Written evidence submitted by the Entertainment Retailers Association

SUBMISSION TO DIGITAL, CULTURE, MEDIA & SPORT SELECT COMMITTEE

INQUIRY INTO THE ECONOMICS OF MUSIC STREAMING

ABOUT ERA

The Entertainment Retailers Association, founded in 1988, represents both digital services and physical retailers of music, video and games.

In music its members include Amazon, Deezer, 7digital, SoundCloud, Spotify and YouTube as well as physical retailers such as HMV, supermarkets including Asda, Morrisons, Sainsburys and Tesco and more than 200 independent members.

Its wide range of members and its 30 year history encompassing the decline of the cassette, the rise and fall of the CD, the emergence first of downloads, streaming and the vinyl revival put it in an ideal position to comment on the economics of music streaming as well as the contribution of streaming services to the wider music industry.

Its core objectives – published as the ERA Manifesto in 2015 and updated in 2018 – include putting the consumer and the creative community at the centre of its concerns.

SUMMARY

All music technologies change music – and the music business. The concept of the 'album' did not exist before the invention of the vinyl LP. Likewise albums were time limited to around 40 minutes until the invention of the compact disc (famously set to the length of Beethoven's Ninth Symphony – 74 minutes).

We should not be surprised that the advent of a dramatically new music technology – on-demand streaming – should have an impact on music and the music industry. Fortunately that impact has been overwhelmingly positive:

- Encouraging millions of music fans to commit to monthly subscriptions;
- Increasing the accessibility of music;
- Providing a platform for emerging artists to find new listeners;
- Generating billions in revenue for the music industry;
- Reducing piracy;
- Creating new high-skilled jobs.

Around 70% of the more-than-£1bn-a-year revenue generated by streaming goes straight to the music industry via licence fees. However, the biggest economic impact of streaming relates not to the quantum of payment, but to the fact that the revenues are divided up based on consumption – on each play of a track.

To put it simply, artists and songwriters are paid the same for a CD regardless of how many or how few times the buyer chooses to play it. In a streaming world, they are paid based on listens to a track.

For artists and songwriters, by definition that creates a change to cash flow –their remuneration is generated over an extended period rather than upfront. By allowing an unlimited amount of artists and tracks to be offered - as opposed to the limited shelf space of physical retail - streaming also means that a much larger number and diversity of artists benefit from the streaming revenues.

Contracts with artists have had to adapt to the streaming model and many creator contracts were struck in a pre-digital world so it is little wonder that the switch to streaming has been challenging for some music makers, highlighted by the recent debates over #brokenrecord and #fixstreaming.

As providers of a service to listeners, streaming services are not typically in the business of signing artists or songwriters or contracting session musicians or producers. Remuneration of these creators is for record companies and music publishers to address within their direct contracts.

Building a streaming service requires substantial and long-term investment. Profitability for most services is still some way off. But by returning to health a recorded music industry which was on the ropes thanks to piracy, and delivering literally billions of pounds of new money to the music industry, ERA believes the advent of on-demand streaming has been overwhelmingly positive for music and music fans alike and has enabled a greater number of artists and songwriters to be paid for their art.

WHAT IS STREAMING MUSIC?

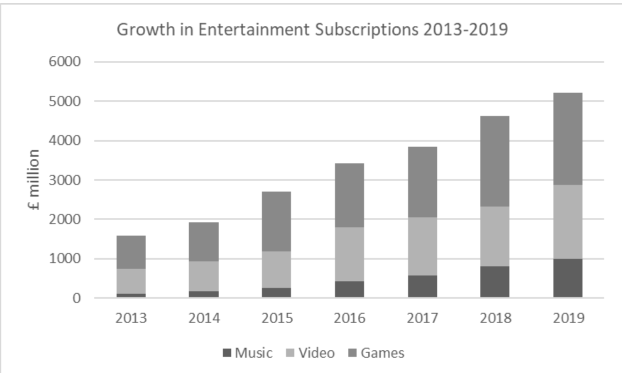
In technical terms streaming means listening to music or watching video in ‘real time’, instead of downloading a file to your computer and watching it later.[1] A stream of music is a stream of data which only exists as it is being listened to (although most services have a facility for subscribers to download a music file for listening to offline).

Streaming is an access model rather than an ownership model, ie unlike buying a CD or a download, paying a subscription to a streaming service does not give the user ownership of an object or file, rather it confers the right to continue listening from the full catalogue available as long as the subscription is current.

WHAT IS THE STREAMING BUSINESS MODEL?

The vast majority of streaming income is generated through selling subscriptions, with an individual subscription costing a typical £9.99 a month. Many services also offer free-to-the-user advertising-funded streaming, often designed as an entry point to a paid-for service.

Subscription models have been enthusiastically embraced by consumers in all areas of the entertainment industry such as music, tv and film, and games as shown below.



Subscribers to these services pay for access to a huge catalogue, much of which they do not use. Subscribers understand and accept that the subscription payment covers access to all the content made available to them regardless of how much or how little they choose to use.

Like many internet-based business models, music streaming normally requires huge scale to operate successfully which means all of the major streaming services operating in the UK also need to operate on a global scale.

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[1] Definition courtesy of BBC Webwise

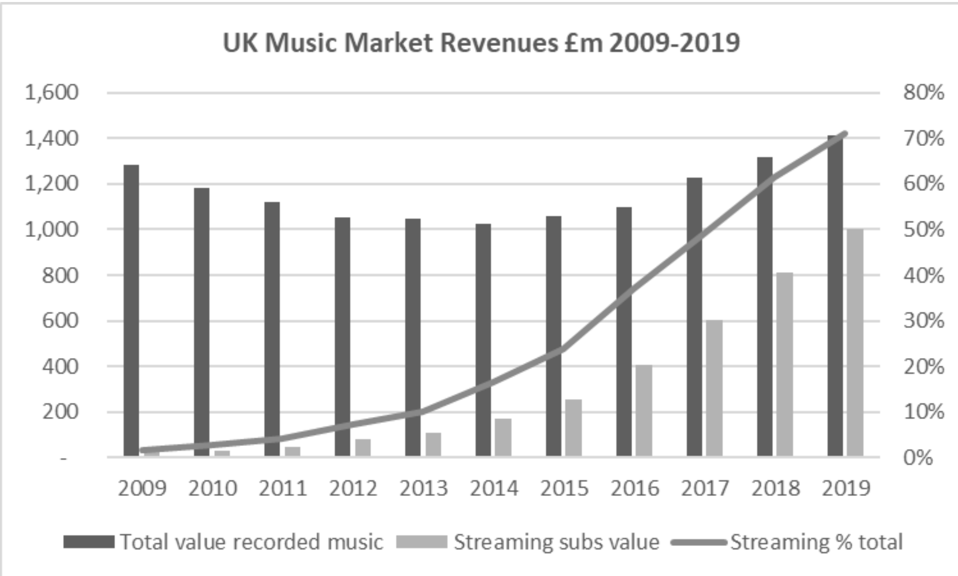
While a single-location physical record store selling a few thousand lines can be profitable, the huge technical infrastructure behind streaming services requires millions of subscribers to succeed. DSP's employ hundreds of UK based staff in areas as diverse as artist marketing, editorial, technical, PR, legal, licensing and customer support.

All of the benefits delivered by streaming services to the UK music industry outlined in this submission – not least the more than £3.5bn in revenues delivered by streaming services over the past decade – have essentially been funded by investment either from new players like Spotify, Deezer and SoundCloud or by existing technology companies such as Amazon, Apple and Google / YouTube.

The result of this investment has been a boom in profits for music companies with the three largest increasing profits by an aggregate 44% between 2017 and 2019 to more than £2bn a year. In contrast the streaming services are still in a long term investment phase with the largest pureplay streaming company, Spotify, having cumulative net losses of $2.7bn.

WHAT STREAMING SERVICES HAVE ACHIEVED

Growing the UK music market



The launch of Spotify, the first mainstream subscription music streaming service, in late 2008 came seven years after the UK music industry's CD-era peak. During that time, digital piracy had exploded in popularity and the sector had lost hundreds of millions of pounds in value.

But from the low point of 2014 the value of the UK recorded music market has grown every year thanks to streaming. Between 2015 and 2019 streaming increased the value of the UK recorded music market by 38%. None of this increase would have happened without the investment of streaming companies.

Streaming now makes up more than 70% of UK recorded music revenues.

The result is that since 2009 streaming services have generated new revenues for the UK recorded music industry totalling £3.5bn.

With recurring revenues

In a business traditionally subject to boom and bust, streaming provides predictable and growing long-term revenues, enabling artists and songwriters alike to continue to earn money decades after initial release. These revenue streams have led to higher valuations for all involved in the music industry.

In October 2019 Rolling Stone reported that Oasis's 'Wonderwall' was generating around 600,000 streams a day on Spotify alone. 25 years after its release, it is grossing around $1m a year, a feat it would have been impossible to achieve in the physical world.

Enabling more musicians to be paid

Meanwhile UK-based independent digital distribution company AWAL revealed in Summer 2020 that "hundreds" of its clients are now earning over $100,000 a year from streaming, with the total growing 40% in the previous 12 months.

While the physical world focuses attention on a relatively small number of record company priorities, typically focused on the Top 40 charts, streaming enables many more artists to earn from their music.

The trend is brought into sharp relief by Official Charts data which shows that in the year 2019 it took 10,662 artists to account for 90% of UK streams, while over the same period just 2,890 artists accounted for 90% of physical record music revenue.

In other words more than three times as many artists share in that top tier revenue pot in the streaming world as do in physical.

Reaching more people

UK consumers are often early adopters of new technologies and recent ERA data demonstrates clearly how the UK population has embraced music streaming. More than 30% of the UK population now use a paid-for subscription music streaming service, rising to an astonishing 84.3% of under-25s. Importantly streaming is no longer restricted to the young and in May 2020 data from ERA's authoritative quarterly consumer tracking study showed that over-55s were the fastest growing demographic in streaming over the past 12 months.

In the pre-streaming era no more than 57% acquired music legally. Many were one-CD-a-year buyers. Streaming is turning even casual fans into £120-a-year - the typical annual price for a subscription - subscribers.

PERCENTAGE STREAMING BY DEMOGRAPHIC GROUP (May 2020)

Streaming	Total	Males	Females	Under 25s	25-34	35-44	45-54	55+
Subscription Streaming	30.8%	31.7%	29.8%	84.3%	50.5%	35.8%	26.4%	14.0%
Free Streaming	24.4%	23.6%	25.3%	77.8%	28.0%	22.7%	17.5%	14.6%

Source: ERA Quarterly Tracking Study

Making more music available

One of streaming's key impacts derives from the sheer scale and diversity of the repertoire it now makes available, benefitting musicians and music fans alike, and driving cultural diversity across the music ecosystem.

As of autumn 2020 the leading services provide access to more than 60m tracks, a number which rises every year as the openness of streaming platforms encourages more and more musicians to release tracks.

In contrast, at the height of the CD boom, a typical record store would stock over the course of a year no more than 50,000 album titles, the equivalent at a typical 10 tracks per album of 500,000 tracks.

This huge increase in availability allows a diversity of new artists to be heard on a global scale, it means established artists need never fear their music going "out of print" and it delivers for consumers instantaneous access to the entire history of recorded music.

By curating content

Like record shops who curate titles for their local customer base, DSP's offer a variety of curation models to aid discovery. These can be based on algorithms, human curation and so called algotorial (a combination of algorithm and human). All DSPs employ a combination of these tools with the aim of creating a better user experience, enabling users to discover music most relevant to them.

Unlike radio, where the radio stations serve tracks en masse to listeners, with playlists DSPs create a personal one-to-one experience. It is not the service that drives the algorithm but essentially the customer's use of the service, thereby increasing personal curation and adapting to consumer tastes.

On more devices

Thanks to investment from streaming services, music can now be enjoyed on a far wider range of devices than its physical forebears, meaning music has achieved its 'Martini moment', able to be enjoyed 'anytime, anyplace, anywhere'.

In May 2020 ERA's tracking study which has measured the entertainment consumption habits of a panel of 2,000 UK consumers for the past seven years, identified a record 10 device types now used to stream music, from phones to gaming consoles to smart speakers.

Defeating piracy

At its low point 15 years ago, music consumption became dominated by piracy, predominantly illegal filesharing. International record companies trade association the IFPI claimed in 2008 that piracy accounted for 95% of consumption, meaning the effective price for music at that point was zero.

Streaming services have helped significantly reduce piracy by offering a convenient, value-for-money alternative which is better than the pirates. Ad-supported platforms monetize users who may otherwise have sought out pirate services with rights owners able to share in the advertising revenue generated. Additionally technology like YouTube's Content ID allows rightsowners to share in the advertising revenue from videos which include their music.

The 2018 *YouGov Music Report* revealed that just one in 10 Britons were downloading music illegally, down from 18% five years previously.[2]

Such statistics support the ERA view that the advent of streaming services rescued the UK music industry from what looked like terminal decline.

HOW THE MONEY FLOWS IN STREAMING

The vast majority of streaming revenues derive from subscription streaming in which consumers pay a typical £9.99 per month for unlimited access to as many streams of individual tracks as they choose.

A typical split of those revenues based on full price subscriptions is as follows:

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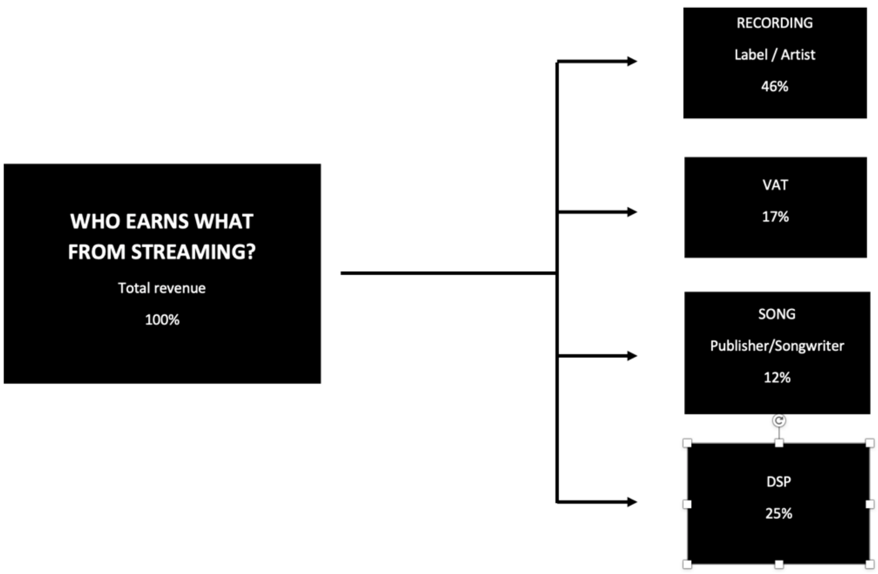
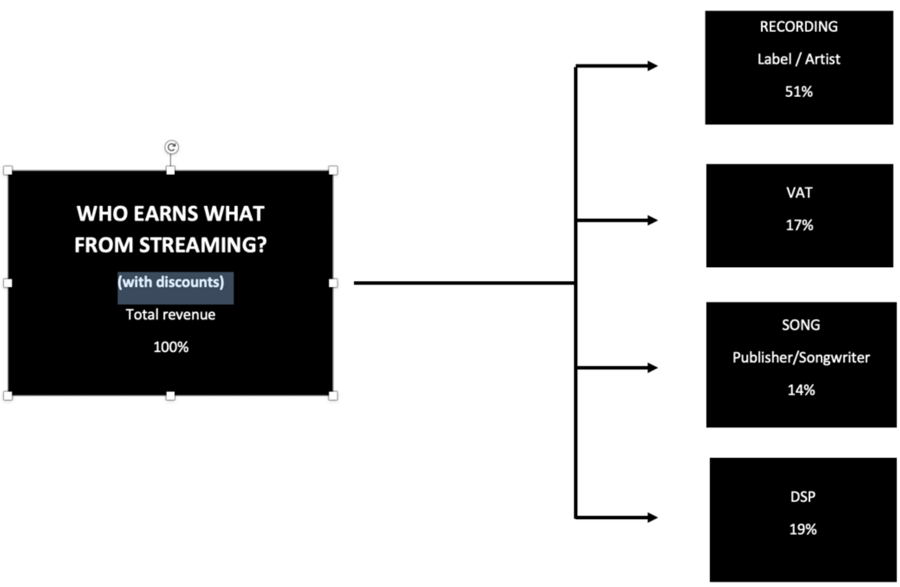
[2] https://yougov.co.uk/topics/arts/articles-reports/2018/08/02/number-britons-illegally-downloading-music-falls



However, in order to encourage customers to sign up to paid subscriptions many services offer free trials and other incentives, which reduces the average subscription value received by them, whilst leaving the payments they make to content owners unaffected. Therefore, the actual margins look more like the below:

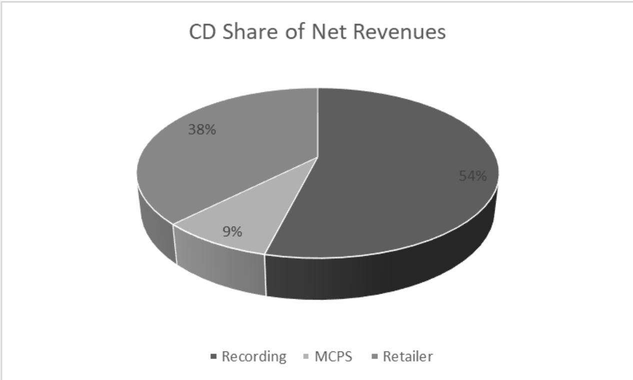


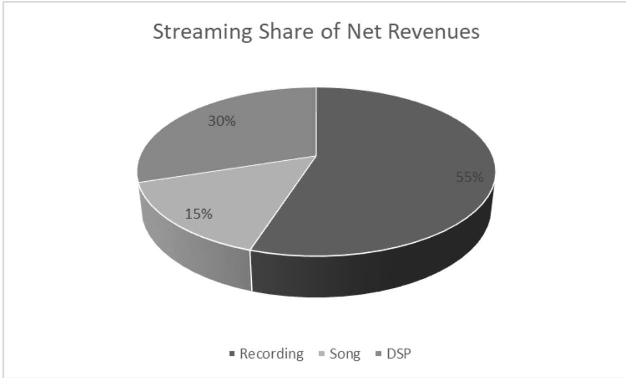
The recorded music industry typically receives therefore between 70% and 78% of the net DSP revenue.

This equates to two thirds of the retail value being paid to the creators with the largest share – over one half going to the recording.

Net margins in music streaming are similar to those for CDs and downloads

Net retail margins in streaming services of around 30% are lower than those in the CD world, where net retail margins average around 38%. This is despite the fact that DSP's take on a larger marketing role in the streaming ecosystem, not just satisfying demand, but also helping drive it.





Gross margins in music streaming compare poorly to those in adjacent sectors

Music remains an expensive acquisition for services. Whilst Spotify and other audio streaming services have yet to deliver profits, similar subscription-based companies like Netflix and Sky in adjacent sectors such as video deliver margins of 13% and 11% respectively.

There is no fixed price for a stream

Some of the confusion about the economics of streaming is caused due to misunderstanding about how revenues to recordings and songs are allocated. Rather than paying a fixed price for each stream, the DSP hands over typically 70% of net revenues to music companies. This means the revenue generated by each 'click' varies according to:

1. The total value of the subscription 'pot' each billing period;
2. The total number of streams generated within that period.

In simple terms, if subscribers choose to stream more tracks, the effective earnings per stream will decrease as the same revenue pot is divided among a greater number of streams.

It is in the music industry's interest that streaming services keep streaming users' engagement high to retain subscriptions. The more 'sticky' the service – ie the more subscribers use and engage with it – the more likely they are to continue to subscribe.

Most subscriptions renew on a monthly basis and can be cancelled at any time if a subscriber feels they are not getting value for money. Streaming services have to constantly innovate and develop their service to ensure subscribers continue to see value in their subscription. All of which adds to the cost of running a streaming service.

While the implied 'per stream rate' may fluctuate, overall streaming revenue continues to go in only one direction – up!.

HOW THE VALUE OF A STREAM CAN VARY MONTH TO MONTH					
Month 1		**Month 2**		**Month 3**	
Notional cost of subscription minus VAT	£8.33				
Subscribers	1,000,000				
Gross Revenue Pot	£8,330,000				
70% payable to music industry	£5,831,000				
Number of streams	1,110,000,000				
Value of stream	0.0053	Month 2			
		Opening revenue pot recurring subscriptions	£5,831,000		
		20% off subscription offer	£6.66		
		Added subscribers	100,000		
		Added revenue (70%)	£466,480		
		New monthly pot	£6,297,480		
		Number of streams	1,165,500,000		
		value of stream	0.0054	Month 3	
				Opening revenue pot recurring subscriptions	£6,297,480
				Return to regular subscription price	£8.33
				Added subscribers	75,000
				Added revenue (70%)	£437,325
				New monthly revenue pot	£6,372,480
				No of streams	1,165,500,000
				Value of stream	0.0055

How do streaming services account to the music industry?

As noted above, around 70% of the net of VAT money consumers pay to streaming services is paid to the music industry in a ratio of broadly four-to-one in favour of the recording rather than the song.

At the end of each billing period, each streaming service calculates the total value of the ‘pots’ due to recordings and to songs. These are then divided up between rights owners on a pro rata basis according to the proportion of streams each of them represents on the basis of their individual contracts with the services.

In other words if Record Company A’s artists generated 25% of the streams that month, in simple terms Record Company A receives 25% of the recordings pot. If Music Publishing Company B’s songwriters generated 25% of the streams that month, they receive 25% of the songs pot.

The record company then distributes money due to artists according to their contracts. Likewise music publishers distribute to songwriters.

In providing a service to listeners, streaming services typically have no direct financial relationship with artists or songwriters, and are not privy to those contracts.

Informally industry sources tell us that artists typically receive between 20% and 50% of the recordings pot from their record labels, while songwriters typically receive 50% to 80% of the song pot from music publishers.

Streaming services have no influence on these contractual terms.

DO WE NEED TO #FIXSTREAMING?

As noted above, it is no surprise that a new technology not only creates new opportunities, but also creates challenges for existing business practices.

In particular the change from a transaction-based ownership model to a subscription-based consumption model changes the economics of the remuneration of artists and songwriters.

ERA believes that the impact of streaming on the music industry has been overwhelmingly positive, returning a declining business to growth and creating an entirely new sustainable ecosystem at no cost to the creators.

There are many examples of artists for whom streaming has been extremely beneficial to their careers. For example, Irish singer-songwriter Dermot Kennedy where the media credits Spotify with launching his career and generating income for him of over Euro 20,000 per month and Lewis Capaldi (the top selling artist in 2019), whose manager first discovered him on SoundCloud.

Nevertheless ERA has some sympathy with those arguing that streaming is not working for them.

Some impacts of the streaming revolution are probably unavoidable.

The increasing competition as new tracks fight for attention against 60m other recordings probably makes it inevitable that more and more songwriters collaborate on hit tracks. 'Havana' by Camila Cabello, for instance, has 10 songwriters listed. 'Uptown Funk' by Mark Ronson feat Bruno Mars has 12 writers listed, while Liam Payne's 'Strip That Down' feat Quavo features 15.

Dividing a songwriter royalty by 15 clearly impacts songwriter incomes.

Again it is probably unavoidable in an age when 60m tracks are simultaneously available on streaming services that not all artists and songwriters will earn a living through their music. The only guaranteed way to increase average remuneration would be dramatically reduce the choice of music available on streaming services, but we do not believe this would be in the interests of artists, songwriters or music fans.

ALTERNATIVE BUSINESS MODELS

There has been much discussion in the music industry over the past year about the potentially positive impact of so-called user-centric licensing in which subscriptions and streams are not aggregated together and then divided, but allocated on a subscriber-by-subscriber basis, such that if a subscriber played only one track over the course of a month, all of the proceeds of their subscription would go to that track.

ERA members are open to providing data to enable the industry to analyse the effects of adopting user-centric licensing, although test data suggests the impact varies service by service dependent upon the nature of their users.

What is clear is that any change in methodology will not increase the overall revenue, rather it will move revenue from one group of musicians to another.

A number of streaming services feel there is considerable complexity in producing royalty statements on a user centric basis which could hamper transparency as well as increase processing and supply chain costs.

There has also been recent discussion about so called "equitable remuneration" in relation to certain types of streams. For us this is about the division of the pot.

It is ultimately for record labels and music publishers to decide how they divide the pot they receive with artists and songwriters.

CREATING A BETTER STREAMING BUSINESS

ERA understands that streaming raises questions over historic business practices and the manner in which labels and publishers allocate revenues.

Whether it be the poor quality of industry metadata which creates delays, how revenues from unidentified streams are divided up, blockages in payment or the slow speed of payments and high level of commissions through some collection societies, there are a number of significant steps which could help the music industry make the best of the opportunities presented by streaming.

With over 70% of net revenues going straight to the music industry, it is for labels and publishers to address best practice with regards to revenue sharing. ERA is willing however to play its part in operational discussions and is happy to put itself at the disposal of the Digital, Culture, Media & Sport Select Committee.

ERA CEO Kim Bayley would be happy to appear before the committee if required.