

# How does the new music economy work?

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## Abstract:

The music industry has changed dramatically over the last ten years, particularly with the introduction of online streaming services such as Spotify. In this essay I will answer the question; “How does this new music economy work?” I will explain how artists make money and also answer; “What is the economic cost of such streaming services?” I will use the economic theory of economic cost and opportunity cost to evaluate whether it is worthwhile for artists, giving a conclusion and an answer to my questions.

Before everything went digital and there were no such platforms as iTunes or Spotify, artists could easily work out how much they were getting paid. Someone would purchase a CD or Vinyl in a record shop for £10, and then a few months later a few pounds would feature on the artist's loyalty sheet. Then iTunes arrived and it was even easier; someone could purchase a single track online and then pennies would be transferred into the artist's bank account. Long gone are those days of simplicity.

"Today, music fans play free music videos on YouTube, stream songs for free on Spotify, MOG or Rdio, customize internet radio stations on Pandora or Slacker and consume music a zillion different ways. The fractions of pennies artists make for each of these services are nearly impossible to track – at least for now." (Steve Knopper, 2011)

Spotify generates revenue from advertising on their free service and from consumers who pay for their tiered subscription service. While the free service is only available on PC or Mac, a premium account allows users to stream tracks online using mobile devices such as smartphones or tablets. This constant online streaming service has now almost eliminated the need for a physical copy or even a saved digital copy of the music, freeing up memory on devices for other tasks. This is why Spotify has attracted over 24 million active users and 6 million paid subscribers (Darren McNarra, 2013)

Spotify's website explains how artists receive royalties; "In general, however, Spotify pays royalties in relation to an artist's popularity on the service. For example, we will pay out approximately 2% of our gross royalties for an artist whose music represents approximately 2% of what our users stream. A popular song or album can generate far more revenue for an artist over time than it historically would have from upfront unit sales." (Spotify, 2013)

In recent times Spotify has been criticised over this royalty process. Thom Yorke, famous for his band Radiohead and now Atoms For Peace, has removed all his new material from the website in protest over how much new artists receive in royalties. He is not alone in the debate, as The Musician's Union, the biggest musicians' union, is pushing for a pay agreement modelled on royalty schemes paid by BBC and commercial radio stations. The debate has now been featured heavily in the media, including music magazines such as NME and The Rolling Stone and online on Twitter and Facebook. From looking online, listening to radio and reading magazine articles with different artists and even talking to my friends who have their music on Spotify, I feel I now have a good enough amount of knowledge to draw a conclusion.

New musicians are receiving very little revenue from the service, as most money from royalties goes straight to the label and distributors. On the other side of the spectrum, more established artists, such as The Rolling Stones or David Bowie, are able to generate large amounts of revenue due to the scale of their back catalogues and writing credits. Smaller bands do, however, have a say on whether their content is available to stream. This is where I will answer the economic cost of the streaming services.

Economic costs are different from accounting costs as they include opportunity costs. "The opportunity cost of any activity is the sacrifice made to do it. It is the best thing that could have been done as an alternative." (Sloman, Wride and Garratt 2011:8) Therefore, the economic cost to an artist offering their music to stream on Spotify would be the next best alternative that they give up in doing so. This will then include any decrease in album sales due to consumers or fans choosing not to buy an album or track and instead using Spotify

where the artist will receive less money in royalties. The cost will also include any costs of using a third party distributor, which is paid for by the artist unless they have a record deal.

However, there is also a cost to the artist if they do not choose to stream their songs on Spotify. This is why there is much debate over the amount of royalties an artist can receive from Spotify. If an artist has music on Spotify this gives them another outlet and opportunity for exposure to new fans, which is particularly useful because Spotify recommends music to users based on music tastes. The cost of giving this up could be very important to smaller, relatively unknown artists. Some people think of this as Spotify actually offering a service to artists in that it raises brand awareness; especially important in today's music industry, as artists' second or foremost revenue stream is from concerts and live gigs.

So a cost-benefit analysis of whether an artist should boycott (like Thom Yorke) the service and push for higher royalties, or upload their music onto the application, weighs up the exposure from the service to the band combined with any royalties (however small) against the potential loss in royalties from consumers using Spotify and any distribution costs.

In conclusion, having weighed these facts up, I believe that for new bands it is incredibly beneficial to use the Spotify service: it allows consumers to listen to their music for free and then, from that experience, they can decide whether it will be worthwhile purchasing a physical copy of the album via CD or Vinyl, and also decide whether it is worthwhile paying to go see the band live in concert. I personally choose to use the free Spotify service along with other applications such as Soundcloud to stream music before purchase, and I regularly spend between £10- 40 on music and gigs each month. The service has also introduced me to bands which have now profited from my consumption.

Something which also needs to be considered is that there is competition to free online streaming services, in the form of illegal downloads which make up the majority of downloads in the music industry. Spotify has offered a free legal alternative to illegal downloads which will help reduce illegal activity and zero artist royalties.

Looking at the music industry as a whole and not just sales, downloads or streams, one must also consider the revenue received from live concerts and merchandise. I listened to an interview of recent successful DJs Disclosure, where they revealed that they feel that artists should not be concerned with sales as priorities anymore, as the majority of the money in music is to be made in live concerts and merchandise. In the past, touring would be an outlet to promote the album; however, the industry has now flipped and album sales or streaming are devices to promote the tour, where most money is made through ticket sales and merchandise. Calculating the value of a band or artist through charts is nearly impossible. Instead multiple indicators are needed; Youtube video views, Facebook likes, Twitter followers, Spotify plays, Itunes downloads, Cd/Vinyl sales, illegal downloads and finally ticket sales and merchandise.

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