Challenges in the music business

The music business seems to be under heavy pressure. The Recording Industry Association of America (RIAA, 2003) reported a decline of CD shipments of almost 9% in 2002, while unit shipments of all music formats (including DVDs) dropped 11%. Rising consumer prices to keep the revenues constant is risky, because the price elasticity is increasing with the high diffusion of free, but illegal file sharing alternatives such as KaZaA (Gosain/Lee, 2001).

The RIAA has identified two main reasons for decreasing music sales. The first is the recession: the global economic downturn has reduced demand for all goods – including music and other entertainment products. The second reason which has been highlighted as the major cause of the decline is physical and online piracy of music. Since modern PCs are usually equipped with CD burners, every month millions of CDs are being copied without loss of quality, labeled with printed covers downloaded from sites like darktown.com, and distributed illegally (GFK, 2003; Durlacher, 2001). However, not only physical piracy of digital master copies (CDs or DVDs) leads to significantly less demand for CDs, peer-to-peer (p2p) networks enable users to search for and download media files from other user’s PCs (Lechner/Hummel, 2002; Schoder/Fischbach, 2003; Kwok/Lang/Tam, 2002). The popularity of networks like KaZaA, Gnutella or iMesh has not been stopped since the pioneer Napster was closed down (Becker/Clement, 2003; Clement, 2003).

With the rise of online and offline piracy, the focus of industry executives shifted mainly towards strategies defending their terrain. The RIAA is staffing up their Anti-Piracy Unit to work with law enforcement agencies and prosecutors’ offices to encourage en-


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Abstract

The music business is facing hard times with declining CD sales and increasing piracy. Whereas the economic downturn is one reason for lower sales, the industry has decided to target the second factor: the fast diffusion of technologies such as CD burners and peer-to-peer networks like KaZaA allowing massive illegal distribution of music. Some labels focused on an offensive strategy to promote their artists. New services are being added to so called Enhanced CDs that create a new user experience. These CDs offer bonus content (i.e. videos, additional songs, pictures, or lyrics) stored directly on the CD that can be accessed on the PC. Other CDs offer (additionally) online access to actual bonus content or services (i.e. tour dates or news) if the CD is entered in the PC. The impact of these services on consumer experience has not yet been researched in depth and it remains unclear if consumers actually use the offered services on Enhanced CDs.

The music label Arista has introduced several new albums on Enhanced CDs to the market providing more value to the user instead of reducing the utility by focusing only on copy protection. This article analyzes the usage of such services provided by Arista and focuses on Santana’s new album “Shaman”. Using a unique data set provided by Javakitty Media (Bandlink) and Arista, we show for the first time what services are actually used by Santana fans and compare the results to albums of other artists such as TLC or Toni Braxton. Our results indicate that Enhanced CDs are used frequently by a relatively small group of fans, providing more value to the customer and creating a stronger relation between fans and artists.

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forcement of existing laws and modifications to existing laws to keep up with rapidly changing and often open source technologies (RIAA, 2003). Some music labels implemented restrictive copy protection or digital rights management technologies to address rising levels of piracy. These technologies sometimes lead to annoying consumer experiences (see the comments on cd-register.de), because the implemented mechanisms reduce the legal usability of the content (Harmon, 2002; Burke, 2002; WSJE, 2002). For example, if a user buys the new De Phazz album “Daily Lama” he is not able to make a copy for personal use of the CD without (illegally) using special software that ignores copy protection. Additionally, the user can not play the CD on the PC using the standard Microsoft Media Player. The De Phazz album has a proprietary player on the CD which starts if the CD is entered in the PC and allows the user to only listen to the music at a low 80 kbps rate quality (universalkopierschutz.de). Although the label reduced the utility of the CD to the legal consumer, the album is priced normally in the market. This defensive strategy could also damage the artist’s identity and image in the long run, causing decreases in loyalty and size of fan base – the record company’s most valuable assets (Hamlen, 1991).

Legal online services from MusicNet, Pressplay or the German site, popfile.de, are growing, but they are still only offering a fraction of the available content. New songs and those in strong demand are sparse and, therefore, it is no surprise that these legal services have not been successful yet. But even if a user finds the required content on one of these services – the experience is not as good as expected for the price the user has to pay for the service (Harmon, 2002). The digital rights management does not usually allow burning on CDs, the standard media player can not be used to play the file and so on. Nevertheless, there seems to be one exception in the market: Apple’s iTunes service is currently breaking all records with selling music online, allowing the user to burn the tracks on CD.

During the last years, music labels have carefully and without any public visibility tested new business strategies, including innovative approaches such as online music services, ring tones, and new physical formats to meet consumer demand for easy and fun access to music (Krasilovsky/Shemel, 2000). The overall picture shows that the interest in music is still high – besides the high and mostly illegal p2p consumption there are increasing revenues for i.e. DVD-Audio (GFK, 2003). MTV is successfully expanding its music channel network internationally, and global music TV franchises like “Pop Idol” (i.e. “American Idol” or “Deutschland sucht den Superstar”) are global pop phenomena that have a strong content and marketing approach across all platforms and with multiple revenue streams.

Nevertheless, an important question remains for the music industry (besides questions how to restructure the music value chain) on the record distribution side: How to increase the desirability of the CD in order to compete with pure digital distribution channels? It still remains unclear what the critical “involvement” factors are that make consumers buy CDs instead of just listening to the artist on the radio or MTV or downloading the track.

Whereas other industries focused on the web in order to achieve substantial strategic advantages by offering more services (Lederer/Mirchandani/Sims, 2001; Srinivasan/Lilien/Rangaswamy, 2002), only few labels offensively promoted their artists online (May/Singer, 2001; Moon, 2002). New services related to the album or artists are being added to so called Enhanced CDs. These CDs offer bonus content (i.e. videos, additional songs, pictures, or lyrics) stored directly on the CD that can be accessed on the PC. The necessary software to play the videos or to watch the pictures is also stored on the CD. Other CDs offer (additionally) online access to actual bonus content or services (i.e. tour dates or news) if the CD is entered in the PC. In addition, some Enhanced CDs have a higher quality packaging to increase the value perception by fans and other consumers that drive these customers into record stores.

The impact of these services on the consumer experience has not been researched in depth and it remains unclear if consumers actually use the offered services on the Enhanced CD. Academic research has mainly focused on the forecast of music sales, i.e. based on prelaunch sales (Lee/Boatwright/Kamakura, 2003; Moe/Fader, 2002; Fader/Hardie, 2001), or on lifecycle modeling (Bradlow/Fader, 2001; Moe/Fader, 2001) ignoring the new services on Enhanced CDs and their possible impact on selling music. Other studies focused on motives for downloading music (Becker/Clement, 2003; Walsh/Frenzen/Wiedmann, 2002), but they also ignore the impact of Enhanced CDs on music sales and analyze only on online issues.

The music label Arista has introduced several new albums on Enhanced CDs to the market that follow the offensive strategy of giving the user more value instead of reducing the utility by focusing only on copy protection. This article analyzes the usage of such services provided by Arista and focuses on Santana’s new album “Shaman”, which offers (additionally) online access to actual bonus content or services (i.e. tour dates or news) if the CD is entered in the PC. In addition, some Enhanced CDs have a higher quality packaging to increase the value perception by fans and other consumers that drive these customers into record stores.
Adding value to CDs as a new strategy

Instead of unsuccessfully protecting the content with copy protection (Clement, 2003), some labels use service enhancements. Universal, for example, provided the first two million pressed CDs of its superstar Eminem with a bonus DVD. Some labels also produce CDs with access codes allowing users to enter the online VIP lounge of their stars. If cleverly managed, these codes can create a buzz around an album: The cross-over rockers of “Sum 41” or the French artists “Daft Punk” successfully used secret codes on their CDs that allowed users to enter VIP content online. Santana’s label Arista added a small sticker on the cover of the new album “Shaman” motivating Santana fans to enter the disk into the CD ROM in order to access the additional online services added on the CD (figure 1).

The CD includes software (i.e. a browser to display offline and online web pages, chat software, a video and music player etc.) to access interactive services provided by Bandlink.com. With a few clicks a user can install the software once the CD is entered in the PC and is guided to the homepage of the service which is displayed in the integrated web browser (figure 2).

Javakitty Media’s Bandlink software provides a player that allows the user to play the CD on their PC. Other players such as Microsoft’s Media Player are supported as well. Using Bandlink’s browser, the user has access to a wide selection of services such as song lyrics, videos, reports, photos, tour dates, fan articles, mailing lists etc. (figure 3).

In addition to the bonus content on Santana, a user can chat with other users of Bandlink (figure 4). As a unique feature, this CD enables users to connect to chat servers and interact with other Santana fans (or with band members etc.). The software displays what
song the chat partner is currently listening to while chatting.

Santana is a good example how music labels try to establish a new service concept. Instead of limiting the traditional usage of CDs, a new user experience is provided. Nevertheless, a user can download all Santana songs on KaZaA—even the bonus content is pirated and available. A burned copy of Santana’s CD also allows the access to the bonus content on Bandlink. The current encryption technology (usually Key2Audio or Cactus Data Shield 200) does not enable the services offered on Enhanced CDs to be encrypted. Therefore, Enhanced CDs offering more than additional music tracks are not copy protected. New technologies are in development addressing this issue, allowing copy protection to be used to limit the use of bonus content to legal versions (Hansen, 2003).

Although piracy is possible, the bundle of the songs with the Bandlink service included on the CD is an innovation that offers CD-owners a higher utility to pirated MP3 files. Services such as Bandlink can be used by other artists as well and labels can use this software as a customer retention tool. The offered services are designed to secure a long-term relationship with the Santana fan base. The labels trust in a close relationship, because they hope that real fans will prefer the original CD to an illegal copy or ripped MP3 file. Especially if specific elements of the offered bonus content are copy protected, Enhanced CDs may serve as a stronger segmentation instrument between fans that want the original and pirates. The labels also believe that true fans have a higher willingness to pay for specific services, or that through the Bandlink service new distribution channels are established (Amit/Zott, 2001; Geyskens/Gielens/Dekimpe, 2002; Webb, 2002).

Jordan Katz (Senior Vice President for US Sales at Arista) states in an interview given to the Los Angeles Times (11/17/2002) that in the short term few new customers are gained. But in the long term he believes, the existing fan base is secured. The identity and image building process of an artist can be suc-
Successfully managed by the label and fans have a closer relationship to their star, which increases their loyalty and turns them into communication agents within their social system. This kind of marketing can initiate substantial word-of-mouth effects (Goldenberg/Libai/Muller, 2001; Vogel, 2001; Rogers, 1995). The new services allow labels to interact with their fan base directly. Arista itself does not believe it will gain more customers on the short or mid run and, therefore, only promoted the Bandlink service on the CD itself and with a few point of presence events. The label sees the advantage of these services mainly in long term aspects, assuming a broader diffusion of the services in the market:

- Building a fan database.
- Direct interaction with fans (i.e. for promotions of new releases or cross selling).
- Market research and A&R decision tool. The Artists & Repertoire (A&R) departments control the artist development process and find the ‘right’ artists, songs and producers and define the artist identity and image objectives. A&R is the ‘heart’ of the music business and monitoring the listening behaviour supports the decision process to release new singles from an existing album.

- Identification of new trends in music or managing image aspects of a star by entering the chats. Negative image aspects (i.e. fans gaining the impression that an artist is not performing live in concerts) can be early identified in the chats and dealt with proactively (if necessary even with public relations efforts).
- Use the new channel for additional revenue sources (i.e. merchandising or ticket sales).

Bandlink users show a certain level of emotional involvement with the star. This involvement can be leveraged to manage actively the fan-artist relationship and monetize on the fan community buying behavior, if the utility of the services is sufficient for the users. This aspect is analyzed in the next section, where the usage of the services provided to Santana fans is presented and compared to other artists.

**Investigation of success**

We base our analysis of the success of Enhanced CDs on unique data provided by Arista and JavaKitty Media (Bandlink). The analysis covers six albums that have been released with the Bandlink service included on the CD: Santana (Shaman), TLC (3D), Toni Braxton (More than a woman), Gob (F.U. EP), Pacifer (Pacifer), and finally Adema (Adema). The three top sellers were Santana, Toni Braxton and TLC. Contrary to many other labels, Arista chose top selling stars to test the new service. Figure 5 indicates the US-sales of the three major stars albums from their release until March 2003.

Usually about 40% of the records are sold in the US, which allows us to estimate that in the first months of release (until March 2003) Santana sold about 4.5m, TLC about 1.5m, and Toni Braxton about 920,000 albums worldwide. Three years after Santana’s album “Supernatural” was sold to more than 11m fans and won nine Grammies another big selling hit was created with...
Considering the fact that the market has been heavily declining (RIAA, 2003) and “Shaman” was released with less hits than “Supernatural” the sales are satisfying. Also Toni Braxton and TLC did well selling their albums, taking into account that the Toni Braxton album did not include a hit. Bandlink was included on all CDs with some exceptions in regional markets. Note that legally and illegally copied CDs also allow the use of the service. Therefore, we can not conclude that only legally bought versions of the CDs have been entered in the PC.

Arista executives stated in an interview given to us that the usage of Bandlink depends heavily on the target group of the artist. According to Diane Weiner (VP Marketing at Arista) the artist Santana is targeted to a broader and slightly older audience. After his multi platinum success with “Supernatural” his audience starts with 24 and includes the 50+ audience as well. With Toni Braxton and TLC Arista is addressing a core audience of 18-35. The image of TLC is more cutting-edge and more “urban” oriented than the image of Toni Braxton and Santana, which is reflected in a different marketing approach by Arista. For TLC communication tools such as music video or street promotion are important to create a “buzz”. For Santana and Toni Braxton radio airplay becomes more important to reach a broader audience. In order to create awareness for Santana’s new album, Arista ran a national TV campaign that covered all major TV stations.

Bandlink was used more often if the fan base was young. Table 1 indicates this especially for TLC in comparison to Santana. The higher rate of using Bandlink can also be explained if one hypothesizes that younger persons copy more CDs, which Bandlink did technically not account for. The usage data of Bandlink indicates that a relatively small group of CD owners actually installed Bandlink and used the service (assuming that no pirated versions are entered in the PC). Of Santana’s 4,5m buyers, only about 90.000 (2 %) were converted to Bandlink users. Toni Braxton converted about 1,5 % and TLC 3 %. These numbers may have been higher if the service was promoted more heavily. Some users just accidentally found the service by entering the CD in the PC. The higher conversion rate for TLC is according to Arista related to the younger urban target audience that might have a higher affinity to technology and the internet.

### Table 1: Bandlink usage

<table>
<thead>
<tr>
<th>CD track</th>
<th>Total</th>
<th>Total page</th>
<th>Average page</th>
</tr>
</thead>
<tbody>
<tr>
<td>plays</td>
<td>users</td>
<td>views</td>
<td>views per</td>
</tr>
<tr>
<td>Santana</td>
<td>2.151.903</td>
<td>89.755</td>
<td>305.136</td>
</tr>
<tr>
<td>Toni Braxton</td>
<td>348.294</td>
<td>9.868</td>
<td>33.780</td>
</tr>
<tr>
<td>TLC</td>
<td>556.653</td>
<td>29.456</td>
<td>136.983</td>
</tr>
<tr>
<td>Gob</td>
<td>13.104</td>
<td>1.409</td>
<td>5.660</td>
</tr>
<tr>
<td>Pacifier</td>
<td>1.086</td>
<td>164</td>
<td>621</td>
</tr>
<tr>
<td>Adema</td>
<td>37.453</td>
<td>4.752</td>
<td>19.517</td>
</tr>
</tbody>
</table>

Source: Bandlink

### Table 2: Service usage

<table>
<thead>
<tr>
<th>Interest of Users in %</th>
<th>Home</th>
<th>Bio</th>
<th>Bonus Content</th>
<th>Discography</th>
<th>Mailing List</th>
<th>News</th>
<th>Photos</th>
<th>Tour</th>
</tr>
</thead>
<tbody>
<tr>
<td>Santana</td>
<td>74.38</td>
<td>1.76</td>
<td>7.22</td>
<td>6.41</td>
<td>1.37</td>
<td>1.75</td>
<td>5.09</td>
<td>2.01</td>
</tr>
<tr>
<td>Toni Braxton</td>
<td>65.08</td>
<td>4.52</td>
<td>9.13</td>
<td>–</td>
<td>2.60</td>
<td>3.80</td>
<td>9.38</td>
<td>5.49</td>
</tr>
<tr>
<td>TLC</td>
<td>57.19</td>
<td>3.54</td>
<td>13.21</td>
<td>7.49</td>
<td>2.68</td>
<td>4.02</td>
<td>8.13</td>
<td>3.75</td>
</tr>
<tr>
<td>Gob</td>
<td>55.58</td>
<td>4.66</td>
<td>20.14</td>
<td>0.11</td>
<td>3.11</td>
<td>3.80</td>
<td>7.72</td>
<td>4.88</td>
</tr>
<tr>
<td>Pacifier</td>
<td>55.39</td>
<td>6.44</td>
<td>13.37</td>
<td>–</td>
<td>4.51</td>
<td>5.31</td>
<td>7.41</td>
<td>7.75</td>
</tr>
<tr>
<td>Adema</td>
<td>52.97</td>
<td>4.20</td>
<td>24.27</td>
<td>–</td>
<td>2.46</td>
<td>4.05</td>
<td>7.08</td>
<td>4.97</td>
</tr>
</tbody>
</table>

Source: Bandlink
Nevertheless, it is wrong to conclude that the Bandlink service was of very limited interest. The usage of the service by fans of development bands, and therefore less known, like Gob, Pacifer and Adema was much more highly related to their sales and chart rankings.

Table 1 also shows the usage of the different services. The 90.000 Santana fans played more than 2,1m songs with the Bandlink player and clicked on more than 300.000 pages displayed in the various sections of the service. We are technically not able to provide numbers about the chat service which was included, but the data of the usage of the other services is displayed in table 2 and figure 6.

The structure of the services and their quality is comparable between all the artists. Once the user enters the service, he is linked to the homepage of the Bandlink service which displays information about the music tracks (lyrics, credits). The player can be directly accessed on the homepage. Therefore, if users just want to listen to the tracks, they enter the service by the homepage which explains the high mean of 60,1%. Between 4 and 5% of the average usage is focused on the biography, discography, and tour data. Of less interest are news and the mailing list. These numbers are as expected, because of the static nature of these services: Once a user has read the biography he is not likely to return many times. Nevertheless, the sparse use of the news section is surprising. One possible reason for the low usage is the low frequency of updates in this section (especially for Santana). The offered bonus content (exclusive music, videos and studio footage) has been used more frequently, varying between the artists (table 2). More than 14,5% of the usage is addressed towards this additional content. Whereas Santana users did not use the offered bonus content so much, the younger fan base of TLC or Pacifer and especially fans of Gob and Adema entered this service section much more. The analysis of the distribution of the usage of Bandlink’s services indicates that bonus content seems to be a service of interest, whereas the other services are of less interest.

### Management implications

The usage of the interactive enhancements provided to music fans on CDs from Arista has been moderate, because the Bandlink services have not been aggressively marketed. Also the content on the service (i.e. news) was not frequently updated. Additionally, the installation and user registration procedure might have had a negative influence on the adoption of the service. Nevertheless, if a fan decides to use the service he spends considerable time with it, playing songs from the CD and enjoying the offered bonus content. The interactive features deliver a rich data set to the label and chat services can be a valuable platform to interact between artists and fans. Fans provide Bandlink with additional demographic information that can be used to target users with services and products. The labels and also the artists have the opportunity of getting closer to their customers and fans – if they respect privacy (McKnight/Choudhury/Kacmar, 2002).

Using Bandlink or other related services, labels are providing additional services and value to the loyal fan and legal customer. The technology will allow future encryption of bonus content (which has already been implemented by Bandlink’s competitor Arcavista.com). This would enable the labels to offer bonus content only to legitimate users. But, at the same time, diffusion of the service will need longer to create critical mass. The software provider aims to penetrate its player in the market and the Record Label may want to attract even illegitimate users in order to keep a consequent proactive strategy of offering value added services and gathering usage data. Enhanced CDs will not be the ultimate instrument to fight piracy, but it might be an interesting tool to secure customer and fan loyalty in the long run. The offensive strategy without copy protection including more services has been chosen by Arista, but critics may ask, if the strategy has been successful to reduce the challenges of the music industry.

First, the illegal use of the CD is not limited and the fact that Bandlink’s bundled services are not available to users that downloaded files from peer-
to-peer networks will not lead to high frustration levels of pirates. The Bandlink software as well as the ripped bonus content is available in peer-to-peer networks and if Santana fans use the chat more than once or twice remains an open issue. Nevertheless, the CDs have been successfully sold in the market, although there are no indications that more users bought the CD because of enriched services. Arista stated that especially Santana fans are generally older, more loyal, and settled which indicates a higher willingness to pay for content. This makes them to highly valued customers – even if they did not use the service so much. Therefore, labels must monitor the profitability and long term effects of Enhanced CDs carefully.

Second, Bandlink offers opportunities for record labels if the value added services are of high quality. Additional revenues (i.e. via transaction fees) can be generated with merchandising, sponsoring, advertising etc. that can be used to subsidize the CD price, if the music label controls the key elements of the value chain and is able to exploit the merchandise or endorsement rights. Therefore, it is necessary for Bandlink to reach critical mass within the music community. But, the fact that the software had to be installed first in order to use the services shows that network externalities are in place. The more users have installed Bandlink on their PC the more users are able to use the services. If reaching critical mass is important, then piracy might even support this software diffusion process (Givon/Mahajan/Muller, 1995). If the installed base of the software is already high then copy protected bonus content may be offered widely. This strategy is followed for example by Arcavista.com.

Third, the Bandlink online community serves as a cheap market research tool, e.g. replacing focus group testing or other traditional methods that might be used alternatively. The likelihood of success for a single release or other versioning of the artist’s music can be higher. Santana has been a good example that an offensive strategy can lead to success, even within “Generation Napster”. The sales have been high and loyal customers are rewarded with an additional service bundle provided on the CD. Further research needs to be conducted on the individual level. Especially empirical studies analyzing the effect of services such as Bandlink on consumer’s willingness to pay will help to understand the value of these services to customers in more detail. Our analysis showed that some services, especially the bonus content, are frequently used. Comparing Enhanced CDs to movie DVDs may be fruitful in order to price discriminate. If users have a higher willingness to pay for Enhanced CDs, labels could introduce a higher priced Enhanced CD simultaneously to a normal audio CD without special content in order to target the different segments.

Finally, the music industry should experiment more with services that add value to legal content which is bundled to specific target groups instead of reducing the usability of CDs by using copy protection. This proactive strategy helps differentiating between “high involved” fans and “low involved” other consumers, because real fans get more value if they buy the CD. Therefore, Enhanced CDs can be used as a customer retention tool with positive involvement impact. They also support a positive relation to the artist – which is a very important issue, because pirates generally do not want to hurt the artist, but they have considerably fewer problems to cheat on labels (GFK, 2003).

References


