MA MUSIC BUSINESS MANAGEMENT

Centre for Media Arts and Design

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FINAL PROJECT REPORT

MUSM 97

'Can creativity flourish within a publicly quoted music company?' An examination of the relationship between finance and creativity within the "major" and independent music companies

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SECTION 1

Executive summary

The problems and objectives

There is an almost ubiquitous belief pervading the media that the music industry is in decline.

The most common explanations, for this apparent decline include global piracy, the affects of the Internet, peer -to -peer file sharing, a declining teenage market or competition from other leisure activities. This report will explore a different explanation for much of what is wrong with the industry and will suggest that many of these fundamental problems stem from the "major" music conglomerates that dominate the industry. It will examine the relationship between these behemoths and the estimated 90% of SME's [1] that comprise the bulk of the creative energy of the industry.

Analysis - This report is an attempt to examine many of the fundamental issues affecting the industry. It will examine the pressures placed upon record labels owned by the media conglomerates. It will focus on an issue rarely addressed within the financial or music business press, namely that there is relationship between the source of external finance and the degree of entrepreneurial creativity within music companies. The report will look at some of the successful creative and innovative independent record companies (including Chess Records, Motown, Beggars Banquet and Creation Records). It will also try to explain why most independents fail eventually and examine why they function so well - even if only for a brief period of time and why they usually end up being acquired by the 'major' conglomerates who are rarely, if ever, able to replicate their success.

A very significant part of the report will review the structure of a typical music business conglomerate and the relationship such a company or more commonly its parent company has with the stock market. It will attempt to show how that relationship affects the structure of a music company and produces pressures that affect the quality of creativity within the company and for which the author has developed a concept of a "creative bankruptcy spiral". This concept is intended to show graphically how a major music corporation can spiral into a vortex of increasingly short term signings gradually producing smaller returns and leading the company into signing yet more short term acts with even less long term potential. It will also raise the question of whether the separation between management and shareholders / owners, that defines a corporation, in fact contributes to (if not directly causes) the lack of long-term creativity within the music conglomerates.[2]

It will also cover some of the additional factors, unique to corporations, which contribute to the constant financial pressures applied to the management of these "major" corporations. It will examine the link between the external pressures placed on publicly quoted Music corporations and the implementation of and insistence on short -term creative strategies.

The analysis will include a review of the external financial pressures placed on the multi-national conglomerates. How these pressures develop into a downward spiral affecting all the various stages of record production, signing and developing creative talent and planning a long term roster of sustainable artists.

Recommendations/Solutions - There are examples of "major" labels that have bucked the trend and it will be worth looking at how they have prospered even within the current climate. There appears to be a significant difference between Bertelsmann's BMG Music and AOL Time Warner's Warner Music Group with one adapting to the changes within the global industry and the other floundering. Is it the culture of the labels or the overall strategy of the corporation that is responsible for their success?

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[1] Anonymous, "Creative, Media & Arts - Music". www.culture.gov.uk/creative/music/html

[2] A marked difference between the independents and the majors is in the turnover of their senior management staff. Contrast the names of senior staff at established independents like Warp or Beggars Banquet (and even Virgin Records in its independent hey day) with the regular hiring and firing of the most senior executives at most of the major labels.

Table of Contents -

SECTION 2

Introduction -

Background -

The global music industry has been severely criticised within the financial press and attracted little sympathy for its stance on P2P file sharing by the music media. What much of the press ignores is that the music industry as a whole has global revenues of $48 billion[3] with the record industry achieving an annual global turnover of $34 billion.

After the period of constant sales growth between 1982 and 1999 that accompanied the rise of the CD as the dominant format, it would hardly be surprising if the global music industry has expanded as far as it can.[4] Certainly this might be the case as far as sales of pre-recorded music are concerned. When Sony sacked their C.E.O. Tommy Motolla, one stock market analyst described this as an 'end of an era' symbolising the end of the 'old way of doing business ' in a declining record industry.[5]

Has the music business peaked? Is it really in decline? What might really be taking place is the decline in the role of the multi -national conglomerates that have dominated the industry over the past 30 years. These "majors" may be in decline, not because they lack the resources, but because their parent companies no longer see the music business as the "cash-cow" [6]it used to be. Maybe they feel the industry has become too risky or volatile and in the current economically uncertain times, it has become unpredictable.

One accusation that can be made of the "majors" is that they are too "short term" in their thinking and in the kind of talent they acquire and develop. According to Robert Sandall;' *This charge of short-termism on the part of big companies more interested in making their figures than in developing careers is widely voiced*'[7]

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[3] Scott, Ajax, 2003, 'Report values global industry at $48 billion', Music week, January 11th, page 1

" The value of the global music industry hit $47,6 billion in 2001, according to exclusive new research" "The figures which cover revenue streams including pre-recorded music sales, music publishing, ticket sales for live events, merchandising and event sponsorship"

[4] Sandall, Robert, 2003, 'The day the music Industry died', The Sunday Times

"Global sales of recorded music have fallen in value by 12% since 2000. "

[5] Edward, 2003 'Sony pulls the plug on its pop playboy', The Observer Media Section, January 12th

[6] Negus, Keith 'Music Genres and Corporate Cultures', Routledge 1999 page 48

[7] Sandall, Robert, 2003, 'The day the music Industry died', The Sunday Times

This theme of 'making the numbers', rather than developing artist careers, is a common complaint and, to some, it is indicative of an incompatibility with creativity. It is articulated by Virgin records co-founder Simon Draper: '*I don't think being a public company with its excessive budgeting and reporting suits a record company at all…The finance people are too frightened to wait to get their money back*'.[8] Others like Sanctuary Group's Andy Taylor blame:' *the conglomeratisation of the sector for squeezing much of the creative life from the business*'[9]

Major record companies are obsessed with short-term gains, signing acts that can guarantee success (even if only of limited financial success) to shore up their (or more commonly their parent company's) share price. Their share price is under constant review and attack by both the stock market analysts and the financial press.

Purpose

The report will examine whether the structural problems of the music business have less to do with the antiquated distribution model that has survived the past 50 years much of which are seemingly threatened by the advent of the Internet. It will argue that these problems have more to do with the majors' obsession with boosting and maintaining their share price. This leads to a focus on making short term decisions and maintaining market share rather than planning for long term investments and signing creative talent on a long-term view. This has an impact on the industry as a whole and certainly on the independent sector.

This "short-termism" results in a set of short term creative decisions that eventually leads the company into increasingly short term signings and eventually abandoning long-term signings altogether. To explain the consequences of this phenomenon, the report includes an explanation of the 'creative bankruptcy spiral'

Historically the "major" labels have had to look to the independent companies to deliver the kind of successful artists short-term creative policies overlook - ironically on much less profitable terms and with less overall control and ownership. This resulted in the "major's" buying the independents,[10] (e.g. EMI /Mute or Island/ A&M / Motown and Universal), to acquire the kind of

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[8] Sandall, Robert, 2003, 'The day the music Industry died', The Sunday Times

[9] Cope, Nigel, 2002, 'Record -breaking run at the rest home for pop music has-beens'. The Independent, December 2nd Page 19.

[10] Sandall, Robert, 2003, 'The day the music Industry died', The Sunday Times: " There are now just five giant music groups, the biggest of which Universal had nearly a quarter of the world market in Cds last year and nearly a third in the U.S. The larger

critical mass in increased turnover and market share, that they need to nurture and sustain their share price. This leads them to the type of merger and acquisition frenzy that arguably causes more long-term problems - with the alienation of artists dropped from the label as well as the need to shed costs and staff. After such mergers, the remaining employees usually adopt the same kind of short-term mindset just to retain their jobs.

The report will argue that the demands of maintaining a company's share price are incompatible with the long tem need to sign and develop successful creative talent. It will argue that for genuine long-term success, its owners, to ensure their interests are identical should manage a music company. The majors need to step back from the abyss they have created and see there are alternatives to the existing approach.

Scope -

Aside from a review of the five major corporations and their relationship with the stock market the scope of the report will cover the treatment of the music conglomerates within the financial press and examine what lessons can be learnt. Do the Stock exchange and /or Wall Street understand the music industry?

The report will look at the five "major" companies and examine the individual differences and their responses to the industry's problems. Sony is arguably the weakest of the Big Five record labels, yet its parent company is the strongest of the five parent companies. EMI is the most creative of the Big Five and it certainly has the best A&R reputation amongst UK majors but its share price is the most vulnerable. The report will examine the corporate need to be part of a multi-media conglomerate. What are the limitations of that strategy?

NB. Obtaining accurate and reliable financial statement from each of the five majors has been very difficult. The results for several of them are not always broken down into meaningful figures for their separate divisions. The report will therefore rely on financial data supplied to and reported by the financial and music business media

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independents have been progressively absorbed"

SECTION 3

Analysis and Discussion

Methodology - Much of what is at issue within this report deals with perceptions of the music industry. Many of the findings and conclusions are therefore based on secondary research such as financial and music industry press..

I should add a note of caution that the music business press tends to take a less critical view of the music industry than the financial press, perhaps not wishing to bite the hand that feeds them. Equally, there is an inevitable reluctance amongst senior staff within the major corporations to discuss many of the issues raised here. That is the only reason why primary research was not carried out - after all it is the employees within these companies that have the greatest awareness of the issues raised in this report

Part 1 -The History of the modern Music Industry

Introduction -The modern music industry has evolved over three quite distinct stages, each one characterised by different technologies

Phase I -"Prior to the gramophone"- "industry dominated by music publishing houses"

Phase II- "With the rise of recording industry (and subsequently broadcasting)" - "Publishers were replaced by the record companies"

Phase III- Convergence- "the industry has involved entertainment groups that bring together a broad range of content distribution and repackaging activities"[11]

During **Phase II**, with the rise of the recording industry there were the original "players' - RCA, Columbia, MCA in US and EMI and Decca in UK. However the independents (Atlantic, Electra, Chess, Motown and Stax) took over the market in the USA in the 1950's and early 1960's,[12] but were all eventually absorbed by their competitors, leading to the creation of the modern 'majors' - WEA, Polygram.

Phase III is marked not just by convergence, but by the assimilation of the latest generation of independent music companies, including Chrysalis, A&M, Island and Virgin, all of whom were bought out in the late 1980's and early 1990s. This created the basis of the modern music

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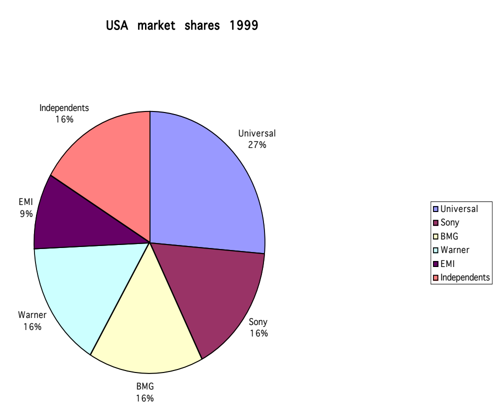
[11] **Anonymous. 2001** 'Shape of the market'. www.ketupa.net/music2.htm

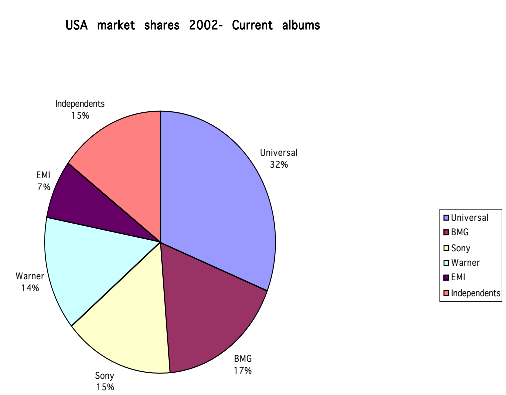
[12] 1955 -1959, 4 major labels in the US lost 34% of market share (down from 78%). The Independents went from 21.6% to 66.3% in a market that tripled in size Anonymous, 2001, 'Music CD Industry - The History'. www.soc.duke.edu/-s142tmo1/main.html

conglomerates, EMI/ Virgin and Universal /Polygram. Ironically this phase also coincided with the sudden decline of Warner Music group.[13] It is worth noting that with the exception of EMI all of the other major companies - BMG Music, Sony Music, Warner Music and Universal Music are now part of larger entertainment conglomerates.

The current Music Industry Structure:

The graphics[14] below show 2 quite different situations. Both indicate how the majors dominate the US album market - in 1999 the five largest record companies controlled 84% of the 755 million albums sold in the US. The overall US album market shares for 2002 are in fact very similar to the those shown in the first graphic with Universal climbing to 29% at the expense of EMI and BMG who each drop 1%. However the second chart - the 2002 USA **'current albums'** market shares - provides an insight into the real state of the majors as this chart only counts 'new albums' rather than back catalogue.[15] The 2nd chart shows how companies like Warner, Sony and EMI have all seen a dramatic decline in favour of Universal (and to a lesser extent BMG). As we will see later on the decline in market share for two of these major record labels is unsurprising given the turmoil their parent companies' shares have experienced on the stock markets. What is noticeable is how Universal - especially given the problem afflicting its parent company- has actually improved its market leader position in every category including widening the gap in "new " releases.





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[13] This is explained in detail in Stan Coryn's book- 'Exploding ' (The Highs, Hits, Hype, Heroes and Hustlers of the Warner Music Group), Rolling Stone Press/Harper Collins Entertainment 2002

[14] These are compiled from statistics at http://www.top40-charts.com/news.php?nid=4355

[15] Because the 'current album' chart shows only new releases and product from new artists instead of the consolidated chart which includes back catalogue. As such the 'current album' chart is better indicator of a company's success in A&R terms

The majors dominate the market -'As with the automobile industry, the "majors" have leveraged what Alfred Chandler characterised as "scale and scope in dealing with recurrent outbreak of competition from independent record labels"'. In addition they have had better financial systems and in particular "better access to capital, licensing and distribution arrangements"[16]

The 'majors' even with a perceived lesser ability to identify and develop new talent have been able to overcome the threats of the independents in the era of 'convergence'. Each time a new wave of independents appeared, they were co-opted through distribution deals and then eventually bought out. Indeed "When majors couldn't buy their smaller competitors, they've tended to simply buy the performers"[17]

Part 2 - An Industry in Decline

With an annual global $48 billion turnover, it is tempting to suggest that the music industry is not only not in decline but actually in good health. This is argued by many within the industry and the general opinion outside of the 'majors' appears to be that: "*There is nothing wrong with the British music industry. It is the record industry that is in trouble*"[18]

Sanctuary Group's CEO Andy Taylor clarifies the point in an interview with the Independent's Caral Milmos:' *that the music industry is one thing and the market for recorded music is another*.'…'*Sales of recorded music only account for about a third of the whole market, which also includes income from tours and merchandising as well as the use of music in commercials and in films*'.[19]

Reading comments like this it is easy to agree with comments like the following from the Independent's Nigel Cope; '*It makes you wonder whether the music industry is in the parlous state newspaper headlines would have us believe*'[20]

The Impact of the Internet - Perhaps the most commonly voiced argument for the 'decline in the music industry' is the impact of the Internet on sales of pre-recorded music. EMI Records have

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[16] Anonymous, 2001, 'Music CD Industry - The History'. www.soc.duke.edu/-s142tmo1/main.html

[17] ibid.

[18] **Milmo, Caral**, 2003, 'Sales falling, tours cancelled. So why is our music industry in such dire straits' The Independent February 20th.

[19] **Cope, Nigel, 2002,** 'Record -breaking run at the rest home for pop music has-beens'. The Independent, December 2nd Page 19

[20] Ibid.

used this as a familiar excuse for their disappointing results.[21]. Sanctuary's Taylor however: '*denies piracy is a serious problem and says that the music majors are using it to hide a more structural issue, lack of decent material by artists with long-term futures*'[22]

In fact according the Independent's Caral Milmos: '*Many believe the industry is exaggerating the effects of piracy to wring concessions from the authorities and deflect attention from its inability to compete*'.[23]

Milmos also cites: '*Research in America shows that those who take advantage of Internet piracy also buy music legitimately. A study by Forrester Research shows that about 85% of CD's are sold to people who download tracks up to eight times a month*'[24]

Is the current decline in record sales any worse than during the 1920s, when the then burgeoning radio industry was blamed for the dramatic slump in sales of records or during the 1980's when 'home-taping' was blamed for similar substantial falls in record sales?

One possible explanation is that the music industry goes through regular cycles of sales increases and decreases, which are accompanied either by the exhaustion of one or the introduction of another new technology. [25]

One commentator Michael Wolfe has another even more critical view of the current 'crisis': "*The music business is about selling technologies as much as music*" and: "*The CD theory hold that the music business actually died about twenty years ago. It was revived without anyone actually knowing it had actually died because compact-disc technology came along and everybody had to replace what they'd bought for the twenty years prior to the advent of the CD*'[26]

Equally with the success of the new DVD format[27] it is clear there are new technologies available.

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[21] Ibid.-" EMI reported a tale of woe the other week with lower profits, missed revenue targets and a primal scream about the problems of music piracy

[22] ibid.

[23] Ibid.

[24] ibid.

[25] Anonymous. 2001 'Music CD Industry - The History'.www.soc.duke.edu/-s142tmo1/main.html

'There was a 122.65 increase in consumer spending per average person on recorded music in America from 1984 to 1994. This is a greater change than any other types of media including cable, movies and theatres, magazines, home videos and newspapers."…"The reasons for this change are linked to the technology structure so prevalent in the music industry'

[26] Wolff, Michael. 2002 'Facing The Music'

[27] Beard, Matthew 2003, 'DVD sales double in leisure time revolution'. The Independent, 9th January, page 7

'Sales of DVD players and discs have more than doubled in the past year'…"Since it was launched in 1997, the DVD has been bought by one-in four consumers, making it the fastest selling electrical entertainment product in retail history'

Part 3 - The Problems with independents

Independent labels strategies

Perhaps the most successful of the few remaining independent record labels, Beggars Banquet's owner Martin Mills has some very clear ideas on why they are still around:

'I think, for any label to be successful they have to reinvent themselves. The independent labels who have been great but have not survived are the ones, which have not reinvented themselves.'[28]

Mills argues that:' *to be a successful label you had to catch successive waves, although you couldn't catch every one. But it was clear that the way to compete with the majors was not …head on, but to find the niche and take things beyond that niche. I think over the years our success has been the ability to catch those waves and also having a stable of labels with a lot of different identities, all of which are compatible. Each bit adds up to a whole.'*[29]

Clearly this ability to re-invent oneself is not one available to all independent record labels and it is tempting to argue that when an 'indie' no longer can 'catch the waves' as clearly happened with Island and A&M they usually end up being sold by their owners. It may be worth examining what took place within A&M and Island immediately before they were sold. Was it the cost of being in competition with the majors or other external financing problems that hastened their demise.

Mills argues that their strategy is not to be a '*big business*' or to "*aim to make huge profits*'. In fact it is: '*to put out great music. And we'll continue to grow as our artists do.*'[30]

Alongside Atlantic, Chess was probably the most successful independent of the post war era and its success like several others was '*giving the public music that they could not get from the larger, established "major" record companies*'.[31]

"*The Chess brothers understood the popular preferences of their predominantly African-American audiences, but also saw the marketability of blues music to a broader audience*'.[32]

Independents failure - typically this appears to happen when the owner is no longer involved and the best examples are Creation Records and Chess. Both owners McGee (post Oasis) and

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[28] James ,Martin. 2001 .'Interview with Martin Mills, founder of Beggars Banquet' http://www.beggars.com/banquet/index.htm

[29] ibid.

[30] Ibid.

[31] Anonymous. 'Story Of Chess' http://www.bsnpubs.com/chess/chesscheck.html

Leonard Chess (busy buying radio stations) became distracted from their main task of running the labels. Inevitably this led to problems:

"The late '60s were banner years for Chess, which makes the decline and fall of Chess Records hard to understand'…'In 1969, Leonard and Phil Chess sold Chess to General Recorded Tape (GRT) for 6 1/2 million dollars plus 20 thousand shares in GRT stock. In October 1969, the company suffered a devastating blow when Leonard Chess died. Quality output declined, and by the summer of 1972, the Chess Chicago offices were almost empty, the Distribution Company and pressing plants had been closed"[33]

Even Motown Records might be considered a relative failure given its creative decline since being purchased by MCA (now part of Universal) and this is borne out by the owner, Berry Gordy's reasons for selling it**:**

"*In June 1988, Berry Gordy sold Motown Records to a partnership between MCA and Boston Ventures, with Gordy retaining the ownership of the Jobete Publishing catalogue. Berry Gordy was always the consummate businessman. As good as he was as a judge of talent and hit songs, he was most of all an entrepreneur who transformed a $800 loan into the largest black-owned business in United States history*" [34]

Funding and Finance issues for Independents -

a) Music Industry seen as too risky - It is when accessing private external financing that many SME's find the music business is thought of as too risky. Even established firms find that external funding comes with the kind of strings attached that many find off putting.[35]

b) Investors call the shots - Ministry Of Sound / Venture Capitalist 3i. Even a successful independent like Ministry of Sound, having raised a staggering £24 million from venture capitalist 3i, found that their investors would soon want input on how their investment was spent.[36] It is little wonder that Ministry of Sound, 2 years after their much vaunted expansion and

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[32] Anonymous. 'The history Of Chess Records'http://www.history-of-rock.com/chess_records.htm

[33] Anonymous. 'The history Of Chess Records'http://www.history-of-rock.com/chess_records.htm

[34] Edwards, David and Callahan, Mike. 1999. 'The Motown Story ' June 11th
http://www.bsnpubs.com/gordystory.html

[35] Anonymous'. 2002. 'Access to Finance Executive Summary'
www.bpi.co.uk/news/display/News.asp?id=189\

[36] "*Rodol dismisses any suggestions that 3i, the venture capital company, which holds a minority stake in the group, demanded that Palumbo be sidelined.*'

signing spree, suddenly had to cut back drastically. This included closing Relentless (by any standards the most successful of their satellite labels) in March 2003, because it was haemorrhaging money. Ministry of Sound's attempts to establish overseas subsidiaries were brought to a sudden halt and have been replaced with a more traditional network of overseas licensing deals. Music Week's Editor Martin Talbot commented as recently as March 8th 2003 that:

"*Artist development will remain a priority but through smaller, cheaper deals, growth which is more organic and more sustainable. That should perhaps be a mantra for the entire business.*"[37]

c) **External Finance brings new pressures**- Beggars Banquet Owner Martin Mill's partner Andy Heath apparently said at the same seminar on 'Access to Finance' that: '*There is a dichotomy of interests when you seek external finance. A music entrepreneur may not want the controls that come with external funding e.g. not being able to make decisions without consulting the investor*' [38]

In this case Andy took the decision to sell his publishing company outright rather than be subject to external constraints"

d)**The decline of Independents can be as fast as their rise** - Music Week's Martin Talbot highlights the dilemma for many independent music companies that their decline can often be a meteoric as their rise. [39] The demise of Chess Records was certainly sudden, but apparently it was a result of several years of neglect by the main owner Leonard Chess[40].

e) Majors adopt the Independents' philosophy. What happens when the majors adopt the business practices of the independents? EMI has attempted to become more "Indie" friendly, whilst acquiring one of the most successful independents - Mute, and this showed that it was trying to formulate a new strategy. Sony has also tried a similar approach with its Hub network that brought the Creation and Nude labels into their international network, leading to the creation of SINE.

Talbot, Martin, 2003, 'Rodol steps up as MoS looks to brand' Music Week, page 1. March 8th

[37] Talbot, Martin, 2003, 'Rodol steps up as MoS looks to brand' Music Week, page 1. March 8th

[38] Anonymous'. 2002. 'Access to Finance Executive Summary'
www.bpi.co.uk/news/display/News.asp?id=189\

[39] Talbot, Martin, 2003. 'Lessons to be learned for all'. Music Week, March 8th, Page 3

[40] Anonymous.' The history Of Chess Records'http://www.history-of-rock.com/chess_records.htm

Corporations like Warner, Sony and BMG have historically funded independent labels in order to secure the international rights on their repertoire - hence deals like Telstar (Warner), Creation (Sony) and Jive (BMG)

Part 4 -Majors v Indies - The structural problem for the music industry

The Paradox - Independent labels like Chess always kept a tight rein on costs /advances. It was this prudence, which gave them their biggest advantage over the majors. Independents are far more cautious about overspending than one would expect from a major. Sanctuary is equally cautious: '*The Sanctuary business model is to keep investment low in new acts to minimise the risk. We limit the exposure to £50,000. That doesn't sound much but you can often sign a new act for £5,000- £10,000 and record an album for £10,000.*'[41]

Equally Zomba before its sale to BMG was famed for its '*tight control on costs.*' [42] However the 'majors', even within the current more cost conscious climate, are still expected to pay more than an independent label by way of advances - thus exposing them to greater risks, if the artist's career does not succeed.

Majors have to pay more because they expect far more commitment from their signed artists, including longer-term deals and usually end up paying higher royalties and more expensive recordings. Ironically this is what makes the financial value of the major labels appear so weak.[43]

Is it the majors that make the music industry look like a bad investment? Even whilst overpaying for new talent they are unable to make more than 5% of their new signings successful.[44] The majors overspend on marketing and promotion costs to try to recoup, or maybe simply to justify their original outlay. But this does not compare favourably with the more modest outlay of the successful independent labels, with smaller rosters and a more cautious approach to marketing and promotion spending.

More recently, majors such as EMI look to 'indies' e.g. Mute to acquire globally successful artists like Moby and Depeche Mode. They are also trying to develop stronger links with the independent label sector.

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41 Cope, Nigel, 2002, 'Record -breaking run at the rest home for pop music has-beens'. The Independent, December 2nd Page 19.

42 Anonymous. 2002. 'Strong margins produce record-breaking deal'. Music week June 22nd

43 Harold Vogel states that this "excessive royalty bidding' started in the 1970's and is an "important reason for the decline in record-industry profitability' Vogel, Harold L , 2001, 'Entertainment Industry Economics', Cambridge University Press, page 162

44 Gundersen, Edna. 2002 "Rights issue rocks the music world" USA Today, September 16th

The Majors see the independents are able develop artists better than they can. The lower financial exposure amongst Independents creates more confidence and a willingness to stick with artists on a long-term basis.

It seems the majors see market share as a more useful measurement of success than profitability - their obsession with competition rather than profit also fuels the inflated price and ephemeral value of new talent. A&R is no longer a breeding ground for spotting, signing and developing but rather a battle field between a small number of labels and their owned "imprints" for the "Next big thing". UK music journalist, broadcaster and A&R guru Steve Lamacq commented recently that:' *If two or three labels get involved in a bidding war for a group, the band's price can rocket within a matter of weeks*.'[45] This means that the majors ignore a large proportion of the available talent pool - leaving the Independents and other industry sectors such as music publishers and artist managers as the only viable A& R outlets.

Independents like Beggars Banquet, Telstar and Warp develop a 'track record' for signing and developing new talent (such labels then become the labels of choice for ambitious new acts). The majors then have to establish licensing arrangements with these same independents to boost their market share and their turnover.

Certain real benefits arise from such licensing deals between the majors and the independents because they contain less risk and enable the major to plan its resources, especially on marketing, that much better. Yet such deals are also usually far less profitable than had the same acts been signed directly and developed by their own A&R team. In particular it is unlikely the major will own the material outright.

In a climate of "short termism", amidst the corporate obsession with market share and share prices, it is less important to actually own material on a long tem basis and/or on a meaningfully profitable basis. It is all about acquiring "hit" material that "looks good" to the media and the stock market analysts, constantly vetting their accounts. These same analysts usually working for one of a select number of merchant banks have an unbelievable amount of power over the direction and strategy of these corporations. Even so the analysts are not always won over by this approach. Sarah Simon from Morgan Stanley warned that "*One-off successes from greatest hits*

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[45] www.bbc.co.uk/radio1/onemusicdata/lamacqlive/190503.shtml.

albums are temporary fixes to a more telling problem: sourcing and promoting new talent and exploiting album sales and follow-on publishing opportunities"[46]

Many of the more successful independents, apart from Beggars Banquet, appear to have no greater long-term goal than to build the artist roster to a point where it becomes a take -over target for one of the majors. This was certainly true of PWL, one UK independent, which went into decline after being purchased by Warner Music. Creation was yet another company that suffered under corporate ownership by Sony. In the case of these two independents, the major label acquiring the independent had little comprehension of what made the independent successful and certainly did not share the unique aspects of the independent that created their successful roster

There must be doubts within BMG over how they can best absorb Jive / Zomba, finally acquired by BMG at the end of 2002, especially as this was one of the most successful independent music companies of the past 40 years. This was the classic example of an independent company selling out at the most advantageous point for its owners - usually at the point at which the independent had "peaked' in terms of its success.[47]

The major, BMG had wanted to acquire the independent, Zomba, because of Jive's turnover and profits and to boost BMG's global market share. The independent - Jive had originally wanted the security of the major's financing, its global licensing and access to important commercial outlets such as Club and Tv advertised compilation releases, both of which are dominated globally by the majors. Yet Jive through its parent company also owned one of the most important components within the UK independent sector namely Pinnacle, the independent distributor. Now that Pinnacle is ultimately owned and controlled by a major label, this must surely bring the whole validity of the independent chart in the UK into question. The term "independent", as far as record distribution is concerned, is now meaningless. Ironically BMG did not greet the acquisition of Jive with any satisfaction given how it was forced to pay a vastly inflated price. It seems this one final deal hastened the departure of Bertelsmann's CEO Thomas Middlehof.[48]

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[46] **Cassy, John**. 2002. "Stuck in the EMI Groove", <u>The Guardian</u>, September 6th

[47] "Sources suggested that the deal involves a 12 times multiple on recorded music profits and a 15 times multiple on net publisher's share, although there may also be a further formula relating to turnover"

"Zomba already boasts one of the best operating profit margins in the business, reliably estimated in excess of 20%. To put this in perspective, EMI's operating profit margin has historically been around 12%, while the Ebitda margins for the year to December 2001 of Warner and Universal were 12.5% and 17.7% respectively"

Anonymous. 2002**.** 'Strong margins produce record-breaking deal'. <u>Music week</u> June 22nd

[48] Anonymous, 2002, 'Strong margins produce record-breaking deal', <u>Music Week</u> ,June 22nd

Part 5 -Corporations - Definitions

There are significant differences between the majors and the independents in the ways they structure their companies' shareholdings.

i) **Typical independents** - are usually owned by a small number of people - say between 1 and 3 individuals - and these same people are actively involved in the management of the company and are certainly involved in any significant decisions regarding signing new talent

ii) **Typical majors** - the 5 major music based conglomerates are all corporations and all 5 usually through their parent companies are quoted (in Bertelsmann's case just 25% of their shares) on the stock markets

The Definition of Corporation - "Principles of Corporate Finance" defines a corporation as an entity that is "owned by shareholders who hold shares in the business"[49]. It distinguishes between corporations where shares are closely held (such as Bertelsmann) and those where shares are widely traded, the so-called "public companies". This definition continues to describe how the shareholders do not manage the corporation. They elect a board of directors to represent their interests. It is this separation, of ownership from management, that gives corporations their permanence**.** It may also be a root cause of some of the malaise affecting the entertainment - arts conglomerates.

Sanctuary Records - this is a unique company, a hybrid between the typical independent record label and a publicly quoted conglomerate. Its portfolio covers almost every type of music business activity - from record labels, music publishing, studios, artist management, concert agency and book publishing. The usual distinctions applied to a typical major and a typical independent record label do not apply to Sanctuary. The company is publicly owned, but its management is still in the hands of the original business partners and shareholders prior to the 'float'. This continuity of management provides Sanctuary with the kind of single-minded focus one usually associates with an independent.

Part 6- The Majors -Vertical Integration and Horizontal Integration-

The Obsession with size, market share, expansion and growth

Introduction

Vertical Integration - the main reason for vertical integration would be to increase a corporation's market share but other reasons would include creating *'a tightly secured network by purchasing forwards and backwards in the supply chain, buying new labels, manufacturing companies, and distributing companies'*[50]

The established distribution systems become highly elaborate and expensive creating a barrier to entry within the industry, which prevent small firms from entering and competing. This is what gives the 'majors' their edge over the independents.

Horizontal Integration As if owning more than 80% of the industry were not enough, these 'majors' are also competing against each other. They must each find an *'unconquered niche within the music industry and try to secure it for themselves'*.[51]

They might do this by specialising in one genre of music such as country music or by conquering a new market in a new country. By buying all the labels in a certain genre or by establishing another distribution channel in a rising market, these huge companies can maintain a competitive advantage over their competitors.'[52]

Quoting economists, Scherer and Ross, Payam Esghraghian states that although *'Vertical integration, in the static sense, describes the extent to which firms cover the entire spectrum of production and distribution stages. The motives for vertical integration include "reducing the costs of production and giving the producer enhanced control over their economic environment"..."The two kinds of vertical integration are upstream and downstream integration'* (Scherer and Ross "Industrial Market Structures and Economic Performance", 1990, page 93)[53]

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49 Brealey Richard and Myers Stewart C, 'Principles of Corporate Finance'

50 - http://www.soc.duke.edu/~s142tm01/compete2.html

51 - http://www.soc.duke.edu/~s142tm01/compete2.html

52 http://www.soc.duke.edu/~s142tm01/compete2.html

53 Esghraghian, Payam. 2001. 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms.' September 3rd Page 13

www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf

He defines the rationale of vertical integration for the modern, media-based, conglomerate: '*In the context of the evolving media content and distribution industries, upstream integration involves a content distribution firm, (TV network, cable or pure Internet firm), buying a content producer, whereas* *downstream integration* *is analogous to primarily content producing firms acquiring distribution channels for transmitting their in-house generated programming*.'[54]

Describing the strategies involved he argues the key issues are '*owning the production and multiple distribution means of transmitting content*'[55]and that the '*The main corporate strategies for combining divergent media assets over the past ten to fifteen years have been mergers and acquisitions (M&As)*'.[56] This M&A activity is what has changed the media conglomerates over the past 3 - 5 years and is the single biggest reason for the pressure to deliver constant growth in all of their divisions.

Part 7 - The Majors and the stock market - playing with Fire

The battle for market share and position has led the major music companies into conflict with the stock market. This part of the report will attempt to analyse how the stock market fuelled ambitions to expand the size and value of the 5 music conglomerates. Three of the 'majors', Warner, EMI and Universal, have fallen foul of the market and subsequently have been forced into drastic restructuring. One of the others, Bertelsmann, although currently 75% privately owned, has been forced to recognise the pitfalls of using the stock market to raise the capital to fund mergers and acquisitions.

In 2001 the global market share of the 5 major record labels looked like this:[57]

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[54] **Esghraghian, Payam. 2001.** 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms.' September 3rd. Page 14

www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf

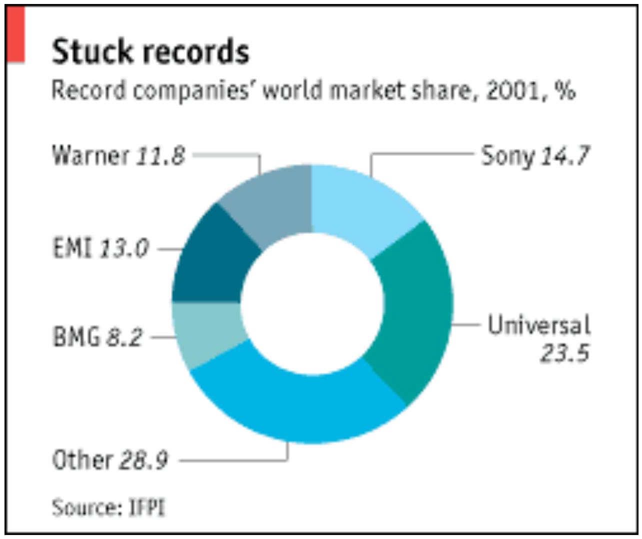
[55] **Esghraghian, Payam. 2001.** 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms.' September 3rd . Page 14

www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf

[56] **Esghraghian, Payam. 2001.** 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms.' September 3rd Page 15

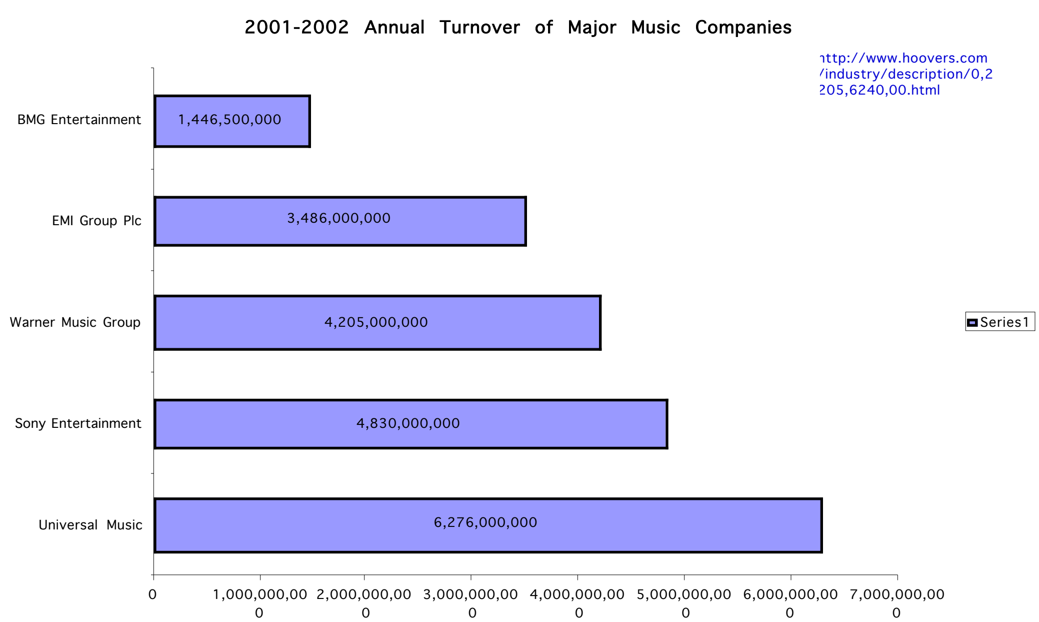
www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf

[57] http://www.economist.co.uk/business/displayStory.cfm?story_id=1611255)



The comparative turnover figures (expressed in dollar terms in the graph below) highlight the vast differences in scale and volume between sector / market leader Universal and 5th placed BMG. It also underlines why firms such as BMG and EMI were so keen throughout the period 2000 to the present day to merge with one of the other remaining conglomerates.

NB The figures shown below however include all the majors combined music activities such as music and record production, music publishing. Record clubs and distribution.



i) Warner Music Group

Described as: ' *A Frankenstein business, since the film, music and entertainment portfolio of Warner Bros. made a strange marriage with Time Inc magazines in 1989*.' [58], the media conglomerate Time Warner (parent of Warner Music Group) merged with AOL on January 10th 2000 to form: '*A Strategic merger of equals and to create the world's first fully integrated media and communications company for the Internet Century*' '[59]

In doing so Time Warner had undoubtedly compromised its status as a leading media brand and this has been made even worse for the company by the dramatic decline in its post-merger share price, amidst accusations of Insider trading.[60]. Most recently these accusations turned into a class action lawsuit against the leading executives. More worryingly it has been accompanied by a failure to reap the benefits of the planned so-called synergies between the 'old' and 'new' media arms of the merged company.[61]

Accused of using '*tricks, contrivances and bogus transactions*'[62] to inflate the value of AOL stock while liquidating their shares '*in a selling frenzy to enrich themselves to the tune of $936 million*'[63], in the subsequent months after the merger, the company executives sold off 10.7 million shares from personal portfolios. During that same period they used corporate money to prop up the stock's value so they could benefit personally and shield themselves from a stock collapse [64]

'The merger has been called: '*a terrible deal*' by Dow Jones, '*the worst deal of the century*' by Time and '*one of the great train wrecks in corporate history*' by Fortune. The New York Times said that Case: '*pulled one of the sweetest deals in business history…by managing to acquire Time Warner with AOL's inflated stock*'. Richard Parson's,

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[58] **Bell Emily. 2002.** 'Divided They Fall.' The Guardian Media, July 29th, page 8

[59] Esghraghian Payam, 2001. 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms.' September 3rd.

www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf

[60] Caney, Derek, 2003. 'AOL-TW Execs Accused of Insider trading'. Reuters April 14th
www.truthabout.org/docs_o3/priniter_041803H.shtml

[61] Esghraghian Payam, 2001. 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms'., September 3rd.

www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf

[62] www.ucop.edu/news/archives/2003/apr14art1.htm

[63] Ibid.

[64] www.ucop.edu/news/archives/2003/apr14art1.htm

AOLTW's current CEO, recently called the merger 'silly' and a 'mistake' based on 'overly ambitious' forecasts that were not 'real'. Due to overvalued assets, the merged company took a $100 billion loss in 2002, the largest in history' [65]

Some months before the merger with AOL, then Time Warner CEO Richard Parsons welcomed news of another pending merger, this time with EMI Music (eventually blocked by the EU), which he described as: '*a match made in heaven. It's going to create value not only for EMI shareholders, but for Time Warner shareholders and we would argue for artists that will be part of our company going forward, and for the employees".*[66]

Clearly Parsons did not anticipate the affect the AOL merger might have on the assets of Time Warner let alone the Warner Music Group, but his statement clearly demonstrates where his priorities and loyalties were - shareholder first, the company's artists second and employees third. It is certainly difficult to see what benefits that merger would have brought to Warner Music group's recording artists. As we will see in the next chapter, the most likely outcome would have been that the majority of their artists would have been dropped and much of the staff laid off. The AOL Time Warner merger has certainly not improved Warner Music's fortunes within the global industry (which have dropped from 20% in 1998 to 11.8% in 2001)[67]. It is readily apparent WMG will be sold by AOLTW, to raise much needed capital for a beleaguered parent company, that announced $25.8 billion of debt shortly after posting the largest loss in corporate history in 2002 (nearly $100 billion).[68] It is remarkable how, the dramatic decline in AOL Time Warner's stock price, from a peak of close to $80 to a low of $8.70 by February 2002, echoes its 1980s predecessor, Warner Communications Inc.'s, fall from grace. In the early 1980's the WCI share price plummeted from $52 to $7, all because of a set of disappointing results from

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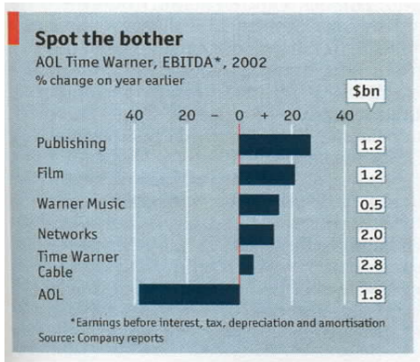
[65] www.ucop.edu/news/archives/2003/apr14art1.htm

[66] Anonymous, 2000, Time Warner- Emi to merge." January 24th
www.pbs.org /newshour/ bb / media/jan-june00/time emi 1-24.html

[67] http://www.economist.co.uk/business/displayStory.cfm?story_id=1611255)

[68] www.washingtonpost.com/wp-dyn/articles/A49857-2002Jun26.html)

its Atari division.[69] The difference then however was that the Warner Music Group was the group's main 'cashcow'[70]



2 years after the '*the worst deal of the century*' the relative unimportance of the Warner Music division to the newly merged conglomerate is all too apparent. In the above graphic the total AOL Time Warner EBITDA for 2002 is $9.5 billion, yet Warner Music only accounts for a modest $0.5 billion, representing a little over 5% of the combined profits of the merged company. Its little wonder therefore that Warner Music is now seen merely as an asset to be sold off or traded to reduce the debt accumulated during the Time Inc and then the AOL mergers.

ii) BMG

BMG Music is owned by Bertelsmann, ' *a privately held stock corporation and international media conglomerate with diversified holdings in television and radio, book publishing, magazines and newspapers, music companies, professional information and online book and music e-commerce assets*.'[71]

Payam Esghraghian identifies similarities between Bertelsmann and Vivendi Universal, '*with their international media presence and a localised content approach across 58*

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[69] Coryn, Stan, 'Exploding ' (The Highs, Hits, Hype, Heroes and Hustlers of the Warner Music Group), Rolling Stone Press/Harper Collins Entertainment 2002 Page 284

[70] Coryn, Stan, 'Exploding ' (The Highs, Hits, Hype, Heroes and Hustlers of the Warner Music Group), Rolling Stone Press/Harper Collins Entertainment 2002 Page 286

[71] Esghraghian, Payam, 2001, 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms.' September 3rd,www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf page 43

countries' [72]. He suggests that Bertelsmann's strategy over recent years was '*growing these assets through Internet commerce*' and ' *attempting to compete on the same level as its publicly traded global media rivals*'.

Bertelsmann has been plagued over recent months by rifts within the company, most of which appear to have been generated by the decision of former CEO Thomas Middelhof to focus the company's resources on an internet strategy, that on reflection was unwise. It appears that Middlehof even proposed a merger with AOL that was only impeded by AOL's inflated stock value [73]. Although this must seem rather fortunate, it should also be remembered that "*It was Thomas Middlehof who made the most money out of the Internet bubble*"[74]

Esghraghian also denies that Middelhof's '*recent growth strategies have been advantageous or predictable*', in particular the aborted merger with EMI Group Plc and the troubled "alliance' with Napster, despite implicit opposition from its own music division which supported the record industry's copyright infringement lawsuit against it.[75]

Esghraghian points out, perhaps the only major impediment in the way of Middelhof's ambition to compete with AOL Time Warner and Vivendi Universal was that Bertelsmann did not own: ' *the hardware that will carry convergent media services to consumers, leaving it with a competitive disadvantage. It lacked vertical integration with scaleable, broadband conduits*'.

These acquisitions in technological hardware to complement its content properties would require the kind of finance available only by publicly trading the company's shares. They would also require' *a unified market extension strategy that includes the approvals of Bertelsmann's private owners*"[76]

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[72] **Esghraghian, Payam, 2001,** 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms.' September 3rd,www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf page 46

[73] **Fox Justin**. 2002 'Thomas Middlehof wants respect' Fortune, June 10th pp 32 -38

[74] Ibid.

[75] **Esghraghian, Payam, 2001,** 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms.' September 3rd,www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf page 46

[76] **Esghraghian, Payam, 2001,** 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms.' September 3rd,www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf page 46

Middelhof clearly banked on securing the company's support for this strategy but the owners were unsure about the way the Internet bubble was heading and balked at his spending spree of close on $2 billion on Internet investments and start-up losses.[77]

Nevertheless Bertelsmann was the only media conglomerate to not be burdened by debt[78] (although this observation was made before the terms of the Zomba/ BMG sale changed that situation by adding around $1.8 billion in debt).

Compared to the other media conglomerates, Bertelsmann was profitable and it is clear the Mohn family did not want to sacrifice this just to achieve Middlehof's aims. Indeed Mohn is noted for his motto '*continuity through change*' but this continuity could only be guaranteed by '*keeping control of Bertelsmann firmly in his hands rather than ceding it to banks or stock market investors*' Equally important Bertelsmann had a reputation for supporting its companies even in hard times.

"*When Bertelsmann decided it liked a business, its staying power and willingness to keep investing were unmatchable*"[79]

Inevitably the Mohn family were able to see the pitfalls of Middlehof's plan to take the company public by 2005[80] and it appears his fate was sealed by the disastrous purchase of Zomba. What is clear however is that what has saved Bertelsmann from the ignominy suffered by both AOL Time Warner and Vivendi Universal is that its value and its assets are not publicly quoted or traded.[81] As such the temptation to purchase other companies using inflated share values as currency (which was clearly the case with AOLTW and VUE) was not open to them but equally the company's value has been maintained. We will see later this has important ramifications for the well being of its Music division and it is worth noting here that BMG has spent much of the past few months consciously

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[77] Nevertheless Middlehof came out of the Internet 'bubble' having netted Bertelsmann close to $7 billion.

[78] **Fox Justin**. 2002 'Thomas Middlehof wants respect' Fortune, June 10th pp 32 -38

[79] Ibid.

[80] **Cassy, John, 2003**. 'Bertelsmann battle over family's remote control' Guardian February 18th page 21

[81] "Mr Mohn and his wife knew that the company had to go public. But they favoured a more gradual transformation."

Karnitschnig Matthew, Boudette Neil E, 2002, 'Why Middelhof is Out -Even without Worries About Shares or Debt' The Wall Street Journal Europe, July 30th page 1 reinventing itself. Middlehof's replacement was able to announce a cost cutting programme as the means to reduce debt.[82]

iii) (Vivendi) Universal / Polygram -

This once staid utility firm, Vivendi entered the media industries through a massive M&A programme, which included a share-for-share merger in 2001 with Seagram/ Universal valued at $34 billion. Whilst '*Vivendi's core competencies were spread over multiple non-media activities', 'Seagram gained digital conduits, added financial strength and film market penetration for scale in competing with long-standing rivals Time Warner, Paramount and Twentieth Century Fox*' [83]

Vivendi's approach demonstrated that:' *M&As are the fastest means for entering a market* ' and: ' " *time to market" has proved critical in the media and telecommunications convergence environment*' [84]

However Vivendi's convergence strategy was*: 'Unlike News/ BskyB and AOL Time Warner yet similar to Disney and Viacom, Vivendi's "gatekeeper" power over its evolving digital content is primarily Internet based'*[85]. Clearly Vivendi's CEO Messier made the same calculations about the impact of the Internet as Bertelsmann's Thomas Middlehof - perhaps the main difference being how they raised funds and how their strategy was scrutinised by Wall Street and institutional investors. Unlike Bertelsmann however, Vivendi were able to use the stock market to raise funds.

'*Using highly priced shares as an acquisition currency, he paid £12.5 billion for control of Canal Plus, a pay-tv group, and spent £32.6 billion to acquire Seagram, owner of Universal*'[86]

Two factors brought down Vivendi and Messier's vision of a global media force - the first was the reluctance of investors to back his strategy amidst concerns*: ' over the*

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[82] "One of the first announcements (by Gunter Thielen, Middelhof's replacement) was a cost cutting programme to tackle the company's debts- boosted by $2 billion acquisition of Zomba' O'Donnell, John, 2002, 'Germany's media star falls to earth' The Sunday Times , Business Section , August 4th page

[83] Esghraghian, Payam, 2001, 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms.' September 3rd www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf Page 39

[84] Ibid. pages 30-40

[85] 'The great convergence gamble', www.Economist.com, 7 December 2001

[86] Anonymous, 2002, 'Messier's mess', The Economist, June 10th, pp 69 -71

French utility stalwart's entry into multiple 'speculative' businesses as well as the divestiture of its stable businesses'.[87] The second factor was a series of setbacks to Messier's Internet plans including the acceptance that as the Internet is free domain, customers could choose alternative portals to Vivazzi, (Vivendi's wireless portal). In addition the European Commission's decided to prevent "*content exclusivity by requiring availability of Universal's content to rivals "on fair terms"*'[88]. Despite their attempts to vertically integrate its distribution base with its content properties, without the guarantee of a significant consumer basis to its online portal, Vivendi were unable to follow through on Messier's strategy.[89]

Despite some astute deals, including forging relatively risk free joint ventures and alliances[90], the company became burdened by the dramatic fall in it share price (40%) as concerns about over -diversification and the size of the debt accumulated during Messier's acquisition spree triggered a liquidity crisis.[91]

(news.bbc.co.uk/.../images/ _1943323_vivendi2_gra300.gif)- Messier's departure in July 2002 was sudden but Vivendi Universal's problems did not stop there with questions being raised about the accuracy of the financial statements made available to Investors and in particular the questionable use of Ebitda that enabled the company to disguise the vulnerability in its cashflow.[92]

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[87] Esghraghian, Payam, 2001, 'Digital Convergence: comparative corporate strategies for consolidating content and distribution channels amongst multinational media and communication firms. 'September 3rd.www.jims.cam.ac.uk/library/infores/mba_dissertations/ EshraghianPayam.pdf

[88] Ibid.

[89] Ibid.

[90] ibid.

[91] . Milner, Mark, Wray Richard, 2002, 'Vivendi's shake-up kicks off a E12 bn asset sale', The Guardian Finance, September 26th.

[92] Anonymous, 2002, 'Messier's mess', The Economist, June 10th pp 69 -71

Ebitda is an inadequate measure because it does not take account of a firm's capital spending, nor does it indicate how much profit is turned into cash. In Vivendi's case Ebitda was used to enable the company to use minority shareholdings in other entities within its own accounts and thereby improve its debt/Ebitda ratio.

In fact according to the Economist,[93]Vivendi's 2001 annual accounts show this ratio as 3.8 rather than the very poor 5.1, it would have scored had the minority shareholdings not been included.[94]

'Vivendi and other big groups are enthusiastic users of Ebitda because it gives a flattering picture of performance'…' The company even bases its bonus schemes for top management on Ebitda. This explains why Mr Messier's total pay last year was an impressive £5.12 m, despite the fact that Vivendi announced France's biggest-ever corporate loss of £13.6 billion.'[95]

It was inevitable that when the new CEO, Fourtou, said: ' *the dream of transforming a french utility group into a global media empire was a "delusion"',*[96] that the company would start cutting its losses. He soon announced a program of disposals: *'Its target of raising more than E7 bn (£4.8 bn) in asset sales this year, which would reduce its debt to below E11 bn from a height of E37 bn.'*[97]

Chief amongst those disposals will almost certainly be the Universal Music Group either alone (as part of a deal with Apple reputed to be worth around $6 billion) [98]

Recently, oil billionaire, Marvin Davis made a $15 bn approach for both Vivendi Universal Entertainment and Vivendi Universal Music[99]. There is talk of the Vivendi Universal entertainment assets being merged with the cable assets of Liberty Media[100] to form a new more focused entertainment division that would be welcomed by those within the division itself.[101]

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[93] Ibid.

[94] A score of 5 or more is the mark of a bankrupt company - Anonymous, 2002, 'Messier's mess', The Economist, June 10th pp 69 - 71

[95] Anonymous, 2002, 'Messier's mess', The Economist, June 10th pp 69 -71

[96] Milner, Mark, 2003, 'Vivendi admits to deluded aims', The Guardian, April 3rd. page 22

[97] Ibid.

[98] Anonymous , 2003, 'Apple Eyes Universal music'- LA Times, April 11th www.washingtonost.com/wp-dyn/rticles/at280-2003April11/html

[99] Milner, Mark, 2003, 'Vivendi admits to deluded aims', The Guardian, April 3rd, page 22

[100] Cope, Nigel, 2002, 'Debt-laden Vivendi may spin off film and music division', The Independent, August 21st, page 17.

[101] Ibid.

iv) Sony Music Entertainment

It has been a comparatively quiet time for this company. It is hard to establish how concerned, Sony was by the its competitors' attempts at convergence between the 'old' and 'new' media companies in Europe and North America. Given its traditional background in technology and hardware it could be said that Sony does not need or is not in a position to invest in further vertical-integration. The company already covers a very wide spectrum of activities including Electronics and Communications, Film production & distribution, Cinemas, Merchandise, Insurance and Financing, Games & Interactive, Music and Television Production & Distribution. Perhaps Sony is intent on focusing on maintaining and consolidating their existing 'soft' assets. Most of these were acquired during an acquisition spree in the late 1980s that saw Sony purchase Columbia Records from CBS (1988) and Columbia pictures/ Tri-Star from Coca-Cola (1989)[102]

Bearing this in mind in recent times Sony has been absent from any significant M&A activity and its parent company's share price has reflected that stability. It might also be a result of what Keith Negus refers to as the shifting of interest away from music and film production.[103]However on the music side Sony appear to have missed the whole rise of 'hip hop' (even selling its stake in Def-Jam to Universal Music).[104] Whilst music is a minor part of the parent company's profits and revenues[105] it is clear Sony has opted recently to restructure most of its international operations resulting in a major shake up in their north american and european companies. The decline in global (from 18% to 14.2 %) and North American market share are clearly the main reasons for this overhaul, although the removal of its charismatic US president Tommy Motolla was seen as "the end of an era".[106] The changes appear to have been made as much in response to the state of the industry, highlighting the demise of music retailing, the consolidation of radio, CD-burning, downloading and unexciting artists. [107]The News that it was to shed around 1,000 jobs, around 10% of its workforce, as part of a strategic overhaul came as no great surprise to anyone, although it included some very senior established executives like European CEO Paul Burger.[108]

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[102] http://www.ketupa.net/sony.htm

[103] Negus, Keith 'Music Genres and Corporate Cultures', Routledge 1999 page 41

[104] Helmore, Edward, 2003 'Sony pulls the plug on its pop playboy', The Observer Media Section, January 12th

[105] Around 11% according to Keith Negus , 'Music Genres and Corporate Cultures' page 41

[106] Helmore, Edward, 2003 'Sony pulls the plug on its pop playboy', The Observer Media Section, January 12th

[107] Ibid.

[108] Scott, Ajax, 2003, 'Burger departs Sony in global restructure', Music Week, April 5th, Page 1

v) EMI Music -

EMI might well be the oldest Music company in Europe, tracing its origins back to 1898 and an early history closely aligned with both RCA's Victor and - independently of CBS and Columbia Pictures - the Columbia Record label.[109] The company's main business strategy after the 2nd world war was based around consumer and defence electronics and this was an integral part of EMI's business until the de-merger with Thorn in 1996. Since that de-merger EMI has had stormy time on the stock markets with its share price constantly devalued Most recently its fall has been cause for some alarm:

www.news.bbc.co.uk/.../1920000/images/ _1923118_emi_300graph.gif

EMI has grown its music business - both in music publishing and recorded music through a series of mergers and acquisitions that have not always been coherent.[110] M&A appears to have been EMI's only means of growing its business and once it had reached the limits of that strategy, it soon fell out of favour with the City. Its executives have been forced - more clearly than with any other publicly quoted music company - into a series of what can be best described as panic measures to pacify shareholders and stock market analysts. In each case these strategies have backfired on the senior executives of the company.

This is most clearly evidenced by the 'Mariah Carey ' fiasco, a wake up call to the company and signifying the moment when the rot had set in, leading to the removal of its CEO Ken Berry.

" *It was this brutal logic that led EMI into their disastrous signing of Mariah Carey*."- "*When your shareholders are clamouring for reassurance and big dividends buying an off-the-peg mega-celeb is a tempting gamble. It cost EMI £50m and lost the company CEO Ken Berry his job*.' [111]

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[109] : http://www.ketupa.net/emi2.htm

[110] Ibid.

[111] (Sandall, Robert, 2003, 'The day the music Industry died', The Sunday Times)

Despite some dramatic action on the part of the EMI Board, including the usual 'restructuring' plans, the stock market was not impressed and EMI's share price continued to tumble to the point, where: '*Equity analysts decided …that the part of the company selling Cds was worth, in effect, nothing*' [112]**.**

More recently the company announced a new deal with one of its existing, one might even say its only 'Mega-star', Robbie Williams, the value of which was reported as being between £25 million and £80 million. The Times' Adam Sherwin reported the deal's success hinged on Williams '*becoming a major success in the American market*' [113]. He stated that the deal was seen as '*crucial by the British music giant, which is showing signs of recovery after a collapse in its profits*'[114]

The Guardian's Caroline Sullivan added a suitable note of caution when she remarked that in an industry '*notorious for signing artists to enormous deals that embarrassingly fail to recoup their multi-million pound advances…EMI announced this week, it had signed Robbie Williams to a truly "groundbreaking" £80m contract*'[115]

The market's reaction to the Williams deal was less generous than expected by EMI's senior executives and the '*share price fell 1.5 pence*'. The situation was made even worse by the news that Williams had split from his long-term musical collaborator Guy Chambers'[116]

Unable to please the stock exchange even with this supposedly 'groundbreaking' deal, EMI by early 2003 had to reconcile itself with new realities of being a publicly quoted company. These realities were underlined out by the announcement that "*EMI's stock market value has dropped to just £730 million since the turn of the year representing a decline of 40 percent since December*" [117]. It has even been reported that EMI might be bought by private investors and indications are that such a buyout would be led by Alain Levy and would be funded by a number of "private equity groups'.[118]

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[112] Ibid.

[113] Sherwin, Adam, 2002. 'EMI stakes future on £50m Robbie Williams deal' The Times , October 3rd page 4 m

[114] Ibid.

[115] Sullivan, Caroline, 2002, 'Robbie's £80m deal puts EMI on new path' The Guardian, October 5th Page 7

[116] Ibid.

[117] Wachman, Richard, 2003. 'Music giant EMI 'faces buyout' ' The Observer Business Section March 16th, page 2

[118] Ibid.

It is clear EMI's senior executives have become exasperated by the City's inability to support the company's rebuilding programme. One article highlighted this: "*EMI is understood to be considering legal action against the stock-broking arm of one of France's biggest banks following the publication of a heavily critical research note.*"[119]

The same article cites stock market analysts reports that question: ' *the legitimacy of the music group's profits and the strength of its balance sheet, It strongly advised investors to sell EMI shares*'

EMI Executives have even been forced to defend their artists and creative signing policy: ' *Norah Jones wasn't a fluke. It's about the management focusing on artists who have long-term potential and backing them all the way*'[120]

Even after EMI's drastic restructuring during 2001 and 2002, which had sacrificed nearly 2,000 staff and 400 artists and apparently: '*swung the company back into profit*'[121], the advice it got from the city and the financial press was: '*it needs to do a deal. In a shrinking market, size matters and a merger with either Germany's BMG or AOL Time Warner would catapult the company to the top of the tree*'[122].

In the midst of this wholesale downgrading of EMI's value by the financial press, the company has still managed to acquire Mute Records, ' *One of the most influential British labels of all time*'[123] , and further consolidate it's reputation within the music industry as arguably the most creatively driven of all the major companies with its unique roster of creative but successful artists including Radiohead, Coldplay, Norah Jones, Blur, Kylie Minogue and Robbie Williams.

The incompatibility of such creatively driven music companies with the vagaries of the stock market and their constant need to placate shareholders is more evident with EMI than perhaps with any of the other major companies. Alone amongst the Big 5, EMI is a music only company and it might be argued the treatment meted out by the City and financial press is in fact an indictment of the music industry as a whole. It certainly highlights the City's complete lack of understanding of and belief in the record industry.

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[119] Cassy, John, 2003, 'EMI may sue over broker's note' The Guardian, January 25th

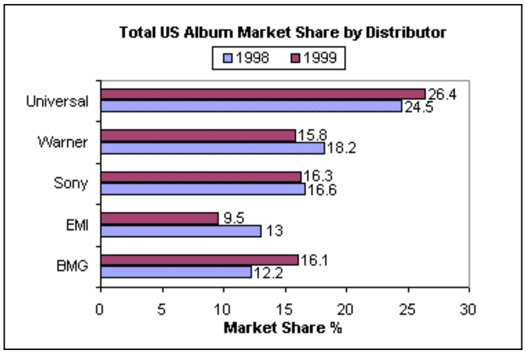
[120] Cassy, John, 2003, 'EMI may sue over broker's note' The Guardian, January 25th

[121] Ibid.

[122] Ibid.

[123] Talbot, Martin, 2002. 'EMI buys Mute in £42m deal' Music Week May 18th page 1

EMI in the US market place-The following graphic highlights EMI's sudden decline in the USA[124]



The City, it seems, judges EMI more by its historically weak USA market share, which admittedly declined from 13% to 9.5% between 1998 and 1999[125], than by its long-standing dominance of the global music publishing business and its very high market share in recorded music outside of North America.

Perhaps it is the case with some of the other majors, notably Sony, that suffered similar declines in market share during the same time period, it is the buffer of their non-music related divisions that shields them from the excesses of the market.

It is questionable whether EMI would have ever embarked on its series of disastrous 'big-money' signings had it not been so desperate to pacify the shareholders. One wonders whether EMI would have paid Mariah Carey (who was meant to provide the company with an immediate boost to its US market share) or Robbie Williams so much, had it not been so desperate to provide it shareholders with some 'short -term' good news.

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124 http://www.soc.duke.edu/~s142tm01/compete3.html

125 www.soc.edu/

Part 8 -The Pressures on Majors to maximise profits:

Whilst the actual affects of the stock market on the 5 music conglomerates can be clearly seen the resulting internal pressure produced by the market within the music divisions of these major companies may not be so evident. This pressure can be characterised as the pressure to maximise profits and can manifest itself in the following ways[126]:

i) Recouping merger and acquisition costs - places an immediate pressure on the company and its staff. As most of the M&A activity within the conglomerates over the recent past appears designed to improve their share price inevitably the main concern is recouping the M&A costs as soon as possible

ii) Focusing only on the most profitable ways of selling music - The conglomerates tend to concentrate only on the most popular types of music to sell to the largest record buying public. Niche or unproven markets are avoided

iii) Focusing on a smaller number of artists with the aim of selling more copies of a smaller selection of records. This is the most cost-effective and profitable means of distribution but it also leads to the cultivation of 'Mega-stars' and 'Mega-hits'.[127] As Robert Sandall states: '*The hard sums of running a conglomerate like the Universal Music Group mean that, if you sell 50 million albums by 100 moderately successful artist, you make far less than if you sell 20 million by an Eminem or a Shania Twain. In the second, most of the £20 m represents pure profit*'[128]

iv) Reducing artist rosters post Mergers - only the most successful artists after a merger or acquisition are retained, meaning that many otherwise successful recording acts, including many who would generally be considered a good investment had they just been signed, are 'dropped'.[129] Ironically many such acts that are let go are subsequently picked up by one of the 'major's' competitors, often an independent (like Sanctuary) rather than another 'major'

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[126] Dobie, Ian, 2002, 'The Impact of the Internet and new technologies on the Music industry', www.music.salford.ac.uk/music2/web/general/staff/id.htm - a useful guide to the impact of M& A and consolidation on music corporations

[127] Recent examples include Kylie Minogue, Coldplay and Robbie Williams (EMI), Jennifer Lopez and Michael Jackson (Sony), Madonna (Warner), U2, Shania Twain and Eminem (Universal), Dido, Christine Agueliera (BMG)

[128] Sandall, Robert, 2003, 'The day the music Industry died', The Sunday Times

[129] Recent examples of such acts include The The (Universal). Rod Stewart (Warner), John Mellencamp (Universal), Alison Moyet (Sony)

v) Maintaining massive Investments in Artists - Even as they acquire successful artists through M&A activity, the majors continue to fund and invest in a very large number of other artists. It is here that the limitations of their A&R and creative policies are highlighted. Signing as many acts as possible - not all of whom will even get their recordings released - is the only creative strategy open to the majors in their search for future 'Mega stars'. Unfortunately a mere 10-15% of these recording artists actually even cover the total investment by their record companies (the figure for those who actually have a hit is even reported to be as low as 5%). '*Given the price for launching a new act starts around £500,000 it's less surprising to learn that fewer than 1 in 10 new signings make money for the major labels*'[130]

The fact is that it is the superstar 10% of acts that are subsidising the other 90%. [131] Clearly this does not reflect well on the typical major's ability to sign and develop successful artists. We will cover this issue in more depth in the 'A&R dilemma ' section.

vi) Share Price Volatility - As is evident with companies like Universal, EMI and Warner Music Group the major corporations are constantly subject to direct pressures associated with volatile share prices. The typical initial reaction of a major to a significant fall in their share price is to shed staff. Usually euphemistically described as 'restructuring' this further encourages staff to always take a short -term view on key matters. It also means they are encouraged what is required to keep their jobs rather than plan for the future and develop acts with long term potential.

vii) The Creative Bankruptcy spiral -

To describe the pressures of trading as a public company and how these affect the major music conglomerates this author has developed a concept to illustrate the various stages of this financial & creative process within a typical music conglomerate. This process follows on from Keith Negus' description of '*the production of culture*' and how "*the commodification of music and the control by a few major corporations has a detrimental impact on the sounds we get to hear*"[132]

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[130] Sandall, Robert, 2003, 'The day the music Industry died', The Sunday Times

[131] Gundersen, Edna, 2002 "Rights issue rocks the music world" USA Today, September 16th

[132] Negus, Keith 'Music Genres and Corporate Cultures', Routledge 1999 page 15

The key corporate strategy is 'applying order and enforcing accountability' [133] with the 'aim is to control and order the unpredictable processes and diversity of human behaviours …which riddle the music business with uncertainties' [134]. This strategy of control forces the implementation of constantly re-assessed and reviewed short-term goals and targets and produces and encourages the kind of short term thinking and planning all too evident within the conglomerates. From the graphic it can be seen that it is the source and application of external finance (especially the constant pressure of meeting stock market and shareholder expectations) that affects the quality of creativity and innovation within the creative units of the music conglomerates.

Within the Music Industry the relationship between the quality of new music, signed and developed by the record labels and music publishers is clearly influenced by the rigorous financial pressures applied by the demands of the modern multi media conglomerate.

What the 'creative bankruptcy spiral shows is that successful innovation and creativity within the music industry cannot prosper within the existing business model of the 'majors'. The demands and pressures placed on these companies are constantly being shaped by the conglomerates' relationship with the financial markets. What this concept demonstrates is how constant short term thinking within the corporations is a direct result of the constant need to please shareholders and the stock market analysts. This produces a series of pressures within the company that demand a short-term outlook on the part of the key employees leading them to sign what works in the short-term rather than what is in the long-term interests of the company. Whilst this can and usually does produce results - especially in companies like Universal imprints Interscope and Polydor - the acts that these label sign usually only have finite shelf life and the label has missed out on sustained growth in its catalogue. Thus when shareholders pressure the company for greater growth and higher profits, it is unable to do anything other than continue to sign the short-term acts.

[133] Negus, Keith 'Music Genres and Corporate Cultures', Routledge 1999 page 31

[134] Ibid.

Stock market-shareholder pressures for growth/Profits -> (1)	Internal financial pressures on Record Label -> (2)	short-term outlook for Label managers -> (3)	Label's creative team sign only 'pop' artists -> (4)	Label gets immediate, but limited sales success -> (5)
short-term pop acts only have short careers -> (6)	No long term development artists -> (7)	no sustained growth in catalogue -> (8)	increased stock market - shareholder pressure -> (9)	Increased Internal financial pressures on Record Label ->10-1
Increased short-term outlook for Label manager -> 11-2	Label's creative team sign only more 'pop' artists ->12-3	Label gets more immediate, but still limited sales success -> 13-3	more short-term pop acts with short careers -> 14-4	Still no long term development artists -> 15-5 etc

From this graphic one might also argue that creative companies should succeed most, when there are few external financial forces such as stock market share price or institutional shareholder pressures in place.

Part 9 - Some manifestations of 'short-termism' -

It is no coincidence that the most obvious example of short-term signings are the so called 'pop acts and that it is these recording artists that the 'majors' have concentrated most of their efforts and resources on over the past few years. 'Pop' music has been the preferred choice to 'alternative' music, not because it is better but because it is easier to sell than "indie' or 'alternative' music. It is also no coincidence that the rise of 'pop' as the dominant force has coincided with the increased consolidation of the major record labels.

'Pop', by definition, is what is popular, even if it may have a lower 'cultural' value than so called 'alternative' or 'leftfield' music amongst the record label's employees and generally amongst the media. Nevertheless it has the simple advantage of providing immediate results and it is relatively predictable and therefore is easy to manage. To the A&R executives within these major companies the benefits of concentrating on 'pop' has several distinct advantages:

<u>The target market is known</u> - 'Pop' music, over the past 5 - 8 years, tends to target one particular age group (perhaps in a way that has never been known before), i.e. the 6 - 15 year old, predominantly female, record buyer.[135]

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[135] " *Erlap notes that the industry has been distracted from its traditional target demographic of 15 to 25 -year old males - the most catalogue building demographic there is - to targeting 10 to 15 -year old girls*"

Anonymous, 2003, 'A new shape for music', Music Week, January 11th.

Compilations - 'easy pickings' - The major labels make very high profits as well as gross revenues from the release of compilations - which in effect merely package together all of their currently successful single releases on one album. These are designed, assembled and marketed to be sold in hundreds of thousands rather than the more modest sales, one might expect from an album release of a new hit artists.

TYPE OF ARTIST	MATERIAL	GENRE
Single Artist	Best Of/ Greatest Hits	Genre Specific
Multi -Artist	Current Hits	Non genre specific
Multi Artist	New releases	Genre specific/ new acts
Multi Artist	Back catalogue	Genre Specific
Multi Artist	Mix Album	Genre Specific

Compilations- the business rationale - the 'majors' usually have a 'break' in their contracts with their exclusive recording artist, which allow them to reduce the main 'headline' royalty in certain circumstances.

The list of these reductions is extensive but the main categories would include; Overseas sales, sales at reduced prices, including the so-called "mid-price" and budget" prices and compilation releases. The rate for compilations is usually 50% of the normal rate.

Given the marketing driven nature of these releases it is inevitable, the majors consider this a vital source of profitable revenue. In fact each of the 'major' UK labels has a separate dedicated 'compilations' marketing division. These include Universal TV, Warner Special Products, and Sony TV. Even when they have their dedicated 'compilations' division, a 'major' might also have an stakehold in another company or a brand releasing similar compilations, e.g. Telstar (part-owned by Warner Music Group) or 'The Hits', (Sony/BMG). The established market brand leader "Now That 's What I Call Music" is a co-venture between EMI Records, Virgin Records and Universal Music.

Affect of Compilations on Individual Artists - There has never been any real industry-wide unanimity on this subject and it would be fair to say, there are two opposing schools of thought.

One side believes the whole purpose of single releases is to 'showcase' an individual artist's album (as it is the most profitable format) and that the album is the springboard to a long-term career. In this situation, the priority should be ensuring that those who like the artist's single should be 'encouraged' if not directed to purchasing the artist's album. Any use of a hit single outside of the artist' album is likely to impair and hinder sales of the album and compilations are considered the most extreme example of this.

The opposing viewpoint is that compilations do not harm the sales of individual artist's albums and are aimed at those who would not purchase individual artist albums.

It is unlikely the 'majors' would ever openly acknowledge that compilation albums could damage sales of their individual artist's albums but it is very clear that the 'majors' make very substantial profits from their compilation releases, certainly well in excess of what they might expect from artists albums. What is apparent also is that if a major label needs to generate quick return revenues and profits it is more likely to choose compilation releases, than increasing marketing spend on existing individual artist releases. This is borne out by the large number of 'best of' compilations released each 4th Quarter to capitalise on the Christmas market

'Compilations' are seen as providing 'value for money' and if Internet based filesharing has proved one thing, it is that music fans are keen to acquire copies of individual tracks rather than whole albums. 'Compilations' appeal to that same attitude and it can be argued are largely bought by those, who may not buy albums as such and are put off by the relative high costs of purchasing one album. Compilations almost by definition now provide more guaranteed value, not difficult when they can offer a much greater quantity of quality material because they contain usually just the most successful releases.

Having said that, it also clear that the long-term development of recording artists requires that sales of their early albums are sufficient to warrant the company continuing to record them. Anything that inhibits sales of these early releases might thwart that ambition.

The Singles market -this author believes that the most clear-cut manifestation of shorttermism - particularly in the UK market- is the dominance of the single as a format. Not because of the financial terms but because of its relevance as guide to what is successful and what is not. It seems obvious to point out that many successful recording artists of the 1970's including Led

Zeppelin and King Crimson, refused to allow the release of singles and their fans bought their albums instead.

Singles are usually bought by a relatively small and, indeed declining, segment of the total number of music purchasers. However, the 'singles chart ' is still used habitually as the main determinate of the actual success of the artist concerned - both by radio and retail. This rather lazy approach to choosing artist releases to rack in their stores or add to their play-lists reinforces the influence of the single on the market as a whole.

Of course the single is by definition merely one aspect of an artist's portfolio and if it does not work it can mean the album - usually produced at considerable cost is not even released. Certainly one can argue that the single format has an influence over the market out of all proportion to its financial value and negates the efforts of album based artists to have access to radio and to retail.

Part 10 - The A&R Dilemma -

The pressures and problems associated with working within the music conglomerates are rarely addressed publicly by their senior executives but given the events of the past few years it is not surprising some are now starting to air their concerns about the viability of creativity within their companies. The dilemma, facing A&R within the majors, is openly debated within the music business trade press. A recent Music Week article, identified how: '*Many highlight an increasing shift away from long-term talent development to short-term, top-line driving pop product, in a landscape, where turnover, market share and share price worries are driving the business- and replacing old fashioned virtues of patience and long-term investment*.'[136]

Perhaps the most articulate and genuine plea came from BMG UK's outgoing Chairman Hasse Breitholz when he argued: '*In its traditional sense, A&R within the majors is an impossible task - bringing with it unbelievable pressures often counterbalanced by unrealistic incentives*'.[137]

He goes on to say that: "*If we in the record companies don't allow artists to grow, we will perish. There has to be a healthy balance between out-of-the box hits and long-term development*".[138]

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[136] Anonymous, 2003, 'A new shape for music', Music Week, January 11th

[137] Breitholz, Hasse, 2003, 'Teamwork not egos: The key to my success running BMG UK'. Music Week, April 5th page 23

[138] Breitholz, Hasse, 2003, 'Teamwork not egos: The key to my success running BMG UK'. Music Week, April 5th page 23

Breitholz also highlights the pressures placed on both artists and the company's creative staff when he comments that: " *One hit you're a genius, one failure and you're history - and that goes for artists and for personnel. Surely there must be room for developing both artists and employees*"[139]

It is evident that A&R - historically the most important creative source within any major label - now rarely provides continuity of vision or purpose given the unstable environment the companies have to operate in has to work in. Yet in its traditional form, A&R - i.e. signing, nurturing and guiding long-term career artists - is possible within the majors and is best exemplified by one person - Clive Davis.

This former President of CBS records founded Arista Records and (after being removed by Bertelsmann because he had passed the recommended retirement age) established his own J Records. In each case Davis has dominated the label's creative strategy and signed career artists (Barry Manilow, Whitney Houston, Alicia Keys,), all of who achieved immediate but sustained sales success. Other notable executives who show signs of following in Davis' footsteps are Jimmy Iovine at Interscope and Lucian Grainge at Universal in UK. Each of these individuals could be described as entrepreneurial and in fact appear to run their labels like personal fiefdoms - ironically along the lines of the successful independents.

Another former BMG executive with experience at both Virgin Records and Sony's Epic label agreed with his former colleague Breitholz: ' *A&R is generally in trouble - it is a major problem on a worldwide basis*' [140]. He identified what he saw as another possible development: '*Companies are looking more and more to outside companies to develop these artists. But I haven't seen any smaller labels develop in recent years either - that's one of the major problems the UK has got*[141]'. Whilst he may be unsure about the next generation of independents Griffiths clearly feels the majors cannot sustain successful A&R policies within the current structure

Independent Companies like XL (part of Beggars Group) have managed to take advantage of the creative malaise within the majors and according to co-owner Martin Mills: "*XL sits in its own place in-between 'indies' and 'majors'. It can do what the majors do in terms of power but with the approach of an independent*'[142]

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[139] Ibid.

[140] Anonymous, 2003, 'A new shape for music', Music Week, January 11th.

[141] Ibid.

[142] Roberts, James, 2003 'Creative fire is real bedrock of XL's independent success'. Music Week March 22nd page 7

Mills does not think '" *the label could have flourished in the same way through a major. It works because of the synergies - each does their role in an unspoken way. A large part of it is about not imposing rules and regulations*'[143]

XL's Managing Director Richard Russell explains that the secret of their success is that: "*We've focused on developing the culture of XL over the past few years and creating an environment in which talented people can thrive. We've made this an exciting fun place to work, where people enjoy what they're doing while taking it very seriously and ultimately feel a real sense of pride in representing XL*".

One can see from the above that is the environment and culture in which the creative staff work and the absence of 'rules and regulations ' that significantly contribute to the creative and financial success of a company like XL. Yet as can be seen from the creative bankruptcy spiral and the pressures on the majors to maximise profits these are the very elements that are difficult if not impossible to generate within the 'majors'.

Even those independents like Ministry of Sound that attempted to emulate many of the majors' business philosophy and tactics have stepped back from the brink and recognised that A&R is not jus t about spending a lot of money to acquire the latest 'big thing' - but in fact means developing creative policies to acquire material on economically sound and viable terms: '*As everyone at Ministry is keen to stress, artist development will remain a priority but through smaller, cheaper deals, growth which is more organic and more sustainable. That should perhaps be the mantra for the entire Business*'[144]

Perhaps as some argue long-term artist development is *a 'thing of the past*'[145] and that companies are unable to ' *sustain such investment and consumers are uninterested in the sort of artist loyalty, that has characterised much of rock's history*'[146]. However most observers believe ' *that long-term acts - and their catalogue - are key to a healthy industry. It is just that the global industry has lost sight of that goal*'[147]

Another BMG executive, the current President of BMG Entertainment UK's Music Division, Ged Doherty makes a compelling case for changing the way in which recording artists and the

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[143] Roberts, James, 2003 'Creative fire is real bedrock of XL's independent success'. Music Week March 22nd page 7

[144] Talbot, Martin, 2003. 'Lessons to be learned for all'. Music Week, March 8th, Page 3

[145] Anonymous, 2003, 'A new shape for music', Music Week, January 11th.

[146] Ibid.

A&R process are treated within the majors. :'*Unless we learn how to develop artists better, then all the synergies and rationalisations will add up to little more than shifting deck chairs on the Titanic. If you are in the business of music, then the people who make the music are the assets that matter most. Its that simple*'.[148] He concludes that the major conglomerates must think ' *in terms of long-term artist development not short-term exploitation*'.[149]

Given BMG's change of strategy (in the post-Middlehof era) and a recognition by its management of the pitfalls of stock market generated expansion, it is noticeable BMG's executives have been the first to openly articulate concerns about short-termism and the blinkered creative policies associated with the major conglomerates. One wonders whether this recognition would be as openly expressed within the other publicly quoted majors.

Part 11. The stock market analyst's and the shareholder's perspective -

This section of the report is based on research, within the financial press. It will attempt to highlight the way the City and Wall Street look at media shares. In particular it will demonstrate how - without a steady flow of positive financial news showing constant growth and increased profits -

[147] Anonymous, 2003, 'A new shape for music', Music Week, January 11th.

[148] Doherty, Ged, 2003. "Development is key to success". Music Week February 1st

stock market analysts can and will undermine and in the case of EMI even destroy the credibility of a publicly quoted music company.

One argument against the way in which the stock market operates would be the manner in which shares in telecoms were traded, which has been characterised '*as the greatest destruction of capital of the modern age*'.[150] The same article concluded that '*of the estimated $750 billion invested in telecoms worldwide in pursuit of the information society, at least $350 billion has been entirely wasted*'[151]

The same author even argues it is the stock market that represents one of the great dangers for the music industry, as, in this scenario, it is the: '*copyright industries, whose rights are deemed to have obstructed the development of a proper market*'[152]. It is the music industries and other content owners that have been blamed for obstructing the digital economy and he anticipates the doomsday scenario of copyright being replaced with a right to equitable remuneration in order to establish a 'proper market'.[153]

During the same week in 2002 that EMI was ejected from the FTSE 100 index, the company achieved an unrivalled 35.6% share of the UK album chart[154] - arguably one of the best barometers of financial and creative success within the music industry. In the same week an analyst at Morgan Stanley warned that: '*Compared to Universal and Sony, we believe EMI is under-performing in bringing new talent to the market*'[155]. The same analyst argued that EMI was weak in:' *Sourcing and promoting new talent and exploiting album sales and follow-on publishing opportunities*'.[156]

This astonishing analysis of EMI - which contradicts what the rest of the music industry believes - is far from untypical. EMI's UK labels have the reputation of being the most consistent of the UK majors over the past few years in signing and developing long-term career artists - from Coldplay to Radiohead.

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[149] Doherty, Ged, 2003. "Development is key to success". Music Week February 1st

[150] Parker Nigel. 2002 " Passing the buck - a feature on the Dis-information Society" Music Managers Forum (MMF) magazine. Autumn, Page 14 - 15

[151] Ibid.

[152] Ibid.

[153] Ibid.

[154] Cassy, John, 2002. "Stuck in the EMI Groove", The Guardian, September 6th

[155] Ibid.

[156] Ibid.

Also open to criticism are the expensive 'big' deals taken on by EMI's executives in an effort to placate and maybe even impress the market. Even a deal to acquire the classic Jobete music publishing catalogue is seen as not much better than the Maria Carey fiasco: "*If I were a cautious EMI shareholder I'd have my doubts. After all the firm recently wrote off a reported £38 million on Mariah Carey and the history of such Mega-deals is chequered to say the least*"[157]. One wonders what shape Emi would be in had it not embarked on such mega-deals over the past 2- 3 years, all of which can be traced to attempts to please the market.

It is clear that for the shareholders financially successful long-term creative signings (as with EMI's Norah Jones) are not enough - what the analysts and investors want to see are 'deals' - which in EMI's case meant a ' *merger with either Germany's BMG or AOL Time Warner that would catapult the company to the top of the tree*'.[158]

This attitude amongst the stock market analysts and investors is all about trying to make " a killing' rather than a profit and shares in music companies are not considered as long-term investments. Music companies might grow but as we have seen in Section 6, the only kind of growth the stock market is impressed with is the very big deal. Yet these are the very deals that in the case of AOL Time Warner and Vivendi Universal brought those companies to the brink of bankruptcy. EMI's lack of the "big deal" has not been good enough to pacify the analysts and brokers who downgraded the company's worth to a mere £730 million.[159].

Even when EMI fought back and even threatened legal action against the '*stock-broking arm of one of France's biggest banks following the publication of a heavily critical research note*'[160], which strongly advised investors to sell EMI shares, the company was powerless to actually defend itself. All this demonstrated was the City's inability to understand a viable successful music corporation and surely has hastened the likelihood that the company will be bought out by private equity investors.

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[157] Jelbert, Steve, 2002. 'Just for the record.' The Independent Review, October 4th. pp 16 -17.

[158] Ibid.

[159] Wachman, Richard, 2003. 'Music giant EMI 'faces buyout' ' The Observer Business Section March 16th, page 2

[160] Cassy, John, 2003, 'EMI may sue over broker's note' The Guardian, January 25th

EMI's treatment by the stock market embodies what appears to be a fundamental truth of share investment namely that '*Market perception tends to drive stocks in the near term, not fundamental reality*'[161].

Shareholder caution- Many investors are increasingly sceptical of the advice being handed out by analysts. One article argues that the whole concept of EBITDA is a misleading measure that allows public companies to hide very serious discrepancies within their balance sheet.[162] The analysts are preoccupied with EBIDA and rarely pay much attention to cash. This was very clearly the problem with Vivendi/Universal and probably led to the dramatic slump in the share price. Once the discrepancies within Vivendi's accounts were brought to light shareholders dumped their shares.[163].

Shareholders are now more aware of the games being played by conglomerates to boost their company's earnings often because the share price has become a tool in take-overs:

'*Conglomerates were trying to pump up their stock to use it as currency in take-overs*'…' *Often otherwise high -grade companies start with a number (for quarterly earnings) and work backward. Situational ethics has reared its ugly head*'[164]

Harvey Goldschmid, Columbia Law Professor, who worked at the SEC in the USA, identified several factors at work within public companies that contribute to how they show their earnings and shape the value of their share prices.

- *Declining quality of company accounts* - accounting standards have fallen ever since the US federal government declared as 'anti-competitive', the code of conduct stopping one accounting firm from undercutting another. Goldschmid argues that this code of conduct:' *protected accounting firms from CFO's who didn't like being told no*'[165]

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[161] Quoting Tobias Levkovich, from Salomon Smith Barney - Greenberg Herb 2002 'Against the grain - Lies, damn Lies - And stocks', Fortune magazine www.fortune.com/fortune/againstthegrain/0,15704,373397,00.html

[162] Anonymous 2002. 'Why Companies fail - Three Quick fixes'. Fortune magazine www.fortune.com/fortune/articles/0,15114,373185,00.html

[163] Anonymous, 2002, 'Messier's mess', The Economist, June 10th pp 69 -71

[164] Sewer, Andy, 2002. 'Dirty Rotten Number' Fortune February 4th www.fortune.com/fortune/investing/articles/0.15114,368567-2,00.html

[165] Ibid.

- '*Rise of the cult of the shareholder*'- he argues that because the emphasis is always on increasing or '*levitating*' a company's share price, ' *many executives will do almost anything - legal or otherwise - to make it happen*'[166]
- *Shares paid to senior Executives* - increasingly senior executives are paid in shares and share options and thus are effectively compensated for increasing the value of the shares or the company's earnings growth[167]
- Accountability of Senior Executives for share prices - this means that the senior executives are under far greater pressure to maintain the share price and increase its value. If a CEO's job is at risk if the share price falls too much, it is fair to assume the CEO will do everything to avoid that or to rectify the situation. Clearly this was what persuaded EMI's former CEO Ken Berry to pay so much for Maria Carey in a desperate attempt to rescue EMI's share price in 2001.

From the shareholder's viewpoint all of the above factors influence their judgement of a company's value. It is clear the music industry suffers more than most other investments because of the perceived 'risks' involved in the industry. These risks include signing and establishing viable long-term musical talent, an inability to maintain regular income and earnings, let alone sustain regular increases in earnings and the affects of global piracy. There is also a sense that, in a shrinking market, the only purpose to owning shares in music and media companies is to profit from the kind mergers and acquisitions activity that will be forced on the likes of EMI or Warner Music group. Within the financial press it is clear that holding shares in music related corporations is not really considered worthwhile in the long-term.

[166] Ibid.

[167] Ibid.

Part 12 -The recording artist perspective

''*We're on the threshold of a whole new system… The time where accountants decide what music people hear is coming to an end*'. *(Keith Richards/Rolling Stones)*[168]

The vast bulk of this report is written from the viewpoint of the music companies - both independent and major conglomerate as well as the shareholders / analysts. However the other real stakeholders in all this are the creators - the recording artists and songwriters and this section of the report will examine how the issues raised elsewhere in the report affect the artist themselves and their reaction to them.

King Crimson founder and acknowledged musical visionary Robert Fripp identifies many of the key issues that affect artists, particularly those who have enjoyed substantial commercial sales. His main argument is that these artists are by and large treated very badly by the industry and that *"The history of the music industry is a history of dissembling, conflict of interest, exploitation and theft - legal, illegal and quasi-legal*"[169].

Fripp establishes the artists perspective clearly when he states that '*I take it as a given that major record companies are not primarily interested in the development of an artist's career, but exploiting them when they're hot. When the artist begins to cool it's easier to move on to the next hot item*".[170]

For an artist like Fripp the current A&R debate within the major labels, i.e. long-term artist development versus short-term exploitation, is little more than hot air. He finds it hard to believe that the majors can ever seriously take the interests of the artist seriously. Rather he believes the mainstream corporate music industry ' *determines and directs the music, which is available to the public*'[171] and in this he echoes the views of Keith Negus about the "*commodification*' of music.[172].

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[168] Gundersen, Edna, 2002 'Rights issue rocks the music world' USA Today, September 16th
The article covers the rise of RAC (Recording Artists Coalition) -
[169] Fripp Robert 2001, 'DGM's founding mission Statement'www.disciplineglobalmobile.com
[170] Ibid.
[171] Ibid.
[172] Negus, Keith 'Music Genres and Corporate Cultures', Routledge 1999 page 15

Fripp is also no great exponent or supporter of independent labels either seeing that they '*function as A&R departments, or talent spotters, for the majors who then exploit the new artists* '.[173]

He sees that there are '*few credible independent record companies*' and that the' *main credible independents have been bought up by majors, so they're not really independent*' [174]

For an artist such as Robert Fripp the future belongs to artist-owned labels and ensuring recording artists do not surrender ownership of the copyright in their songs and recordings to faceless corporations. This is central to the arguments of many of the artists who belong to the RAC9 Recording Artists Coalition). The RAC has been lobbying US lawmakers to change the way in which contracts and royalty accountings are handled by the major labels. In particular the RAC has argued against the way in which successful artists are tied to punitive 6 - 8 album recording agreements, that are actually illegal in any other profession - the music business having secured an exemption from the California Statute restricting contracts to a maximum of 7 years.[175]. Other issues raised by the Coalition include:

- **Accounting practices.** - LA Lawyer Don Engel calculates the extent of underpayment to Artist as anything between 10% and 40%, and Engel argued that music industry accounting practices are '*Intentionally fraudulent*'*... with* '*Royalties based on complex and antiquated formulas that favour labels* '[176]

i) **Copyright and ownership** - it is said that '*the record business is the only industry in which the bank still owns the house after the mortgage is paid*'[177]. This might have been tolerated in the industry of the 1970s and 1980s but given the extent to which the industry has consolidated the artists are only too aware that it is their wares and rights that have been traded for vast sums. US Artist manager Simon Renshaw puts the point very clearly: "*The truth is, this system would not be suffered in any other business. You have record companies bought and sold on the strength of copyrights created by artists who sign away all rights in perpetuity to a faceless corporation*".

ii) **Payola reforms** - the system unique within the USA of '*hiring of independent promoters to lobby radio stations to play certain records*.' This is one aspect of the majors domination of the

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173 Fripp Robert 2001, 'DGM's founding mission Statement'www.disciplineglobalmobile.com

174 Ibid.

175 **Gundersen, Edna,** 2002 'Rights issue rocks the music world' USA Today, September 16th

176 **Gundersen, Edna,** 2002 'Rights issue rocks the music world' USA Today, September 16th. page 2

177 ibid.

market that can be seen as stifling creativity and diversity as it requires only financial muscle not creativity to secure radio play

Tom Waits, one of the high-profile members of the RAC, comments: "*These corporations don't have feelings and they don't see them selves as stewards of the work.*[178] Another RAC member Don Henley argues that: "*Like all other corporations, the music industry has gotten greedier…It's all about profit, profit and more profit that always comes at a cost of principles. The predicament the record industry finds itself in is of it's own making'*[179]

Henley also argues against '*media conglomerates who have little or no knowledge of the record industry and no communication with artists. Even the midlevel people who love music have to march in lockstep with corporate policy'*[180]. This point is echoed by Simon Renshaw when he comments that:' *In the past 20 years, an industry that was led by visionaries and music lovers has become dominated by accountants, financial analysts and people who can't think ahead more than 90 days'*[181]

What is clear is that successful recording artists are tired of the current heavily consolidated music industry. When faced with statistics that show 'fewer than 5% of signed artists deliver a hit'[182], they see this as evidence that the music industry is simply not up to the task of breaking new talent. It is doubtful whether many would agree with Miles Copeland's argument that ' labels need the cushion of long-term contracts to recoup investments and justify risk'.

The issues raised above are not likely to inspire confidence amongst shareholders and market analysts. Furthermore it is clear that many musicians no longer see the mainstream music industry as being representative and as we move to the realities of global digital distribution of music more and more artists will attempt to side-step the majors altogether.

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178 **Gundersen, Edna,** 2002 'Rights issue rocks the music world' USA Today, September 16th . page 3

179 ibid.

180 ibid.

181 Ibid.

182 **Gundersen, Edna,** 2002 'Rights issue rocks the music world' USA Today, September 16th . page 4

SECTION 4

Alternatives and Recommendations -

A) The new way forward - This report highlights how the major music conglomerates are struggling to balance the twin demands of meeting investor expectations and maintaining and continuing to invest in their main intellectual property assets.

There are other ways to nurture creative talent and it is these alternatives that must be examined because of the inadequacies of the majors. They are no longer interested in just acquiring talent - they are only motivated by the successful artists. Whilst this is the result of the M&A activity of the 1980s and 1990s and the resulting consolidation of the industry, it also means that the majors miss out on 'start up' talent and usually end up overpaying for such talent, when they become available. This author believes that it may be necessary to look into new ways for the independent sector (which is far more successful in discovering new talent) and the conglomerates to work together, particularly in what might well be a shrinking market.

It is clear that the majors have to look to reduce their costs and increase their profits and this can only happen if they invest on a meaningful long-term basis and avoid the pitfalls of chasing market share to boost the appearance of success.

The primary observation of this report is that the creative needs of the music industry, in itself a high risk enterprise, are unlikely to be met by the continued dominance of the entire sector by the entertainment-arts conglomerates. The goals of the majors are dictated by a risky and volatile stock market and it is the pressures that result from this, which compounds the industry's problems. The stock market has been a useful source of funding for those corporations wishing to expand but it is an inappropriate source of funding within an industry that requires fine-line judgement calls and creative instincts or hunches.

The main recommendations of this report are:

1. **A&R should be a function of the independents** - the majors have to look to a future where the primary creative activity within the industry takes place within the independents. It is the independents who can develop and nurture talent in a low cost, less risky and more profitable fashion.

2. **Majors should focus on finance and distribution**-The function of the majors should be to distribute and finance the independents in return for a share of the profits.

3. **The majors should not 'buy out' the independents** - as is clear from previous sections this usually only results in the elimination of the people responsible for discovering successful talent. The music industry can prosper only when there is a thriving independent sector. That is why the structural problem between majors and independents cannot continue - the two sides have to find a new way to collaborate otherwise the artists may take matters into their own hands and set up their own companies to distribute their wares.

B) Universal Music v Menace Music - an example of the new way forward

The following analysis of this author's recent attempts to establish a new way of working - between an independent music publisher and one of the 5 multi-national conglomerates - is included to show how new ways of working between the independent and 'major' sectors might work

For the past 12 months I have been negotiating a new kind of publishing agreement with Universal Music Publishing one that I hoped would establish some new kind of principals for acquiring and developing new talent. With 28 years experience in both music publishing and artist management, it is hard not to worry that the music industry is steadily losing touch with one of its primary goals. Signing and developing new creative talent on profitable, long term mutually fair agreements.

It is apparent that artist management and the artist's professional advisers are motivated by the size of the deals that they can do. It is easy to survive on the commission and fees that can arise from these deals. Equally clear however is that managers and professional advisors are not always primarily motivated by the goal of long-term success for their talented clients.

Managers can blindly accept the short-term outlook of the industry as a given and adapt to this outlook by maximising their share of the short term spoils usually in the form of inflated advances. Managers no longer or very rarely believe that record label deals or publishing agreements offer a long-term guarantee of success. Equally clear is that the labels (and the music publishers), the managers and lawyers do business with, are very willing to pay inflated advances. This is where managers take advantage of the companies' obsession with gaining short-term advantage over their competitors.

10 years of running Menace Music Management has proved that there was little to show for a commission-led existence. Discussions with Universal Music Publishing showed they had an entrepreneurial outlook and a willingness to invest in new talent. This was not because of absolute guarantees about short-term success, but a genuine belief that they could make artists/ writers successful with some prudent financial and even more importantly substantial creative support.

After these discussions, it became obvious that there was more to achieve over the next 10 years than the previous 10. This meant something more substantial than commissions to show for all the work and effort and meant being involved on a long-term basis with the music publishing copyrights of the management clients.

The downside of this deal is that Menace will not commission it's clients' advances as before and Universal would not replace these lost commissions with big advances for Menace's share of the income. Menace can only make money based on the actual earnings of each signing as it receives 50% of the profits from each of the deals. The deal with Universal changed this company's outlook on the industry. It is also a significant reason for choosing this topic for my dissertation.

The deal with Universal also highlighted the pressures on creative individuals working for other "major" conglomerates, especially how they are not encouraged to think and plan long term. This mindset is to be expected, when success comes down to making your numbers each month or quarter rather than with planning the long-term roster of talent.

C) Financial Analysts View - three strategies for the industry:[183] are recommended in the following article in the Economist,

1) Further Consolidation - EMI need to merge with Warner - but can they afford it?

2) A renewed effort "to *rely less on instant stars and more on long-term talent*"

3)"*Transform narrowly defined record firms into broader music companies*"- include and participate in revenues from touring, concerts, sponsorship, (40% of music industry is made up of those revenue sources)

D) EMI - Going private? - Writing this report was also as a result of having read very many adverse comments about EMI,, and by implication the music industry, within the national and in particular the financial press over the past two to three years. These adverse comments and

[183] Anonymous, 2003, 'The Music Industry - In a spin', the Economist, February 27th.
www.ecomomisr.co.uk/business/displayStory.cfm?story id+1611255

criticisms added new pressures on the company and arguably led to the series of management errors that compounded the corporation's problems rather than solved them. It showed that with the market there is no pleasing anyone and once the 'perception' exists that the firm is weak and vulnerable the market will not be kind.

It is difficult to reconcile a company that has been so vilified and pilloried by the financial press with one that is widely considered the most attractive label for most recording artists and one of only two capable of developing and sustaining a long-term recording artist's careers. EMI has shown itself willing to come up with innovative ways of dealing with creators and in almost every significant genre of music it is the market leader.

With the dramatic decline in the EMI share price, is it time to now consider whether a dedicated, stand-alone music company can even operate or survive as a publicly quoted company? Perhaps EMI would be better off going private than continuing its roller coast ride on the stock exchange. The senior management of EMI have, according to the Observer's Richard Watchman, already started talks to achieve this goal. Watchman states that EMI has been: '*Targeted by private equity groups after a dramatic slump in its share price during the past three months*' and that '*The buyout would be led Alain Levy, the much respected head of EMI's recorded music division*'[184]

[184] Wachman, Richard, 2003. 'Music giant EMI 'faces buyout' ' The Observer Business Section March 16th, page 2

Section 5
Conclusions

The main conclusion of this report is that creativity can flourish within a publicly quoted company, but that the affects of the stock market make sustained creativity much more difficult than it would be within an independent. The external financial pressures on the majors are usually a consequence of - parent company indifference (as with Sony), over-ambitious merger and acquisition activities of a parent company (e.g. Vivendi and AOL Time Warner) or (as with EMI) an irrational and false perception of the company's value by the market. Whatever the cause these pressures will adversely affect the major company's goals and strategies and the quality of the music produced will become secondary to the need for constant growth, increased market share and higher turnover, irrespective of whether that is achievable only on a short-term basis.

The report recognises that the interests of the shareholders in public companies rarely align themselves with those of the management, artist and employees. The former is looking for a speedy, guaranteed return on investment and the latter for a long-term view on the holdings. It also notes that the distinction between shareholder and management rarely applies to the successful independents, which enables the independent to set its goals and targets without the prospect of intervention.

The report acknowledges the essential, vital role of the independents in maintaining standards of excellence within the market and argues that a thriving independent sector is good for the music industry as a whole, including the majors. It also concludes that the independents and majors need to establish a new relationship and that each should recognise the benefits of the other. The majors in particular should acknowledge the wisdom of Martin Mills who believes '*that small companies are better equipped to weather the future, partly because they can survive with lower sales*'[185]

As the uncertain future of music distribution is very much one of the key problems affecting the industry as a whole, it is important that the industry work together. The general view appears to be that: '*Like it or not the way to restore the industry to health is to embrace digital distribution of music via the Internet. Doing so would be difficult but far from impossible. After all, the music business has long survived by introducing new formats: the long-playing record that replaced the*

78 *single in the 1950s, the cassette in the 1970s, the higher-priced CD, which fuelled a huge increase in sales in the 1980s.*'[186] *EMI's David Munns agrees that 'if we combine digital distribution with physical, we can probably replace the decline in CD sales',* although BMG's CEO Schmidt Holz argues *"BMG should be in the business of producing music, not worrying about how it's distributed*'[187].

BMG's disenchantment with distribution is possibly a reaction against the excesses of the stock market, which very nearly brought his parent company to its knees in its quest to be at the centre of an Internet digital distribution revolution. Ironically now that all the mergers and acquisitions that accompanied that quest are a thing of the past, several conglomerates are losing patience with the music industry. Apparently: '*the Industry forecast is so gloomy that many of them are trying to get out of the music business altogether, Vivendi reportedly considered unloading Universal Music last year but decided against it because there was no way to get a decent price. Debt-laden AOL Time Warner is thinking about selling Warner Music. EMI whose stock price tumbled 61% in 2002 has met with BMG about a possible merger.*'[188]

Perhaps the words of Michael Wolfe describe the future of the music business, one long since abandoned by the very media-conglomerates, which wrought so much damage. '*It will be a low-margin, consolidated, quaintly anachronistic business, catering to an ageing clientele, without much impact on an otherwise thriving culture awash in music that only incidentally will come from the music industry*'. He adds that: '*there will continue to be a market for selling music, however diminished- but it will have to be cheaper music. Margins will shrink even more. Accordingly costs will have to shrink*'.

It is apparent many acknowledge the:' *Effect of the corporatization of the music industry and its growing reliance on Wall Street, that brought about mega media conglomerates like AOL TW*

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[185] **Sandall, Robert**, 2003, 'The day the music Industry died', The Sunday Times

[186] **Leonard, Devin. 2003.** "Record Companies - Facing The Music - They've got the stars, They've got the profits. But does BMG- or any record company - have a future?" **Fortune magazine** March 1st www.fortune.com/fortune/investing/articles/0,1514,433359-2,00,html

[187] **Leonard, Devin. 2003.** "Record Companies - Facing The Music - They've got the stars, They've got the profits. But does BMG- or any record company - have a future?" **Fortune magazine** March 1st www.fortune.com/fortune/investing/articles/0,1514,433359-2,00,html

[188] **Leonard, Devin. 2003.** "Record Companies - Facing The Music - They've got the stars, They've got the profits. But does BMG- or any record company - have a future?" **Fortune magazine** March 1st www.fortune.com/fortune/investing/articles/0,1514,433359-2,00,html

and Vivendi Universal'. [189] Attention should now be paid to developing a new music industry structure, beyond the current model so it can to flourish again.

Section 6

Lines of Further Investigation/Inquiry -

1. The rise of Clear Channel and the impact of US deregulation and subsequent consolidation of the radio industry - the impact on diversity and creative opportunity.
2. The affects of consolidation in retail - how the major labels may have caused the conservative attitudes of retailers to new music.
3. New sources of venture capital for the music industry - especially for 'new model' independents involved in a variety of different revenue sources
4. The influence of the internet on established recording artists decision to set up their own record labels

[189] **De Fontenay, Eric. 2003.** 'The new music industry according to Miles Copeland' www.musicdish.com/mag/bio.php3?author=10

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