it happened, Florence was back to say a generous 'thank you' for the early support she received from BBC Introducing. Her presence hopefully encouraged others in pursuit of creative recognition, recording contracts, festival bookings - on a macro level, those looking ahead at the difficult road to economic success for UK music.

The encouragement and mentoring that presenters like Zane Lowe, Tom Robinson or Steve Lamacq give to these grassroots artists is part of the offer – how to get a good contract, what the A&R department might bring and all the other questions relating to the professional world of the industry. The UK has an extraordinary and unique young music-making culture and the BBC provides resources and powerful platforms.

As this report states, the UK, in per capita terms, remains in the top three recorded music markets in the world, towering over the US market. This is an astounding result from such a small yet hugely artistic nation. In a recent BPI survey, 83% of people are proud of British music's achievement, a major award in itself for the UK music industry. Despite the challenges, the UK is still in a remarkable leadership position in this creative sector.

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