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MUMT 301
Final Project 2020

Streaming Services and a Changing Music Industry

Position paper on the negative effects of the rise of streaming services in
regards to the power of major music labels and artist revenue

Abstract

This paper discusses the ways in which the music industry has shifted over the last two centuries, but particularly in the last two decades following the advent of the internet and emergence of music streaming services. Major record labels, particularly the big 3, continue to dominate the industry as they have since the creation of modern sound recording devices, and artists must now procure millions of streams in order to earn the equivalent of an annual salary on the US minimum wage. From most to least distributive platform, Napster leads the DSPs at a per-stream rate of \$0.019, followed by Tidal, Apple Music, Deezer, Amazon Music, Spotify, and Pandora. This has resulted in major backlash among artists, with the likes of Vulfpeck, Taylor Swift, and Jay-Z acting out in efforts to protest these insufficient micropayments, though no significant changes have been made. Parallels can be drawn between some of the tactics used by majors to maintain their high profit margins in both the old and new music economy, notably their (part) ownership of distribution channels and the rates at which they wish to pay their artists. There is hope that, with a rise in total streams and premium subscribers of DSPs this year, there will be an increase in artist payouts, though this is unclear in the short term. The ideal solution would be to renegotiate royalty rates with majors and DSPs, re-center the industry on the artist as opposed to the label, and create more options for artists to monetize their work.

How did we get here?

To understand the rise of streaming platforms and their subsequent effects on the industry, we must first discuss the history of music production and distribution. Throughout the last two centuries, music has been molded by the *limitations* set by the inventions that have enabled the recording and reproduction of sound, starting with the phonograph. Prior to its invention in 1877, music as audio had no medium. Songs were sung or played into existence and passed down from generation to generation through practice, until the development of Western musical notation by European churches in the 6th century. Thomas Edison's phonograph, a wax cylinder engraved with audio recording, became the first commercial means of recording and reproducing sound. It is important to note that for all tangible musical mediums (until the

1980s), the physical parameters of these units determined how long they could be played for. The parameters of the phonograph cylinder, being its diameter and height specifically (and thus the length of its engravings), made it so that it could be played for 2 minutes. If this was recorded music's first medium, this was then music's first modern *limitation*; if you wished to record a song, it had to be no more than 2 minutes long. In 1887 and well into the 1890s, Emile Berliner initiated the transition from phonograph to gramophone by replacing the wax cylinder with a rotating flat disc and needle, making its photoengraving, copying, and mass manufacturing significantly easier. Given that the gramophone record had a larger surface area and fewer rpm (revolutions per minute), this allowed for longer recordings. 3-4 minutes became the new maximum, giving rise to the standard length of what we now know as a "single" in music. 1948 marked the introduction of LP's (long-playing records) by Columbia, commonly known as vinyls. These had an even slower rpm, allowing for 22 minutes of playback on each side. Thus, artists began writing to the size of this new limitation, and it quickly became the industry standard. Vinyls were cheap, easy to use, and incredibly easy to mass produce and distribute, and following the rising popularity of radio broadcasting during and after the Great Depression, the music industry saw a gradual incline in net revenue. Music recording was digitized in 1975, and cassettes eventually overtook LP's in the 1980s before both of these technologies finally succumbed to the emergence of a new medium for music, the compact disc.

This marks the beginning of the digital era and subsequent new music economy. In contrast to vinyls, CDs were small plastic discs that held megabytes of information instead of storing audio in grooves, making its physical parameters irrelevant to the amount of information it stored. With the rapid development of the internet and newfound portability of music (prompting the invention of the walk-man, then iPods), technology continued to surpass and eventually eliminate any limitations previously upheld by the physical unit-based music market, resulting in the downloading of music as MP3s. Online, albums were unbundled song by song, peer-to-peer platforms such as Napster were taking the industry by storm by facilitating the sharing of files between over 57 million users as its peak, and record labels scrambled

to make sense of this limitless and seemingly uncontrollable new medium, being the cloud. Fast forward a couple years, and iTunes leads the industry in sales and downloads, charging users \$1.29 as a one-off payment in an exchange for the permanent download of a song. Fast forward to today, and music has become a commodity completely separate from any physical medium. CDs and vinyls continue to be produced and sold, but the changes in accessibility brought about by the internet have rendered music as a physical good almost completely obsolete; physical sales only make up about 7% of revenue today, in contrast to streaming services, which account for 85% [4]. The music economy has shifted from a unit-based to a service-based one, and artists are now under the thumb of both major record labels and the new industry giants; streaming platforms like Spotify, Apple Music, Pandora, Deezer, Tidal, and Amazon Music. Through a financial lens, and in regards to artists specifically, this dramatic shift in medium and mindset, and the subsequent rise of streaming services is arguably one of the most detrimental shifts to take root in any creative industry as fundamental to society as that of music.

The Structure and Power of the Label

Major record labels have held the reins since the day music distribution was made possible. For simplicity's sake, we can think of record companies as being responsible for what seems like every possible industry interaction imaginable, save for the recording and performing of the music itself (the artist's job) and its distribution (the streaming service's job in our case). This can be anything from the discovery and development of artists, to marketing, promotion, licensing, merchandising, sponsorships, live performances, and artist management [8]. With these responsibilities comes a significant amount of expenses, making labels particularly reliant on steady revenue from any and all sources that will earn them a profit. Given the exceptional power they hold over almost all actors in the industry, recouping their costs is not very hard to do. It *is* hard, however, now more than ever, for the artists.

When an artist signs a contract with a label, they are essentially giving up copyright ownership of their masters (both the original recording of a song as well as the edited, mixed, and mastered version) and

agreeing to receive a royalty rate of whatever income their label receives in exchange for the distribution and selling of their catalogue. Traditional recording agreements see artist royalty rates range anywhere from 10-20%, depending on their level of fame and how much bargaining power they hold in regards to their contract [9]. However, 10-20% of streaming revenue pales in comparison to what 10-20% of the wholesale price of a physical album. The Weeknd, for example, garnered over 5.5 *billion* cumulative streams on his 2016 album, *Starboy*, generating roughly \$4 million. If he had sold even 5 *million* copies, he would have netted upwards of \$10 million [7]. This is the current biggest problem in the music industry in its most basic terms. Of course, there are an unprecedented amount of variables that go into how revenue is allocated, but control over most of these nuances lay in the hands of the major record labels, and the power they hold over streaming platforms.

The first record labels were established in tandem with the phonograph. Remember LPs? They were introduced by Columbia Records, a label that is still widely recognized today. A number of record companies like Columbia were founded as music became a physical commodity, and after a little over a century, left us with what we now call the “big 3” [9]. Universal Music Group, Sony Music Entertainment, and Warner Music Group are the three players that took up 87.9% of the market share in 2017, with the other 12.9% being fragmented amongst thousands of independents [10]. In music’s physical era, some majors would give recordings to distributors who would then sell the physical copies to retailers and radio stations. Columbia Records, founded in 1889, was a consequent iteration of The American Gramophone Company, a manufacturer and retailer of the then modern gramophone machine [3]. While some labels existed as entities separate from distribution channels, some owned these channels or acted as distributors themselves. With only 3 companies making up close to the entirety of the market share today, and the internet allowing for anyone to upload and share their own music without the help of a label, distributors are being phased out, almost absorbed, by these majors. Lest we forget that these majors also own a number of major label subsidiaries [9]. Sony owns the likes of the aforementioned Columbia Records, Epic, and RCA, Universal is the parent company of Interscope, Capitol, and Def Jam,

and Warner controls Warner Bros, Elektra, and Atlantic, to name a few. Maybe unsurprisingly to some, a vast majority of the independent labels that make up the remaining 12.9% of the market share are also owned by these majors [9]. *Major-distributed* independent labels sign artists and make deals with labels to take care of everything except recording, being promotion, marketing, and distribution. *True independents* deal with independent distributors, but are still financed by majors. The play here (there seem to be quite a few once you begin to analyze the inner workings of major labels) is that even independent distributors are owned by the majors. The only difference lies in their sales staff and standards [9].

Revenue Streams

With a shift from unit-based to consumption-based distribution following the digitization of music comes a shift in financial models, and this is where things get complicated. In 2000, CD album sales generated about \$13B US dollars. By 2014, physical sales had dropped 86%, making the industry only \$1.85B that year [13]. Today, Goldman Sachs projects that streaming is set to “increase global music revenue to record highs”: \$40B dollars by 2030. On-demand streaming platforms have essentially “cannibalized” alternative sources of revenue since their launches in the early 2010s, particularly physical sales and digital downloads [15]. This would be an entirely positive transition for the music industry if everyone profited proportionately to one another, but alas, the majors reap the benefits while the artists count their pocket change.

Digital service provider (DSP, or streaming services) payouts vary per service, but usually pay labels 60-75% of their total revenue after taxes. This number tends to be mainly negotiated by the major labels and is split between all artists on the service. It is worth noting that streaming revenue can vary dramatically depending on a number of factors, particularly 1) whether the listener has a free or premium account, 2) where they are geographically, 3) how many subscribers the DSP has, and 4) how many total streams the artist accrued compared to 5) how many total streams the DSP got [9]. Let’s analyze Spotify

first. Spotify pays out 75% of revenue ($\text{DSP revenue} = \text{total revenue} / \# \text{ of streams}$) to rights holders, or in our case labels, who then pay their songwriters and publishers. They are paid separately from artists due to mechanical and public performance licenses, an entirely different payment that we can disregard for the sake of our argument. Of the remaining revenue left after paying songwriters and publishers a portion of that 75%, the label then pays the artist whatever royalty rate has been negotiated in their contract (usually about 15%), and keeps the rest [15]. When you break down the numbers, this amounts to quite literally no money per stream returned to artists. As of 2020, Spotify's per-stream rate for artists falls between \$0.003-\$0.005 [11]. Confused? Here's a different way of looking at it. Spotify first takes its monthly revenue, multiplies it by an artist's streams divided by the platform's total streams of that month, then multiplies that number by 75% to be given to labels. That revenue is then multiplied by the artist's royalty rate, resulting in the artist's payout. What Spotify does not disclose, however, is how streaming payouts differ per geographic region. All we are told is that, given that premium subscriptions differ in cost depending on the country (\$1.67 in India, \$14 in Denmark, \$10 in the US), the value of each stream differs accordingly [12, 10]. Unfortunately, most major on-demand streaming services use a similar formula. Spotify's close competitor, Apple Music, pays artists about \$0.00735 per stream, Deezer's per-stream rate has risen slightly to \$0.0064, Amazon Music pays \$0.00402, and Pandora (a non-interactive webcasting service) has settled at paying artists \$0.00133 per stream. To my surprise, Napster (which was reincarnated in 2011) pays \$0.019 per stream [11]. What's more, DSP typically posit that plays don't count if the user skips the song before the 30 second mark. If you listened for less than 30 seconds, you didn't really listen, and because you didn't listen, no one gets paid. James Shotwell's take on Spotify's per-stream rate is a rather staggering way to put things into perspective:

“[...] Let's consider that the minimum wage in the United States is defined at the federal level as being \$7.25 an hour, which amounts to an annual salary of \$15,080.40 when based on a full-time, 40-hour workweek. With an average payout of \$0.004 per stream, solo artists need 3,770,100 Spotify streams to

earn that amount. That figure is much higher for groups, especially when you factor in label splits, songwriter payouts, and management cuts.” (shotwell)

Using this annual salary, we can estimate how many streams are needed for an artist to earn minimum wage given the per-stream rates of the aforementioned DSPs to evaluate which platform is most distributive, and which is the least. It would then take 2,051,755 streams on Apple Music, 3,751,343 streams on Amazon Music, 2,356,312 streams on Deezer, a staggering 11,338,646 streams on Pandora, and only 793,705 streams on Napster for an artist to earn minimum wage. In ranking these services from most to least “fair”, Napster tops the list (by a lot), followed by Apple Music and Deezer, then Amazon Music and Spotify, with Pandora coming in last. If you ever needed a convincing argument to get your friends or parents to stop using Pandora, this is it.

The Industry’s Revolt

If you are having a hard time wrapping your head around this, you wouldn’t be the only one. Streaming platforms have come under scrutiny as they have risen to the forefront of global music revenue streams, and artists’ responses have been less than subtle. Vulfpeck, an American funk band, countered Spotify’s 30 second rule in 2014 by releasing an album consisting of 10, completely silent, 31 to 32-second “songs” [14]. Fans were instructed to play the album on loop while going about their day, and the band made over \$20,000 before Spotify pulled the album from its catalogue. Taylor Swift removed her entire discography from the platform in protest, only rejoining the service when services agreed to pay artists for plays during the freemium period of their subscription service (free trials) [6]. Jay-Z went so far as to remove his and Beyoncé’s music from popular DSPs and founded his own streaming platform, Tidal, which used behind the scenes content and exclusive rights to their music as a way to acquire customers. Today, Tidal pays \$0.0125 per stream (1,206,432 streams for minimum wage), making it the second highest payout platform of all previously mentioned above, after Napster [11].

The effects of this pay discrepancy are rather profound. For one, selling music at as low of a price as it comes nowadays completely devalues music as we know it. Though the rise of the internet and streaming services have changed how we access music in a number of positive ways, it comes at the cost of economic sufficiency in keeping artists' careers afloat. What was once a one-off payment for a permanent purchase has become a game of picking and choosing songs to stream at will, resulting in micropayments that not only undermine artists, but continue to fill the pockets of majors, whose contracts remain restrictive and market-centric [15]. These innovations have also changed the actual content of what we listen to. Have you noticed that songs with eccentric beats or startling intro verses often grab your attention for longer periods of time? Maybe they become a go-to song of yours. I can't help but attribute this to the 30 second stream rule. Some artists are pouring everything they can into the first few seconds of a song so they do not risk getting skipped, and therefore not getting paid. To think that music's commodification has resulted in artists altering their creative works to play into the hands of these platforms and their standards is deeply disheartening, especially as an avid music fan. It seems that the only player with the power to make a significant change is, of course, the majors.

The Majors' Response

Despite backlash, Spotify has recently come up with a new attempt to undermine and underpay their artists. They claim that, upon artists' requests, they have developed a way for listeners to be more connected with artists [1]. What this really entails is a royalty cut in exchange for a "visibility boost", where a creator's songs are selected for the platform's radio and autoplay algorithms. In layman's terms, the feature means more exposure at the cost of already-low royalty rates, further taking advantage of the little power artists' have over the distribution of their music. This has evidently caused an uproar in the industry, though it is too soon to see exactly how this will play out.

We can assume that majors have no interest in changing how much revenue they make in favor of their artists, but this then begs the question: why are the labels earning so much in the first place? Their

primary argument for why they deserve a large portion of revenue is because of the expenses that come with digitizing masters, adding metadata to songs (particularly the SKU, aka “shop keeping unit” that acts as a barcode for each master to track who gets paid), storing files, and monitoring sales [9]. This would make sense in the context of physical distribution, as manufacturing, shipping, returns, etc are indeed costly, but given the ease of the internet, this argument is not sound. Labels also tend to ask DSPs for advances in exchange for access to their entire musical catalogue, which is usually millions of dollars. What music lawyers argue is that artists deserve a share of these advances because there would be no deal to begin with without the label’s catalogue of artists. Similarly, labels sometimes buy stock in DSPs as an investment, arguing that they need not share the proceeds because the equity was purchased knowing that it came with the risk of failure [9]. Again, this argument holds no water because without masters and a plethora of artist discographies, there would be no capital to make said investment. Finally, majors claim that distribution and advertising still requires a substantial amount of money. Not only is distribution easier than ever with the advent of the internet and the ease that comes with uploading content, but advertising is a baseless excuse. Most, if not all, streaming services have deals with music intelligence platforms aimed at creating user “taste profiles” [2]. They track everything from the amount of times a user listens to a song, to what playlists they follow, how many minutes they stream, who their favorite artists are, and more. You have probably been presented this data in the form of the annual “Spotify Wrapped”. This service virtually eliminates the need for majors to advertise, as the streaming services handle the promotion of music through their algorithm and radio autoplay features.

We can draw parallels between how the majors have weaseled their way to the top of the food chain in both the old and new music economies. Much like how record companies either acted as or owned the major distribution channels that took care of physical sales in the last century, it has come to light that major labels have invested millions into streaming services in exchange for equity, which can be traced all the way back to 2009 [9]. At the time, the big 3, EMI records (the UK label that would be in that group if it were the big 4), and Merlin (a digital rights agency of independent labels) were all given a total sum of

18% stake in Spotify [5]. This not only means that they knew they would profit significantly as streaming services rose in popularity, but this also gave them undeniable bargaining power, both in the payout agreements made with Spotify as well as the general distribution of their artists' catalogues. In short, having all the largest record conglomerates as stakeholders meant Spotify had a vested interest in keeping the labels happy. Though all labels have gradually sold most of their stakes over the past decade, their total equity is still valued at \$2.5 billion dollars [5]. Another ploy used in both music economies was artist payment rates. "When downloads came along, companies did everything they could to treat downloads as sales instead of licenses so they could pay artist's royalty (10-20%) instead of 50%" [9]. For context, before digital rights, record deals stated that artists would receive 50% of all income from licensing masters. When downloads came about, artists argued that they were not sales, but licenses, which was eventually proven to be true in court (this has to do with the mechanical and public performance licenses mentioned earlier).

The Future of the Industry

COVID-19 has been exceptionally hard on the music industry. Paid subscription to music and entertainment services has increased by 24%, and music streaming revenues are up 12% overall [4]. My hope is that we use this time to find solutions for the pay discrepancy faced by artists and creatives today. In 2016, recorded music made up only 16% of total revenue for artists, while touring accounted for 80% [8]. We can assume that those numbers have continued to change over the last four years. Now that the pandemic has halted all live performances, and streaming is projected to continue its exponential growth over the next decade, we need to address and restructure the industry in a way that can be profitable for more than just the major labels who have dominated it for the past century. If it were up to me, I would negotiate better royalty rates for artists vis a vis streaming services *and* their labels, bringing up the minimum rate from 10% to at least 30% (this is realistic given that hugely popular artists are sometimes able to negotiate a 50% rate). I would create more ways for artists to monetize their music and presence on DSPs, perhaps through subscriptions to internal services such as live (virtual) performances, master

classes, or exclusive access to content. In an ideal world, I would have the financial, human, and social capital to completely reform the industry from a label-driven market based model to one that is centered on the artist, songwriters, producers, and engineers that produce the music we know and love today. Right now I can only hope that with the next generation of executives and industry moguls will come a brighter future for the artists who have molded me into the fervent music listener and maker that I have become.

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