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**As the music industry dust unsettles...**

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At the time that this is being written, the Wall Street Journal had just declared that “in a dramatic acceleration of the seven-year sales decline that has battered the music industry, compact-disc sales for the first three months of this year plunged 20% from a year earlier.” Such news coming on the heels of what had been other major industry developments – the substantially increased royalty rates for Internet radio operators, the announced but uncertain merger of XM and Sirius Satellite Radio, and the lack of finality to the Clear Channel going-private deal – leads us to wonder if and how any of these events relate to each other and, more importantly, to the industry taken as a whole. Here are a few recurring themes and some initial thoughts:

Does the music industry need services such as Internet radio to help reverse its slide?

Abundant supply. According to executives interviewed for the referenced article “CDs have become little more than advertisements for more lucrative goods like concert tickets and T-shirts.” One wonders if the millions of songs performed by almost as many artists and produced by thousands of labels, distributed digitally or otherwise over almost as many outlets, contributes to an environment in which – not only very few profit, but what’s worse – brand values are diluted to a degree that even in the aggregate industry economics suffer. “This year has already seen the two lowest-selling No.1 albums since Nielsen SoundScan, which tracks music sales, was launched in 1991,” according to the same article.

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Imprecise value proposition. As the Internet radio industry prepares its case against the per-play royalty structure recently implemented by the Copyright Royalty Board, which according to many observers could shut down Internet radio as we know it, it is likely that the promotional benefits of this medium to the recorded music industry will feature prominently. It will be interesting to see which side of the double-edged argument eventually takes hold: Does the music industry need services such as Internet radio to help reverse its substantial slide? Or do highly customizable (and free of charge) services like Pandora take away from the music industry’s revenue opportunity? While sound business practice would probably not favor near-term revenue relief at the expense of shutting down a major long-term PR machine, the precise tradeoff may be difficult to quantify. The relative proportion of Internet radio outlets that indeed enhance music purchases (and the degree of their effectiveness) may be an imprecise estimate, while, unfortunately, the significant drop in music purchases (that maybe just by coincidence matches the advent of alternative delivery mechanisms such as Internet radio), is well documented. In either case, however, the decision is not so much binary as one of establishing an appropriate royalty rate to reflect a balanced assessment of all factors. It will also be interesting to observe the precedent-setting quality (if any) of this decision upon other audio media (e.g., satellite and for that matter even terrestrial radio).



The current state of the music industry may be a case study to test the scenario in which excessive competition can potentially be unhealthy.

Unsettled competition. The fate of Internet radio cannot be lost upon the factions currently proposing, opposing, or assessing the soundness of the XM/Sirius combination. The companies have often cited the emergence of digital music distribution (via wireless broadband connections to handheld devices) as a defensive motive behind the proposed transaction, and Internet radio is undoubtedly a big part of this threat. With wireless broadband access to laptops and now also cell phones, listening to one's favorite Internet radio station "on the go" is a reality. Should this threat become lessened by copyright developments described above, the argument used by XM and Sirius could be weakened. And as the two companies apart would constitute a less formidable competitor than together, (while Internet radio is also set back in this hypothetical scenario), one cannot help but wonder about the traditional radio community and its role in these events, watching the urgency of the extensively planned, expensive, and complicated HD rollout (forced upon these operators by excessive competition) diminish by the day.

Variety of unknowns. And speaking of traditional radio...the postponed shareholder vote of Clear Channel's pending buyout may be a sign of many things, none of which seem to be that the deal as proposed is ready to happen soon. Perhaps the extra time will allow for a new deal to emerge and for further negotiations to happen, but perhaps as importantly, the extra time will offer greater clarity on the competitive environment and the fates of its varied participants. One has to assume that the radio operator's competitive analysis, as well as the impact thereof on growth projections in support of valuation, are likely incomplete and even bordering on speculative in the present dynamic. One may also wonder to what extent Clear Channel's announced strategy to streamline its portfolio of properties, focusing on major markets, would also be impacted by the competitive unknowns yet to be settled.

In the depicted situations one senses a recurring motif, a sort of underlying tension, between highly fragmented competition on one hand and, on the other, sweeping consolidation, simplification, and industry organization. Whether it is the proposed satellite radio merger, the repositioning of pieces within the traditional radio landscape, or the prohibitive Internet radio royalties that threaten to shake up an entire segment, there does seem to be a push towards diminished numbers and an easier to navigate business climate. This push is naturally countered by competitive interests, and it remains to be seen which of the two forces will prevail. With the conventional wisdom being that more competition is better than less, the current state of the music industry may be a noteworthy case study to test the extreme scenario, in which excessive competition can potentially be unhealthy. After the dust does settle, though we may even see a further increase in the number of consumer alternatives, we would not be surprised to see a significantly smaller



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number of competitors in the market... much like the way it used to be, you know, way back in the day, like, four or five years ago.

By Dan Ramsden  
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