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## **THE ROLE OF RECORD LABELS IN THE DIGITAL AGE**

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### **Introduction**

Hello everyone and thank you to London Calling for inviting me to speak today. I'm lucky enough to lead the BPI, which brings together more than 350 independent labels as well as the four major record companies under one roof. In a nutshell what we do at the BPI is work together on the key things that affect all record companies and which can best be tackled collectively.

One of the great things about this job is that everyone has an opinion about what you're doing. And I mean everyone. A book by Dr Oliver Sacks (*Musicophilia*) recently showed that as human beings, we are hard-wired to love music. He said that "it lies so deep in human nature that one must think of it as innate .... music occupies more areas of our brain than language does ... humans are a musical species".

If only our Creator had gone the extra mile and hard-wired people to love the music industry, my job would be an awful lot easier. Because as we go through this transformation in how music is communicated to and between people, our business is under more scrutiny from the media

and the public than ever before. It's not always easy to communicate exactly what we do; and our audience - music fans who (just like us) connect emotionally and spiritually to music - doesn't always embrace the economic reality behind the music. That to be successful and sustainable, music needs a business infrastructure to support it, and that the smooth operation of that complex machine is vital to the quality and diversity of future British music.

This is a room full of people who spend their lives working in different ways to make British music a success, discovering it, promoting it, distributing it, publishing it, creating the business partnerships that connect talented musicians to audiences around the world, in person, on social networking sites, mp3 players, USB keys, mobile phones and more than a hundred million shiny bits of plastic every year.

What I'd like to talk about today is where record labels fit in to this matrix, and the positive future they have in the digital age.

Now, if you believed everything you read in the newspapers, you'd probably think the music business – or at least the part of it that I work for, UK record labels - are in terminal decline.

That's become the received wisdom. The thing is, that the received wisdom is so often complete rubbish.

I well remember the mid 90s, when the business world was convinced that as the internet took off, content was going to be king. Everyone assumed that media moguls would need bigger swimming pools in

which to park their new Bentleys. But that view underestimated the challenges that we now face in monetising digital content, something which I will be talking about later on.

And now, there has been a 180 degree turn. The received wisdom is that:

- The internet has democratised communications, so that in the digital age, all information, including music, is going to be free
- The business model of record companies is broken. That they're dinosaurs that haven't evolved and don't deserve to survive
- And that would be a good thing for music and our culture because they were parasites anyway.

These points of view are particularly prevalent in the blogosphere – a field of human activity where veracity and accuracy of course do not always hold sway.

It's up to us to explain why those points of view are wrong, why we've got an exciting future as a business, one that will benefit not just for those who make music, but everyone that loves music. So today I am going to going to look at where we are as a business, where we're headed, and how we're going to get there. And in doing so, I'm going to propose that it is time for a reassessment of the role of the record company in the digital age, one which understands that record labels make a positive contribution to the music community and towards building a future in which musicians and creators are fairly rewarded.

## [Where are we now?]

One thing everyone agrees about is that the distribution of music is undergoing a revolution. But exactly where we are in that process is more difficult to judge. The thing about revolutions is that while they are going on, there's smoke and bullets everywhere, the streets are barricaded, everyone's shouting and it's not easy to get your bearings or know what the world will look like when it is over. Even looking back at past revolutions, it is not always easy to say when they started or when they finished.

Ask a room of ten historians when the industrial revolution began and ended and you would get ten different answers. The same must be true for the *digital* revolution. All we know now is that we are right slap bang in the middle of it.

There are some road signs we can use to help navigate, even if parts of them are obscured. The CD business is gradually declining as more and more people switch to digital, both legal and illegal. But the pace of decline is often overstated - the album market is still bigger now than it was throughout the late 1990s and deluxe editions are becoming a strong market segment. The CD remains a fantastic product, easy to use, durable, with great sound quality, widely compatible, containing artwork, lyrics, and built-in back-up copy once it has been ripped – and the satisfaction of a tangible object. Research published by our friends at BMR shows that music lovers still place great value on the CD – the majority of people said that they would continue to buy CDs even if they

used a legal sharing or streaming service. Rumours of its demise have been greatly exaggerated.

Meanwhile, the growth of digital sales has not yet made up for the reduction in CD sales, but the figures are still encouraging. Just four years after the first major legal download services launched in the UK, we are now selling around 2 million tracks a week, and have already broken the 200m tracks barrier.

The singles market has led the way in digital, but the albums market is growing strongly. Sales of digital albums have increased by 65% in the first half of 2008 to 9% of total album sales. In the past year 8 million digital albums have been sold in the UK. In three days last week, Coldplay sold more than 30,000 digital copies of Viva La Vida – over 10% of its total sales.

In the first quarter of 2007, digital provided 8% of our trade industry income: but in the first quarter of 2008 this has already increased to more than 13%. So we have every reason to be proud of our progress in the digital market – we are certainly a long way ahead of every other digital content industry.

Yet in revenue terms the market is still in decline. Why is this? The reasons why digital sales have not yet offset the physical decline are complex. The ability to purchase single tracks rather than whole albums is a factor, as is competition for wallet share with other leisure products, in particular mobile phones, DVDs and games. But these factors alone do not explain what is going on. Independent research by Jupiter shows

that the single greatest factor holding back the digital market from reaching its astonishing potential is the scale of illegal downloading and sharing of music. There are more than one billion illegal downloads of music in the UK alone every year.

Now we often talk about this being a major problem for music companies – and it is – but of course another way of looking at it is that it represents the most amazing opportunity for the industry to seize.

Just occasionally a politician or journalist makes the mistake in meetings with me of drawing a comparison between the music business and the coal industry. I don't mean the metaphor that "the music industry is the canary in the coal mine of digital content", which is of course true when it comes to feeling the effects of illegal downloading, but the suggestion "aren't you just like the coal industry, your days are gone?". At this point my director of public affairs Richard Mollet tries to calm me down and stop me saying anything I'll regret later, because the comparison of course misses the fundamental point that demand for coal dried up because more attractive sources of energy became available. As far as music is concerned, nothing could be further from the truth. Demand for and interest in recorded music has exploded – the only issue is creating a mechanism for monetising that demand more effectively so that musicians, and those who invest in their careers, are fairly rewarded for the use of their music.

I'll come on later to how we are working towards achieving that goal, but it is important not to lose sight of the astonishing untapped potential that the music market offers.

And thankfully, the creative engine of our business continues to perform at the highest level. British music is selling strongly at home and abroad with acts like Coldplay and Duffy performing well in the US; and the British love of music remains exceptionally strong. British music fans remain the most avid collectors of CDs in the world. There is so much to play for in British music; so many factors in our favour which other industries would give their right arm to have.

But even with these fundamentals in place, we face an uphill battle persuading commentators that we are headed in the right direction and that this is a fight we can win.

So let's look at what they say.

### **[Taking on the Digital Utopians]**

First, they say that in the internet age, all music and all information is going to be free and that the "old fashioned" laws on copyright have no place in the digital domain.

A term that has recently been coined to describe this view is "Freetard". It's a bit strong perhaps – but contains a kernel of truth. I haven't yet seen a dictionary definition, but may I offer the following: "Noun. Pejorative. Individual who holds the ultimately self-defeating proposition that all content should be accessible for free on the internet, but who ignores – wilfully or otherwise – the obvious fact that such a system

would eventually result in no payment to creators and hence a massive reduction in creative output.”

Central to the ethos of these digital utopians is the belief that they are the future. Their view is that payment for creativity is an outmoded concept, belonging firmly in the ancient history of the twentieth century. The rules of economics are seen to have broken down some time around 1998 when internet protocols finally snapped the pernicious link between the words “intellectual” and “property”. It’s an anarchist view, but instead of wielding a Molotov cocktail and a typewriter, they wield a mouse and write blogs in their bedrooms.

No-one in the record companies that I know opposes a business model which, for certain uses, provides music to the consumer “free at the point of consumption”. There is nothing new about this, we have been providing advertising supported music for many years by licensing commercial radio. And now we are experimenting with ad-supported on-demand streams and even ad-supported free downloads. It is too early to say how these models will fare in the marketplace. But even this isn’t enough for the utopians – they don’t like the adverts. They believe that they should have the right to take all the music they want and no-one should get paid.

It’s time that we joined together to dismiss this preposterously naive view of the future. That there is no such thing as a free lunch is an economic cliché. But like all good clichés, it’s true.

And there's a larger issue here. It is simply not sustainable to believe that basic rules of civilised society, including respect for the law and for property rights, can just be suspended or ignored in the virtual world. Those rules exist and are supported in our society for good reason. It is becoming more and more clear that citizens, as much as creators, require protection from crime, fraud, abuse and other risks in the online world. As President Sarkozy put it recently "The Internet must not become a high-tech Wild West, a lawless zone where outlaws can pillage works with abandon or, worse, trade in them in total impunity. And on whose backs? On artists' backs".

Increasingly this is recognised in the UK too. Speaking at the Convergence Think Tank just last week, our Culture Secretary Andy Burnham said that "the internet shouldn't and mustn't sweep away all the values and standards that have served us well in the past"

Yes, the internet has launched a revolution in content distribution and we must all adapt to the changes that it brings. But some fundamental principles must stand – and that creators should be fairly rewarded for their work is one such principle.

### **[Record companies missed the digital revolution]**

Next they say that labels missed the digital opportunity and will die as a result.

In the blogosphere, this mantra is often the starting-gun for an invective filled account of how record companies were so busy trying to make money that they, well, didn't see a better way to make money.

And I'm not going to totally refute the charge. Like all other media businesses, we haven't got everything right, we didn't see everything coming or always back the right horse.

Now this isn't going to turn into a Soviet-style self-denunciation (though I know you'd all enjoy it!) because I don't think that's a surprise. As A&R departments prove week in, week out, people in record companies don't have crystal balls! In fact, it's a part of normal economic development that trends and important changes are not fully understood at the time. The boss at IBM who confidently asserted that the world would only need four computers did not foresee the power and potential uses of the PC. Even Bill Gates appeared to underestimate the importance of the internet, and spent the mid-nineties catching up with Netscape.

And an important factor that is usually forgotten in the debate is that, even if record companies had been more prescient, it was always likely that illegal distribution of music on the internet would get ahead of the legal alternative. Building legal platforms for the distribution of music required not just deploying a new infrastructure for digital music, but choosing and negotiating deals with commercial partners, digitising masters, providing accurate metadata, sorting out the clearance and administration of publishing and artist rights, making long-term decisions about pricing, track unbundling and technical protection, all of this in an environment of great uncertainty. It isn't realistic to think that this could

all be done in less time than it would take for free P2P software to become widespread.

Nonetheless, when I look back, naturally I wish that we had somehow managed to accomplish all of this faster and offer really compelling legal alternatives earlier than we did. But the world has moved on. Record companies most certainly do get the digital revolution now – they have licensed hundreds of digital services of all different kinds and, as I'll touch on later on, are experimenting with many different types of new business model. Indeed, of all the so-called content industries, we are now right in the vanguard of the digital revolution.

So can I say to those who continue to lambast us for our perceived mistakes in the past, yes you have a point. We've heard what you're saying, and we understand it. Now let's move the debate on and reflect where we are now.

### **[Role of the record company in the digital age]**

The final shard of received wisdom is that music will be better off without record companies anyway.

This sentiment explains why one can sometimes detect a sense of satisfaction when record companies' woes are in the news. An educated audience like this will know that the word for this is *schadenfreude*, not in fact of German origin but a Scottish term describing the feelings

experienced when England doesn't qualify for a major football tournament.

We clearly have work to do to explain to some music fans what it is that labels do and why they deserve to be supported. But it is more disappointing when similar feelings are expressed within the music community itself. There are certainly historic tensions between different parts of our industry that still reverberate today. And no doubt there are current tensions too. But I'd like to spend the next few minutes making the case that the difficulties facing labels are in fact challenges to all of us, and that the health of record labels is vital to the whole British music community.

To do this, we need to consider the role of the record label in the digital age. There are three areas that I want to explore: the continued relevance of the labels' core activities; second, the role of labels in helping to move the industry forward to embrace new business models; and third, their contribution in promoting and defending creativity by standing up for copyright.

## **[Our Role in the Music Community]**

So let's begin with the core activities of record labels. First, talent.

### Talent

Identifying and nurturing talent is at the centre of what we do. The A&R teams at record companies – alongside those of publishers – continue to act as the vital gateways into a professional career as an artist. This is

very important, yet often understated or mis-understood role. It is the function that any successful market needs: the brokering of supply and demand.

Music fans, especially British fans, have an insatiable hunger for quality and diversity. But, like consumers in any sector, they are limited by their available time. Music makers are competing for their attention against a huge range of other entertainment services. Record companies are the shop windows of the music world, simultaneously showing fans what is available and giving artists the platform to find an audience.

In this age of MySpace, Bebo and other social networking sites it has never been easier to get your music out there to the world. Distribution – which in the purely physical days was expensive and difficult to organise – is now the easiest thing. But ask anyone with a *low hit-rate website* about how easy it is to get real traction and you will know that it is not enough to just be “out there”.

Of all the functions which record companies perform, the identification, development and promotion of musical talent will never lose its salience. Not in the digital age, or whatever age may follow that.

### Finance

And of course, supporting new artists takes money. You don't have to read the FT these days to know that it is not a great time to be a bank. Loans have been made to people who are not able to pay them back, dealings between banks nearly seized up and business models like buy-

to-let mortgages, which until recently seemed full of great promise, have turned from being great assets to dangerous liabilities.

This digression has a point – and it isn't just to temporarily to make our concerns in the music business seem less worrying.

If it was not for the role that record companies play in investing in performers, then they would have to turn to the financial community for funding. Given its current tribulations it is clear that this would be a tough time for creators. Explaining to risk-management experts at a bank why investing in an untried and untested recording artist, whose chances of commercial success may be no better than the historic industry average of one in ten, would be a hard enough task in the best of times: let alone the worst of times.

Record companies' key role lies in providing an implicit understanding of the needs of the recording artist and the wherewithal to drive their career. They provide the financial support system for performers, that allows them to pursue music full-time, to record their creations so that they sound as good as they possibly can, and market, distribute and licence them around the world. No bank – even ones not troubled by the credit crunch – could do this reliably and with the understanding that a label can provide of the needs and motivations of the artist.

### Business Services

Even with the support of a record company at the beginning of your career, there is a great deal of business experience and resource still

needed to push it to the next level. Most importantly, promotion and marketing, but also negotiating the best deals possible with bricks and mortar retailers and a huge variety of digital partners, capturing international revenue from sales and licensing, providing tour support, ensuring that everyone who needs to get paid (songwriters, session musicians, producers) gets paid. These vital services are not well understood outside the music business and too often they are casually dismissed as just another middleman taking a cut. They are not, they are essential support for any artist's long term career and they are just as important in helping the wheels of professional music to turn in the digital age as they ever have been.

Let's be clear - I'm not trying to argue that record companies are more important in the music community than anyone else. My point is that the world of music is an eco-system in which we are all co-dependent. As labels we depend on the support of publishers, talented artists and songwriters, session musicians and producers of the highest quality and the excitement generated by live performances. But equally, without the continual investment of record labels into new music, to the tune of hundreds of millions of pounds every year, many of the opportunities that now exist for young artists, session musicians, songwriters and publishers, and live music, would simply not exist.

### Cross Industry Action

The BPI recognises how much we depend on each other. We have been working hard to build better relationships with other music industry organisations and I'm pleased to say that more and more there is now a

real sense of cooperation and common purpose between us. Last year we helped form the Music Business Group, which brings together the BPI, AIM, PPL, MCPS-PRS, British Music Rights, the Music Publishers Association, the Musicians Union, the Music Managers Forum, and the British Academy of Composers and Songwriters. The MBG has worked together to put in a joint submission in response to the Government consultation on copyright exceptions. As an example of cross-industry action, consensus and sheer hard work I don't think it has any comparison.

### **[The Future Business Models]**

We've looked at the core activities of labels and why they continue to be important in the digital age. But as the revolution continues, they have another crucial role to play. That's in innovating to help adapt our business to the changes in the way music fans now enjoy music.

As I've said, the UK's digital music business has taken great strides over the last four years. But at the BPI we believe that there is more we can do to legitimise and monetise a significant proportion of the illegal use of music and to offer better licensed alternatives to P2P filesharing.

The first aspect of this is harnessing the power of music to create and sustain online communities. More and more online social networks are emerging that use music as one of the key factor in establishing communities. Record labels are licensing services like Bebo, and

MySpaceMusic, bringing new revenues into the business and helping to add value to such services with previews, exclusives and so on.

The second example of this is supporting services that can reach music fans who may be time rich but cash poor, in particular in younger demographics. Services like We7, Qtrax and Spiralfrog are yet to have a significant market impact but labels are showing willing to experiment with new models that offer a licensed alternative to peer to peer.

Indeed, labels are diversifying rapidly and changing from companies that sell music by the unit into sophisticated licensing businesses with multiple revenue streams. The regular media reports about falling record sales are not yet taking into account the very promising growth in licensing of all types - synchronisation into games and films, revenues from ad-supported services, 360 deals and so on. The BPI is now collecting data on income from these non-traditional revenue streams and hopes to be able to release market figures for the first time over the coming months.

The next step is working in partnership with ISPs to develop new music services for UK broadband customers - services that we think could offer even greater value for regular music fans than a la carte purchases, plus the ability to explore and possibly share music with other subscribers, but which still make sense as an economic proposition for the music community. Crucially, such services could allow ISPs to increase revenue and reduce churn, by sharing in the value that can be realised from converting illegal filesharers into subscribers to new legal music services.

There is no single “right” model for what such services could look like, and BPI members are exploring various possibilities with a number of ISPs. While discussions are ongoing and there remains much work to do, we are hopeful that some positive announcements will start to come through in the second half of this year.

### **[Protecting and Promoting Creativity]**

The third important role, indeed responsibility, for record companies in the digital economy is to stand up for the right of everyone in the music community to be paid for their work.

In many ways, this is the flip-side of creating future business models. You cannot have one without the other. The mass availability of free music on P2P networks and from other illegal sources strangles the prospects for new music services that do want to fairly reward creators, and stops them reaching the penetration, or realising the value, that they ought to attain.

We firmly believe that two vital components of dealing with this problem are building new business partnerships, and doing even more consumer education than in the past.

A good example of this approach is the BPI’s recently announced education initiative with Virgin Media. In a joint campaign, we will provide Virgin with publicly available information about illegal music sharing by customers on its broadband network. Virgin Media will then write to the

customer to give them the information they need to prevent it happening again.

This initiative will help to inform and advise thousands of UK broadband subscribers about copyright on the internet and how they can enjoy music legally online. It's a very positive first step in the right direction, but obviously we will need many more such steps if we are to have a real impact on the scale of illegal filesharing in the UK and create a better environment for new legal digital music services to succeed.

So this is the inevitable section where I bang on about service providers, because the role of ISP's is crucial in tackling illegal downloading and creating an internet which fairly rewards creators.

The good news is that almost everyone now recognises that mass filesharing of music is against the law, is seriously damaging the music sector in this country and that urgent action must be taken. The government thinks it, Parliament thinks it, many ISPs acknowledge it and responsible consumers accept it. The debate is no longer around whether something should be done, but precisely what should be done.

Our position is very simple. We believe that where ISPs have information that customers are using their broadband service to distribute music illegally, then they have a legal and a social responsibility to prevent it from happening again. Dealing with this issue at a business to business level is greatly preferable – for consumers, ISPs and the music industry – to having to take action against individual filesharers. Our goal should be to try to prevent illegal activity occurring

in the first place, through education, making available great new legal services and proportionate dissuasive measures that can encourage people who are currently filesharing to use licensed services instead.

The BPI's approach is to be pragmatic in finding solutions, not dogmatic. We are engaging in a dialogue with ISPs that are willing to talk to us, and with Government, which has committed itself to enacting legislation to require ISPs to take action to deal with illegal activity on their networks, unless a voluntary agreement is swiftly found.

We have already proposed a simple, non-technological solution which doesn't involve ISPs spying on their customers or invading their privacy. We call it three steps. After a first guidance letter, continued illegal activity would result in a temporary suspension of an account, and if a second warning is also ignored, then the ISP's terms and conditions allowing for cancellation of the contract should be applied. But we are also prepared to look at the use of technology by ISPs that will effectively prevent illegal distribution of music by their customers.

It is encouraging that a few major ISPs are engaging in a constructive dialogue to find such solutions. But we must also be prepared to stand up for ourselves and take action where necessary against ISPs that take the position that illegal filesharing by their customers on their network is nothing to do with them.

Unsurprisingly, there are sometimes differences in emphasis amongst us as to how best to reach our objective of ISPs playing a responsible role in tackling illegal downloading.

But we all share the goal of ensuring that music is valued and respected in our culture; that creators are fairly rewarded in the digital age; and that the future of British music shines even more brightly than its scintillating past. I believe that's a cause worth fighting for, and a goal we can achieve if we stand together.

## **Conclusion**

In the digital revolution, labels are not defending the ancien regime, they're insurrectionists themselves.

In fighting for change, we remain true to the principles that music is precious, talent should be nurtured, and that creativity must be rewarded and protected.

People love music because it is an inherent part of themselves. I believe that, working together, we will ensure that the digital revolution will unlock new value in music, which music fans and the music business will share.

Thank you for listening.