# A Look at the Future of the Music Industry
by
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The commercial music industry is among the largest, wealthiest and certainly most glamorous enterprises in the world. Every year, the music industry attracts thousands of young artists, who eagerly envision a chance at stardom and the "fairy tale" lifestyle that accompanies it. Yet, behind this alluring façade is an industry scrambling to secure a financial base in a technological world that threatens its very existence. The dramatic changes taking place in the music industry reflect largely the development of the recording industry, the engine that drives the music business.

## The Development of the Recording Industry

By the late 1920s, the Radio Corporation of America (RCA), one of two principal radio networks, had created a subsidiary, "RCA Victor," to manufacture phonograph records, a medium still in its infancy.[1] In the late 1930s, the Columbia Broadcasting Company (CBS), the other major radio network, had purchased a small record manufacturing company and renamed it "Columbia Records." By the mid 1940s, the demand for recorded music was such that three additional record companies – Decca (U.S.), Capitol and Mercury – had emerged. These five labels, known collectively as the "major" labels, comprised the hub of the music industry. Yet, during the next 15 years, they would have little impact on the most important innovations in commercial music.

Several of the major labels aided the war effort of the 1940s by supplying the American public with recordings of the best-known "big band" orchestras of the day. But, not everyone was listening to big band records. By the end of the decade, two small genres of music, known as "race" music and "hillbilly" music, had captured the attention of

[1] RCA created its subsidiary by purchasing an existing company, the Victor Talking Machine Company. Hence, the name "RCA Victor."

African Americans and rural white southerners respectively.[2] Although the major labels were aware of both genres, most had no interest in recording either, believing that the market for this music was too small to be profitable.[3] This decision opened a door for new, independent recording labels to enter the marketplace.

By the early 1950s, African American audiences clamored for recordings of a new style of dance-oriented music known as "rhythm and blues."[4] At the same time, white teenagers searched for a type of music to reflect their growing discontent with the placid lifestyle of post-Word War II America. To the dismay of their parents, white teenagers were also drawn to the jumping rhythms and the raw singing style found in R&B records, produced by fledgling, independent record labels. The major labels were aware of the growing interest in R&B among white teenagers, but they were reluctant to add any of the young African American R&B artists to their rosters.[5] Instead, when sales indicated that an R&B record was gaining popularity among African Americans, one of the major labels quickly released a "cover" (i.e. new recording) of the song, sung by a white pop artist.[6] The "white" versions contained more sedate rhythms and even re-written lyrics, changes the major labels believed would not only appeal to white teens, but also placate their parents.[7] Because the major labels had the resources to more effectively promote and distribute new releases, white covers of R&B hits typically outsold the original versions. But, better promotion and distribution also created a larger pool of white teenagers interested in R&B. For many white teens, hearing the "tame" covers merely fueled a desire to find copies of the original recordings. To the delight of both the independent labels and their artists, white covers of R&B hits drove sales of the originals

[2] "Race" music referred to all music created and performed by African American artists for African American audiences. "Hillbilly" music referred to a body of Irish inspired folk music, which had been passed down by several generations of people living in the mountains of the south and southeastern United States.

[3] An exception was Decca (U.S.), which did exploit the "hillbilly" market in Nashville.

[4] The term "rhythm and blues" had been coined by Jerry Wexler, a young writer for *Billboard* magazine, to replace the derogatory term "race" music. Wexler would go on to lead Atlantic Records, one of the most successful independent labels in the history of the recording industry.

[5] The racially charged climate of the 1950s demanded clear separation of the races, which included their music.

[6] So, for example, the Moonglows, an early 1950s "doo-wop" group, recorded "Sincerely," which was covered by the McGuire Sisters, a pop trio. Likewise, Richard Penniman, an early African American rock 'n' roll artist known as "Little Richard," co-wrote and recorded "Tutti Frutti," which was covered by Pat Boone, a teen pop star of the day.

to new heights. More importantly, the popularity of African American R&B artists and their songs among white teenagers ultimately lead to the development of “rock ‘n’ roll.”[8]

For the most part, it was the entrepreneurial vision and efforts of independent labels that created the rock ‘n’ roll era of the late 1950s. The major labels contributed little creative effort, focusing instead on developing pop artists of the day.[9] This is not to say that the major labels failed to profit from rock ‘n’ roll. When record sales identified a potential rock ‘n’ roll star, in many cases, one of the major labels responded with a contract promising the young artist more money, better promotion and better distribution than any independent label could provide.[10] To survive, independent labels were forced to continuously uncover new talent capable of replacing their best artists lost to the majors.[11]

When the British rockers stormed the U.S. in the mid 1960s, the major labels were able to negotiate distribution agreements to ensure that recordings by these new stars found their way from Europe to record stores in the U.S.[12] At the same time, the major labels searched for American alternatives to the British acts. Columbia, for example, signed both the legendary Bob Dylan and the Byrds, a San Francisco folk rock sensation. Likewise, Capitol, based in Los Angeles, saw potential in the California surfin’ sounds of a local act known as the Beach Boys. Capitol also signed many West Coast country artists like Buck Owens, Merle Haggard and Barbara Mandrell, who would go on to push

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[7]Lyrics of R&B songs were often sexually suggestive and even explicit for the day. Such lyrics were altered for white covers. In fact, the term “rock ‘n’ roll” was taken directly from R&B song lyrics. The term has no relation to music in any of those lyrics.

[8]Some of the earliest rock ‘n’ roll recordings were created by African American artists, who developed their craft performing R&B songs. The recordings of early white rock ‘n’ roll artists, such as Elvis Presley, Jerry Lee Lewis and Carl Perkins, demonstrated the influence of not only African American R&B and gospel but also “hillbilly” music.

[9] In some cases, it appears that the major labels misunderstood rock ‘n’ roll. For example, in 1956, Decca (U.S.), a country label, signed a promising rock ‘n’ roll star named Buddy Holly. But, Decca attempted to shape Holly into a more traditional country singer. Unable to convince the label to let him try things his way, Holly left Decca for a small independent label in New Mexico, where he produced a series of hit songs, until his untimely death in 1959.

[10] In many cases, the artist took the initiative. For example, Elvis Presley’s manager, Col. Tom Parker, actively pursued RCA, convincing the label to purchase the contract between Elvis and Sun Records, an independent label in Memphis.

[11] As a result, most of the major stars of 1950s rock ‘n’ roll and early 1960s folk music were signed to independent labels.

[12] One of the most visible was Capitol, which distributed recordings of the Beatles. At the time, it was not well known that the British conglomerate EMI had purchased Capitol in 1955. Capitol was the logical distribution choice for the Beatles, who recorded for Parlophone, a subsidiary of EMI in England.

country music into the national spotlight. Already experienced in uncovering new talent, independent labels were responsible for new American stars like the Mamas & the Papas, who recorded for Dunhill, a production company that partnered with ABC-Paramount, an independent label with distribution clout to match the majors.

## The Multinational Conglomerates get in the game

In spite of its success in both promoting and countering the British invasion during the 1960s, the recording industry experienced a sharp downturn in the 1970s, the result of two unrelated occurrences.[13] First, a demographic shift dramatically challenged the financial base of the industry. As teenagers in the 1950s and college students in the 1960s, "baby boomers" made up a considerable portion of the record buying public. By the early 1970s, the boomers were out of school, working for a living and even starting families. With less disposable income, baby boomers purchased fewer records, causing sales to drop sharply. The recording industry delivered the second blow to itself with the introduction of record albums in prerecorded cassette tape format, a medium designed to replace less-than-perfect 8-tracks and supplement the sagging sales of vinyl LPs. While cassettes were smaller, sounded as good or better than 8-tracks and allowed the listener to enjoy half of the album uninterrupted before turning the tape, [14] they were also extremely easy to copy onto another cassette.[15]

In a 1983 joint venture, Sony Electronics of Japan and Columbia, now "CBS Records," introduced the compact disc to America, which, to the relief of the major labels, replaced both easy-to-copy cassettes and out-dated vinyl LPs. Financially, the introduction of the new technology turned the economic slump of the 1970s into 15 years of double-digit growth.[16] Dramatically increased sales of CDs soon caught the attention of several multinational business conglomerates, looking to cash in on what appeared to be a

[13]Danny Goldberg, interview in *The Way the Music Died*, a *Frontline* Public Television presentation. Aired May 27, 2004.

[14] The design of 8-track tapes caused track changes to occasionally interrupt a musical selection.

[15] Cassette copies could be made by simply connecting two cassette players. The process became even simpler when manufactures introduced dual cassette deck machines to the public.

[16] Ironically, the introduction of digital technology, which solved the 1970s downturn, would threaten the very existence of the music industry by the end of the century.

booming industry. Unfortunately, the surge in CD purchases was not the result of an expanding record-buying market. Instead, it was the result of music enthusiasts replacing their old collections of cassettes and vinyl LPs with new, improved CD copies.[17] The music business was no more stable now than in previous years.

In spite of this fact, Sony Electronics of Japan acquired its partner, CBS records, BMG, a German corporation bought RCA, Seagram of Canada purchased Decca (U.S.), now called MCA, and a Dutch company, Polygram, purchased Mercury. In short order, the majority of the American music industry became the property of foreign corporations.[18] In addition to acquiring all of the major labels, the conglomerates also monitored the activity of independent labels and purchased those that were most successful, thereby expanding their holdings.[19] This practice continues today and has created an oligopoly, in which a handful of corporate leaders, with little knowledge or interest in the type or quality of music produced, control a large portion of the American music industry.

## The Introduction of Digital Music

When the compact disc was introduced in 1983, music listeners were delighted with the improved clarity of sound. Analog sound waves could be transferred from a master tape to a compact disc with no loss in sound quality and a noticeable reduction in background noise. In other words, the copy sounded about as good as the original. But, this new technology came with a price. A $9.00 to $12.00 vinyl album shot up to $21.50, when created in CD format. While the industry defended the price hike, claiming that the new technology did cost more, many record buyers speculated that they were being gouged. They were right.

[17] Melinda Newman, interview in *The Way the Music Died,* a *Frontline* Public Television presentation. Aired May 27, 2004.
[18] Remember, EMI, a British conglomerate, already owned Capitol. American corporations have not participated in this acquisition process, with one exception. In the late 1960s, Steve Ross, who had purchased the Warner Brothers film studios and its fledgling record label, acquired Atlantic Records and Electra, two highly successful independent labels. By merging the three, Ross created the Warner-Elektra-Atlantic (WEA) distribution system that led the industry in sales for years. WEA would eventually form the nucleus of the Warner Music Group, under the ownership of an American conglomerate, Time-Warner.

In 1984, digital audiotape and professional “DAT” recorders were introduced, which enabled the recording industry to create all-digital recordings as well as all-digital transfers and additions to analog recordings. The result was an even cleaner, clearer CD product. But, when manufacturers of professional DAT recorders released a consumer version, the music industry went into a panic – and for good reason. Overnight, the ability to create copies virtually identical to the originals was handed over to the music-buying public. The industry reacted to this calamity by appealing to Congress for legislative action. In 1992, the DART (Digital Audio Recording Technology) Act was passed, which levied a tax on both DAT recorders and tape. The tax was intended to compensate the labels, along with their artists and songwriters, for the potential loss of income from consumer duplication. In addition, the DART act mandated that all recorders include a device that prevented making a copy from a copy.

In 1992, a year after the passage of the DART Act, the standardization of the MP3 audio format allowed computer users to copy songs from a prerecorded CD and store the music on a computer.[20] Had this new technology been contained by the recording industry, things might be quite different today. But, at the time, no one could conceive that, by 1999, a communication pipeline known as the” Internet” would provide a conduit for the transmission of MP3 files from one computer to another, thereby making it possible to distribute illegally duplicated recordings worldwide.

By the year 2000, an alarming number of Internet web sites had been set up as file servers, through which MP3 recordings could be swapped. The pleas of the recording industry to “cease and desist” fell on deaf ears. In a desperate attempt, the Recording Industry Association of America (RIAA), a trade association now representing the conglomerates and their labels, filed suit against Napster, the largest of the music-swapping networks. More recent court rulings have forced the RIAA to aim their lawsuits at individual users instead of file servers, a practice that continues today. Although the RIAA’s methods shocked the world, the action came too late. In 2001, recording industry

[19] Usually, the deal was structured around a multiple of annual sales. Because independent labels are such speculative ventures, many owners were willing to cash out entirely or continue to run their label as an employee of the conglomerate.

sales fell by 5% and in 2002, the figure almost doubled at 9%.[21] During the first three years of the new millennium, the recording industry lost a reported $12 billion in sales.[22]

## Current Changes in the Music Business

The conglomerates have reacted to this financial disaster by either selling their music holdings or combining forces to lower expenses. In the spring of 2004, Time-Warner sold its music division, the Warner music group, to private investors. During the summer of the same year, Sony and BMG won court approval to merge.[23] In spite of these actions, the recording industry still reported a small loss in 2004. Although the industry is cautiously optimistic that 2005 may show a profit, their troubles are far from over.

Since the 1950s, commercial radio has served as the primary vehicle of record promotion. By the early 1990s, many radio stations were struggling financially. The Broadcast lobby, a powerful American political force, convinced Congress to raise the limits on station ownership, a plan designed to reduce expenses by centralizing station operations. With the passage of new legislation in 1996, companies previously restricted to ownership of some 40 stations could now purchase as many as they could afford. Thousands of stations changed ownership, and radio conglomerates – such as Infinity and Clear Channel – emerged. Centralized operations have reduced operating expenses, but they have also established a new practice of creating a single play list for multiple stations. To accommodate the varying tastes of listeners in different geographic areas, only songs with the broadest appeal are selected for these multi-station play lists, resulting in a decrease in the total number of songs played and a heavier rotation of the songs that make it on the list.

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[20] Ironically, in 1991, a year before the passage of DART, a *recordable* CD had been introduced to the market.
[21] *The Economist.com* (http://www.economist.com/research/bandgrounders/Jan. 6, 2005).
[22] Melinda Newman, interview in *The Way the Music Died*, a *Frontline* Public Television presentation. Aired May 27, 2004.
[23] Originally, six different conglomerates owned portions of the American music industry. In 1998, Phillips sold its music division, Polygram, to Seagram of Canada. Seagram merged these new labels with its existing labels to create Universal Music, and the total number of conglomerates was reduced to five. With the Sony-BMG merger, the total number now stands at four.

Without radio exposure, it is virtually impossible to sell large volumes of records. Since the total number of songs played on commercial radio stations has decreased, labels have intensified efforts to make certain that their records make it on the air. These efforts include coercing play list decision-makers with expensive promotional “gifts” and “perks,” a practice that has gown into a “$100 million-a-year trade.”[24] As a result, only those labels with substantial financial backing can effectively influence selections. Therefore, most of the records played currently on commercial radio are those produced by labels owned by the wealthy conglomerates.

Yet, even the ability to guarantee radio airplay may not be enough to ensure success because commercial radio must now share airtime with satellite radio, a new medium making an all out effort to go after commercial radio listeners.[25] Satellite radio offers more than 100 channels of music, sports and news in high quality digital audio to home, portable and automobile receivers.[26] Unlike the current commercial radio practice of limiting the number of musical selections broadcast, satellite radio offers a wide variety of individual stations, each dedicated to a specific musical genre. Because it is this *variety* that attracts the customer, who pays the costs of operation by means of a monthly fee, any limitation in the selection of music or heavy rotation of songs would defeat the purpose. For now, it appears that Satellite radio is immune to outside influence.

## The new Distribution System

To date, the RIAA has filed some 7,000 lawsuits against individual “peer-to-peer” (P2P) file sharers, claiming that it had no other choice. While this may be true, I know of no business which has been able to retain its customers after filing suit against them. In this

[24] Chuck Phillips, “Logs Link Payments with Radio Airplay, *LA Times*, Tues. May 29, 2001 (http://www.bumblefoot.com/otherstuff/articles/payola.htm) Diane Rapaport adds that these “gifts” amount to nothing less than “legal payola.” Diane Rapaport, “Parallel Universes” (http://www.dianerapaport.com/articles.htm).

[25] For example, Sirius Satellite Radio has named Jimmy Iovine, chairman of Interscope Geffen A&M Records as creative consultant and Wall Street giant Mel Karmazin as chief executive officer. Radio star Howard Stern has announced that he will take his commercial radio talk program – along with his audience – to satellite radio in 2006.

[26] Many auto manufacturers now offer satellite radio in their new cars. Most deals offer the customer a free subscription to one of the satellite services for a period of time, after which the customer agrees to pay a small monthly fee to continue the use of the service.

case, however, the major labels furnish the majority of records available; therefore, their customer base remains strong – at least until now.

In a recent article, “The Long Tail,” author Chris Anderson traces a fascinating shift in entertainment marketing that is certain to chip away at the solid customer base of the major labels.[27] Marketing entertainment products in cyberspace, via the Internet, is challenging the marketing of such products via physical outlets (record, book and video stores). According to Anderson, physical retailing is based on “hit-driven economics, ” which assumes that people are drawn only to the most popular CDs, books and movies. This is good because no physical store has enough room to carry all available products. Internet retailers, on the other hand, require no physical space to warehouse inventory, which means they can offer their customers an unlimited number of items from which to choose. In doing so, cyberspace stores have discovered that many people want more than just hits. In fact, the more choice Internet retailers offer the customer; the more the customer buys.

More choice is good news for music lovers who want more than the record (and radio) conglomerates are willing to offer and great news for new artists trying to bring their music to the marketplace. It is terrible news for the major labels, whose control of available products has kept them safe from consumer mutiny. On the other hand, too many choices can overwhelm and actually discourage the customer from making any purchases whatsoever. Many Internet retailers, that sell all types of products including CDs, have cleverly solved this problem. For example, at Amazon.com, when the customer selects an item to consider, information regarding the selection appears along with a box entitled: “Customers who bought this title also bought . . . .” The box contains a list of additional items similar to the one selected. By directing the customer to similar products, this type of marketing system may make it possible for a new musical artist to attain worldwide exposure simply by being “linked” to a well-known artist via the “recommendation box.”

[27] Chris Anderson, “The Long Tail,” *Wired Magazine* (http://www.wired.com/wired/archive/12.10/tail.html).

All Internet retailers offer the customer the convenience of simply traveling to the mailbox to pick up purchases. Some newer Internet music retailers, like Apple's *itunes*, offer the customer instant access to purchases by means of (legally) downloadable MP3 files. Since its launch in 2003, *itunes* has sold over 300 million downloads.[28] At the 2004 Midem conference of the recording industry, the Forrester Research firm predicted that music downloading would continue to grow over the next three years and could represent a third of the estimated business by 2008.[29] An even newer approach – renting music – has been recently adopted by Internet music services like Rhapsody (RealNet)[30] and the new, all-legal Napster.[31] For a monthly fee, the customer has access to an unlimited number of downloads. The system is designed in such a way that the monthly fee must be paid to maintain access to the music. Napster offers an additional incentive in the form of "Napster to Go," software which allows the user to transfer rented music to MP3 devices manufactured by vendors competing with Apple's "ipod."

## Predictions for the Future

1. Despite their current stranglehold on the commercial music industry, it appears that the conglomerates are beginning to lose their grip. No doubt, they will do all within their power to retain control.[32] However, in the coming months and years, I believe we will see a rise of existing and new independent labels offering a much broader selection of music, via Internet retailers and satellite radio, to an expanding group of music listeners who want more options. If this happens, the conglomerates may follow Time-Warner's lead and sell their music holdings, or they may attempt more mergers. If they choose to stay in the game, conglomerates could continue to focus on "mega stars," or they may use some of their resources to search for new innovative talent, thereby following the lead of independent labels. Regardless of what they do, the impact of the conglomerates will be

[28] Peter Cohen, "iTunes Store Downloads Pass 300 Million," *Digital Music Playlist (http://playlistmag.com/news/2005/03/02/itunes/index.php)*
[29] Steven Patrick, "The Search for Digital Music Nirvana," *The Star Online* (http://star-techcentral.com/tech/story.asp?file=/2005/2/15/itfeature/10094264&sec=itfeature).
[30] http://www.listen.com/
[31]http://www.napster.com/
[32] The conglomerates latest strategy involves the release of a new CD/DVD hybrid that contains videos, mini-concerts and interviews, along with the music. This is an attempt to encourage music fans to buy the CD with its added value, instead of downloading the music for free.

less than it is now. Music listeners, independent labels and new artists attempting to break into the business have reason to feel optimistic about the future.

2. As Internet music retailing grows, more record-only (physical) retail stores will likely be forced out of business, the result of their inability to carry enough inventory to satisfy the customer who wants more choice.[33] Larger, non-record-only retailers like Wal-mart and Best Buy, which currently sell the largest volume of hit records, may also experience some decrease in record sales.[34] Internet music retailers will seek additional products to offer their customers, which should open a window of opportunity for new, independent labels and new artists. Correspondingly, the major labels will be forced to share more of the music pie with the indies; however, both Internet music retailers and satellite radio will want access to the older catalogues of the major labels. Ironically, after the dust settles, the conglomerates may end up with an improved bottom line.[35]

3. Despite the furor of the RIAA, illegal downloading will continue. Statistics suggest that the current barrage of lawsuits levied at P2P file sharers may be curtailing downloading, but it is certainly not eliminating it. [36] However, the RIAA is convinced that its lack of action in the past is the cause of the current mess.[37] Therefore, more lawsuits will be filed, which will fuel more attempts to steal music by those who believe that the major labels are simply getting what they deserve for all the years of overcharging the consumer.[38]

[33] I say "more" because in 2004, Tower Records, a major record retailer, closed 1,000 outlets nationwide.
[34] I say "may" because both Wal-mart and Best Buy are currently shoring up their positions by initiating programs that combine online and offline offers. Brian Garrity and Ed Christman, "Web Shapes New Co-op," *Billboard* 117 (Mar. 5, 2005), pg. 1.
[35] The major labels incur no promotional costs for older songs in their catalogues, so profits increase.
[36] Despite the legal actions of the RIAA, it is estimated that some one billion songs per month are still being traded for free online. Jeanne Anne Naujeck, "File Sharing Battle Plays in High Court," *Tennessean.com* (http://www.tennessean.com/business/archives/05/03/67204633.shtml?Element_ID=67204633)
[37] Don Valdez, regional counsel for the RIAA, explained to me that the conglomerates are suffering more from the effects of international record piracy than P2P file sharing. On Feb. 9, 2005, the RIAA requested that the U.S. Trade Representative add China to its list of countries that present "significant piracy problems" for U.S. rights-holders. Tim Culpan and Steve McClure, "RIAA Calls for Action Against China," *Billboard* 117 (Mar. 5, 2005), p. 6.
[38] The new targets for P2P lawsuits are American colleges and universities. Campus computer networks make it is simple for students to illegally download music from the Internet, then share the songs with other students. No university is exempt from investigation and violators are being prosecuted with fines. So far, no one has actually been taken to court

4. Any success achieved by satellite radio in attracting new listeners will be felt by commercial radio, which is fueled by commercial advertisements. Advertisers pay to guarantee that potential buyers of their products will hear their commercials. Fewer listeners will no doubt result in reduced advertising revenue to commercial stations. If profits drop, radio conglomerates will likely follow the path of their record counterparts and either sell their stations or attempt to merge forces.

5. The era of "mega stardom" may be on the decline, which is all right. Artists are simply regular people with a God-given talent. To see them as they are is healthier for both the artist and the public.[39] In light of the predicted redistribution of power, more new artists may decide that their chances for success are better with an independent label than with a major label. Because independent labels can survive only if their records sell, they are highly motivated to ensure that the artists they sign deliver a marketable product. More new artists signed to innovative independent labels almost guarantee better music for all of us. In the future, artists may enjoy more regional, rather than national notoriety, but maybe that is the way it ought to be. While Internet distribution allows new artists to be heard by those interested in their music worldwide, the additional number of artists available to the public will curtail "mega stardom."

7. All of the changes outlined above suggest one final prediction: With the knowledge of how to run a profitable business, the willingness to live a reasonable lifestyle and the connection to an innovative record label driven to produce the best possible music, the new artist ought to be able to build an excellent career doing what he or she loves most – making great music.

[39] For example, many believe that Elvis Presley's drug use, which ultimately caused his death, was largely the result of his inability to live up to his title, the "King of Rock 'n' Roll."