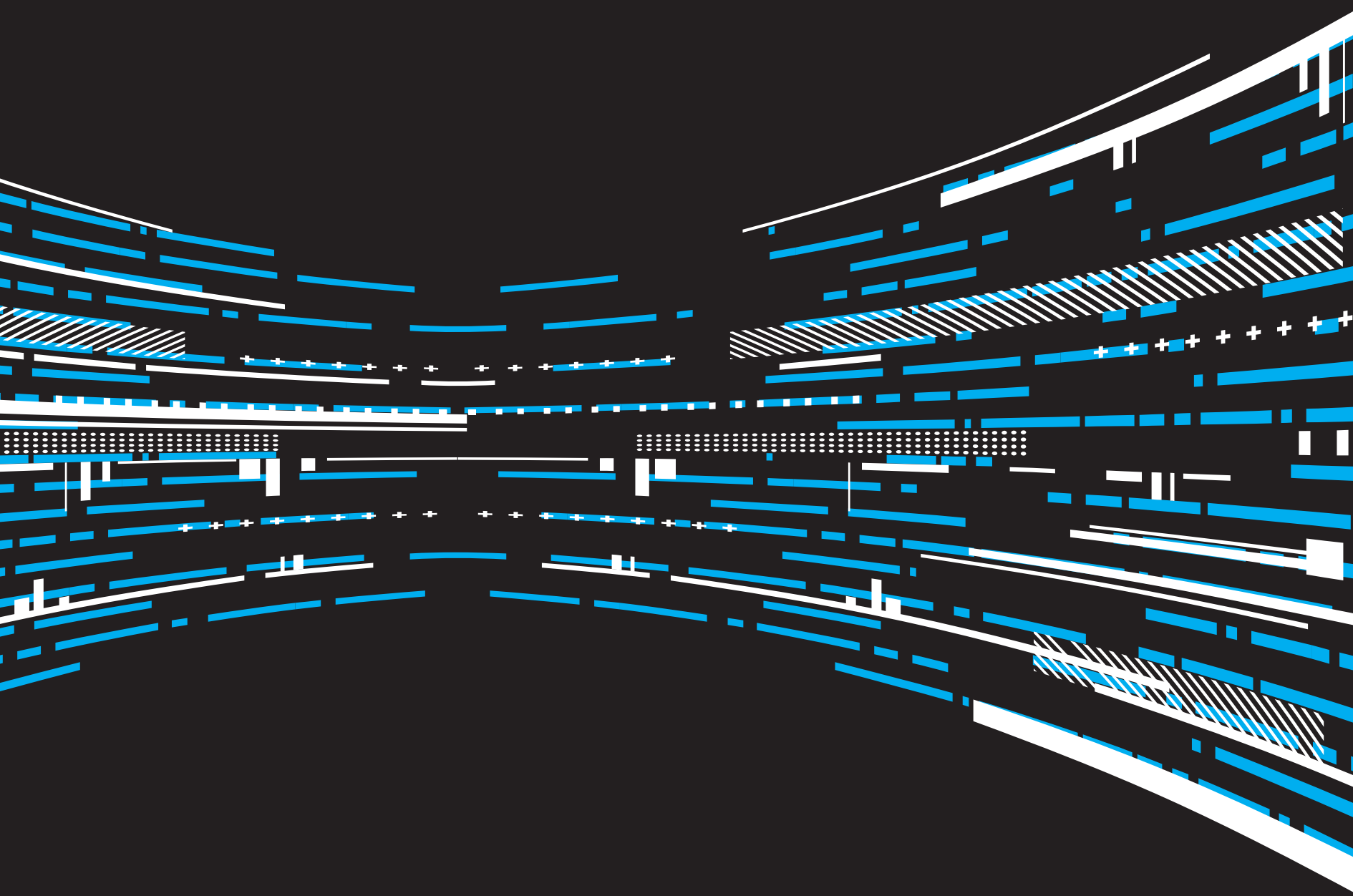
IFPI Digital Music Report 2008



Revolution
Innovation
Responsibility

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Introduction:
Making ISP Responsibility a Reality in 2008

In 2007 ISP responsibility started to become an accepted principle In 2008 it must become a reality

By John Kennedy, Chairman and CEO

An incredible revolution is sweeping the music industry and in the pages of this report you will read how record companies are adapting their business to the dramatic changes brought about by the digital age. In the US, only five years after the commercial music download business first emerged, 30 per cent of all recorded music sold is online or mobile. Record labels are becoming broad-based entertainment companies, developing new revenue streams. The consumer has better choice, availability and flexibility in enjoying music than ever before.

Our digital revenues are growing and diversifying as our business model changes from one dominant format to hundreds of channels and products.

Yet behind the innovation, experimentation and diversification of the digital music market in 2007, another change has happened – of possibly even greater importance to the long term future of our business. The last year has finally seen the wind of change blowing through old assumptions about the role internet service providers (ISPs) should play in protecting copyrighted content. ISP responsibility is becoming an accepted idea.

This is a critical development, because until now ISPs have played no such role. Copyright theft has been allowed to run rampant on their networks under the guise of technological advancement. Some estimates say no less than 80 per cent of all internet traffic comprises copyright-infringing files on peer-to-peer (P2P) networks. ISPs have largely stood by, allowing a massive devaluation of copyrighted music. This in turn – and despite all the positives about our digital growth – has prompted a crisis in recorded music that has wide implications for the whole digital market place and all those businesses to whom music is an important ingredient.

Today, however, a sea-change is happening. The whole music sector, governments and even some ISPs themselves are beginning to accept that the carriers of digital content must play a responsible role in curbing the systemic piracy that is threatening the future of all digital commerce. After years of discussing and debating, I am convinced it is no longer a question of whether the ISPs act – the question is when and how.

More than anyone else in 2007, our industry has to thank French President Nicolas Sarkozy and the Chairman of FNAC Denis Olivennes for the change of mood. The Sarkozy Agreement, announced in November, is the most significant milestone yet in the task of curbing piracy on the internet. It sets up a groundbreaking three-way partnership between the creative sector, ISPs and government. It takes the protection of intellectual property online into new territory, requiring ISPs to disconnect copyright infringers on a large-scale, using an automated system and to test filtering technologies.

Not every detail of the French plan will be exportable to other countries but the overriding principle behind the plan – the fundamental role that ISPs play in stopping piracy – sets an exciting example internationally. President Sarkozy summed it up: the internet must not be allowed to become a Wild West; it must be a medium where we protect our culture.

There has been progress elsewhere too. An extremely important court decision came in the form of the Sabam-Tiscali judgment in Belgium in June. The court not only confirmed that the ISP must take responsibility for curbing infringement on its networks – it referred to no fewer than six possible technological solutions for blocking the traffic of unlicensed music.

Similar movements have happened in different parts of the world: new legislation engaging ISPs in Taiwan and Korea; a hard-hitting message from the Swedish government's Renfors Report; and intensifying intra-industry discussions in other countries. In the UK, with talks proceeding against the ticking clock of the government-commissioned Gowers Review, ISPs need to prove that they can deliver action that will have a real impact on piracy. In the US, AT&T has shown cautious leadership, acknowledging ISPs' responsibility to protect content and working on filtering technologies with the music and film industries.

Of course, one key reason for this apparent sea-change is the commercial self-interest of ISPs. Unlicensed traffic has always been hogging their bandwidth, but now, as ISPs get further invested into the business of digital content, it poses an increasing danger to their future revenues.

A turning tide of opinion is one thing – a concrete programme of action is another. There is only one acceptable moment for ISPs to start taking responsibility for protecting content – and that moment is now. After years of prevarication in this discussion, the French government's decision to "seize the day" is deeply refreshing. It shows an urgency of approach that is badly needed in every market where music is today being massively devalued by piracy.

In Europe, we look to the European Union to capitalise on the momentum created by the Sarkozy Agreement. The moment for EU legislation to be drawn up has already arrived. There must be obligations on the ISPs to warn, suspend and eventually disconnect infringing users and to apply filtering measures. This should be achieved by agreements, backed by legislation where necessary. At the same time, we as an industry will not be shy to use legal action to force ISPs to act when dialogue fails but I would like to think that they now understand that meaningful voluntary action is a more attractive option than coercion – we have always advocated that!

This report reflects revolution and innovation in the music business. Music is more advanced along the digital road than almost any other content business. As the table on page six reflects, we have transformed our landscape in the last five years. I am hopeful that in 2008 the online subscriptions business, hitherto held back by a range of problems, will finally realise its huge potential as a revenue stream.

Revolution and innovation, however, are not going to be enough to secure a healthy future for the music industry. The third corner of the triangle is responsibility. 2007 was the year ISP responsibility started to become an accepted principle. 2008 must be the year it becomes a reality.

Section 1: Revolution and Innovation – the Digital Market in 2007

US$ 2.9 billion
Estimated record company revenues from digital sales

15%
Estimated digital percentage of the total music market

The digital music sector is advancing by innovation and experimentation

A revolution is happening in the way consumers obtain and pay for music and the music business is transforming itself for a new environment. Like many revolutions, this is a continuous process and there are many divergent views within the industry on where it will end. Today, the digital music sector is characterised by innovation, experimentation and diversity of new business models.

Record labels are proactively reinventing themselves, moving away from a "record-centric" model and diversifying their revenue streams across a much broader range of products and platforms. Digital is no longer a separate entity in the operation of a record company – it is wholly integrated into all the products and services being offered and planned.

A release from an artist today may appear in dozens, sometimes hundreds, of different products. Consumers have more choice than ever as to how they want to connect to and experience the music from their favourite artist – they can buy a download, a CD, wallpaper for their mobile phone, a mastertone, an e-ticket, a music video, become their friend on a social network or sign up to a subscription service. In many cases consumers will choose various products and acquire these on many different platforms.

Key Indicators (2007)

Broadband lines	350 million (up 23% on 2006)[1]
Mobile subscriptions	2.5 billion (up 11% on 2006)[2]
Portable music player sales	140 million (up 15% on 2006)[3]
Legal tracks downloaded	1.7 billion (up 53% on 2006)[4]

1 Source: IFPI, based on Point Topic data
2 Source: PriceWaterhouseCoopers
3 Source: Understanding & Solutions
4 Source: IFPI

Technology has enabled these changes. Growing use of broadband, mobile phones and portable devices has helped the rollout of hundreds of digital music services. These have provided access to vast music catalogues that extend far beyond the reach of traditional retail stores. Portable digital players have enabled an 'always on, anywhere' music environment. Instant access and portability have become the norm.

The consumer is king in the digital world and entertainment spend is shared competitively among a wide range of products and services. Consumers' time is also a valuable asset and industries are vying for their attention.

Music is pioneering the creative industries' advance into the digital world. The task of creating commercial value from content online or through mobile platforms confronts a swathe of creative content industries from newspaper publishing to television and film. However, music's digital market share by revenue is higher than in any other entertainment sector except games.

The advances of technology have brought huge challenges too – the ease of access to music has damaged its perceived financial value to consumers.

There have also been significant brakes on the digital music sector: the lack of interoperability between services and devices due to different providers' digital rights management (DRM) standards; proprietary software tied to particular device brands, regardless of DRM; the lack of investment in marketing to promote new music services; consumer offerings that have not yet fully evolved, particularly in the mobile sector; and piracy.

Widespread copyright theft continues to be the most significant barrier to the development of a legitimate digital music business. The mass availability of unauthorised, unpaid-for music has also caused major damage to CD sales.

Digital piracy is also developing into more varied forms, requiring more sophisticated anti-piracy enforcement strategies and highlighting the critical need for increased cooperation from the internet's gatekeepers, the ISPs. 2007 saw significant progress on both fronts.

The digital music market in 2007 reflected both the progress of the industry and the very significant challenges that remain in creating a commercially successful digital music business. Record companies' digital sales continue to grow strongly, but have not yet offset the sharp decline in CD sales, resulting in a worldwide overall market decline in 2007.

There are exceptions in some countries where digital sales have offset physical decline, led by Japan, the world's second largest music market, and including markets such as India, China, Indonesia and South Korea.

Global Digital Revenues by Industry (2007)

Industry	Digital %
Recorded music	15%
Newspapers	7%*
Films	3%
Books	2%

Source: IFPI, PWC Global Entertainment and Media Outlook.
* US only

Digital Music Sales in 2007

The digital market continues to grow worldwide

Five years after the emergence of a market for legal online music downloads, the digital music business is continuing to see growth internationally.

Record company revenues from digital sales are estimated at approximately US$2.9 billion in 2007 – up roughly 40 per cent from US$2.1 billion in 2006 and up from US$380 million in 2004. The digital share of the total music market has risen from only two per cent in 2004 to around 15 per cent in 2007. In the US, digital sales account for nearly 30 per cent of the music market and in South Korea they account for over 60 per cent of the market. Globally, the digital market is split roughly 50:50 between online and mobile sales.

These figures exclude other digital income streams such as licensing income from advertising-supported models and performance rights income. These areas are growing sources of revenue to record companies.

Top 10 Global Digital Singles 2007

	Artist	Song	Sales (m)
1	Avril Lavigne	Girlfriend	7.3
2	Utada Hikaru	Flavor of Life	7.2
3	Rihanna	Umbrella	6.6
4	T-Pain	Buy U A Drank (Shawty Snappin')	5.9
5	Akon	Don't Matter	5.7
6	Soulja Boy Tell'Em	Crank That	5.2
7	Shop Boyz	Party Like a Rock Star	5.2
8	Sean Kingston	Beautiful Girls	4.8
9	Mims	This is Why I'm Hot	4.8
10	Beyoncé	Irreplaceable	4.6

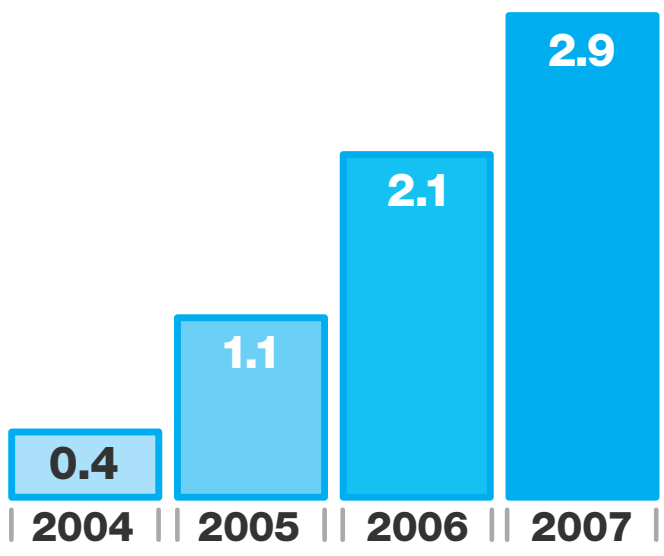
Chart includes: online single track downloads, mastertones, ringback tones, full track downloads to mobile, video mastertones. Period Dec 2006-Nov 2007. Combines all versions of the same song. Sales figures rounded.
Source: IFPI

Reinventing an Industry – The Digital Difference Over 5 Years

	2003	2007	
Number of legal services	Less than 50	Over 500	A legal digital music market has been created from scratch over the last five years, with consumers now able to shop around more than 500 legal services.
Licensed tracks	1 million	6 million +	Consumers can now legally access more than six million tracks through legal services.
Value of digital music sales	Around US$20 million[1]	Around US$2.9 billion	Record labels have created a digital music industry worth approximately US$2.9 billion in just five years, a rate of growth many industries would envy.
Digital as a percentage of overall recorded music sales	0%	15%	Almost a sixth of music sales already come through digital channels just five years after legal options opened up and this figure is set to grow.
Number of formats available per artist release	Less than 10 and dominated by the CD and cassette	Over 100	Today a single artist release can be packaged in multiple formats include video downloads, ringtones or mobile full tracks. Sales of Justin Timberlake's FutureSex/Love Sounds comprised of 115 products which sold a total of 19 million units, of which only 20 per cent were in CD format.

[1]Estimated digital sales, USA, IFPI.

Digital Music Revenues US$ Billions



% of the total industry:

2004: 2%
2005: 5%
2006: 11%
2007: 15%

Source: IFPI. Includes online and mobile sales & record companies' revenues. 2007 figure is an estimate

> "The record business is turning into a true music entertainment business. We are breaking away from the single product format to a vast range of different and complementary products, all centred around the release of an artist."
>
> Thomas Hesse, President, Global Digital Business, SonyBMG Music Entertainment

Online and mobile downloads continue to grow

Online single track downloads are the most popular digital music format on a global scale, accounting for 30 per cent of overall digital revenues. IFPI estimates that 1.7 billion online tracks were downloaded in 2007 globally (including digital albums) – up 53 per cent on the comparable figure in 2006.

Consumers' ability to buy individual tracks rather than whole albums has been one of the defining features of the digital music market, dramatically reviving demand for singles.

Mobile music has enormous growth potential. The most popular mobile music format remains mastertones – short excerpts from an original sound recording that play when a phone rings – but in 2007 there was notable pickup in sales of full track downloads to mobile, with sales accounting for 12 per cent of all digital sales in the first half, compared to 6 per cent in the same period in 2006. This marks an ongoing shift in consumer demand from mobile personalisation features, such as mastertones and images of favourite artists, to 'core' music consumption over the mobile phone.

Mobile music continues to face obstacles however, and in the first half of 2007 grew at a slower rate internationally than online downloads. Limited marketing, prohibitive data charges and a lack of consumer-friendly offerings are partly to blame, as is the low penetration of advanced handsets and 3G, slowing growth in the mastertone sector in some markets.

The potential of mobile was demonstrated by the number of new business models emerging in late 2007 (see page 14).

Digital bundles in demand

Digital consumers want not only single tracks, but bundled content as well. Digital album sales grew by over 40 per cent globally in the first half of 2007 and accounted for 15 per cent of the digital market's value. In the US, digital albums now account for 10 per cent of total album sales and five per cent in the UK.

Exclusivity and added value in the form of bonus material bundled with digital albums are helping drive consumer demand for premium product. Premium albums outsell the basic versions in most cases.

"Whenever we release a premium download as well as a basic album bundle, it's usually the higher value product that sells the most, especially within the first couple of months. The fact that fans choose the expanded version, at an enhanced price point, demonstrates how much they value that additional content and the deeper connection with the artist it offers."

Eric Daugan, Vice President, Digital Business, Warner Music International

Interest in digital album sales was also boosted by the launch of iTunes' 'Complete My Album' feature. It allows consumers to turn their individual tracks into a complete album at a reduced price by giving them a full credit for every track they have already bought from that album.

"The mobile platform is an enormous part of the future of the music business. And I believe that music is crucial to the future of the mobile industry. People want a more interesting form of mobile music content. Any player in the mobile value chain who thinks they can provide less than a great experience for consumers and remain competitive is fooling themselves."

Edgar Bronfman Jr, Chairman, Warner Music Group

The Move to Digital Varies by Region

Mobile and online are split across different markets

The switch to digital music is happening in varied ways and at different speeds across the world. Sales are still concentrated on the top ten markets, which account for 90 per cent of all digital sales.

The United States remains the leader in digital music sales worldwide, with online and mobile accounting for some 30 per cent of the market. It is also the most significant market for subscription services such as Napster and Rhapsody.

Single track downloads in the US totaled 844 million, up 45 per cent on 2006 (Nielsen SoundScan). Digital albums grew faster than singles by 54 per cent to 50 million. Mobile sales also grew strongly with single track downloads to mobile growing more than fourfold between the first half of 2006 and the first half of 2007.

US mobile operators have pursued different music strategies in 2007, broadening the mobile offerings available. AT&T partnered with eMusic and Napster to offer music to its consumers while rivals Sprint and Verizon have built their own music stores. While mastertones still account for the bulk of mobile sales, full track downloads are growing strongly. The launch of the iPhone in June, linked consumers to the iTunes store via their mobile handset, allowing them to choose from a much broader catalogue and purchase seamlessly through mobile billing.

Online, Amazon opened a digital download store selling DRM-free tracks and Microsoft launched a refreshed line of Zune players alongside its online store. There has also been a surge in the popularity of music on social networking sites.

In the UK, 77.6 million tracks were purchased online in 2007, a 47 per cent increase on 2006. Sales during the 2007 Christmas week were double the previous year's sales. More than 90 per cent of all UK single sales are now digital, and more than 200,000 different titles are sold each week. The UK singles market is still driven by hits, but the 'long tail' accounts for most sales volume, with the top 40 accounting for just 10 per cent of all single track download sales in 2007.

The UK has the most advanced mobile music market in Europe, with the greatest penetration of music phones (43% of mobile subscribers) and the highest percentages of consumers using their phones to play music (M:Metrics). The BPI estimates that 10-12 per cent of all chart sales are made through mobile channels in the UK.

New mobile music offerings introduced in the UK in final quarter of 2007 included Omnifone's MusicStation subscription service and Nokia's Music Service. Nokia's service is expected to expand into the rest of Europe, Asia and the US in 2008 and will benefit from Nokia's global brand and its commitment to developing a business that involves music.

> **"Nokia's entry into the music download market is part of a strategic move to develop a strong stand alone services business."**
>
> **Richard Sandford, Regional Manager, Nokia Music UK & Ireland**

The German digital music market grew by an estimated 38 per cent up to the third quarter of 2007 year-on-year (IFPI Germany). Although iTunes is still the market leader in Germany, with an estimated market share of 42 per cent, Musicload is a serious competitor with a market share of around 32 per cent (GfK).

In France digital sales were weak in 2007, accounting for around seven per cent of the market. High levels of unauthorised file sharing have stifled market development. In November, President Sarkozy launched the most significant plan yet for cooperation to curb online piracy, committing ISPs to a system of disconnection of illegal file-sharers on their networks.

South Korea illustrates for some the huge potential of the digital music business, yet it is a market of contradictions. South Korea was the first market where digital overtook physical sales. Over 60 per cent of the South Korean market is now made up by digital sales and this share is advancing rapidly. This is a reflection partly of the devastating impact of piracy on CD sales and partly of a highly wired society with a successful music download and streaming service. Warner Music released Baek Ji Young's album 'Smile Again' late last year and generated over 67 per cent of its revenue through digital sales.

In the rest of Asia, ringback tones continue to dominate the digital music market of many countries, creating a new form of music consumption. Indonesia is the third biggest market in the world for ringback tones, behind the US and Japan.

Top 10 Digital Markets, Sales by Channel

		Online	Mobile
1	USA	67%	33%
2	Japan	9%	91%
3	UK	71%	29%
4	South Korea	63%	37%
5	Germany	69%	31%
6	France	39%	61%
7	Canada	58%	42%
8	Australia	59%	41%
9	China	27%	73%
10	Italy	44%	56%

Source: IFPI, based on first half 2007 industry revenues.

China has enormous growth potential in mobile music, but any serious market growth is currently shackled by a rampant online piracy rate, estimated at more than 99 per cent of the market. China Mobile is reported to be in talks with Apple to bring the iPhone to the country. However, as in many Asian markets, the music industry needs to achieve better rates of return from mobile operators in order to build its digital business. In China where the mobile music sector has been cited as worth around US$700 million annually (In-Stat), record companies are estimated to receive less than five per cent of those revenues.

In Australia, digital revenues continued to post strong gains, increasing from 5.5 per cent of the market at the end of 2006 to almost 10 per cent by the end of the first half of 2007, and digital only tracks are now included in the weekly sales charts.

Latin America saw strong mobile music growth with sales more than tripling in the first half of 2007, while online sales are overshadowed by massive unauthorised distribution. The Brazilian digital music market increased by 168 per cent in the year to October. Sales of pre-loaded content on mobile handsets boosted digital sales in both markets. Current barriers include the low adoption of advanced phones, relatively low 3G penetration and rising mobile piracy. In Brazil, a number of illegal websites distributing mastertones were shut down by IFPI's affiliates in 2007.

> **"Digital technology has shifted power to consumers, and music marketing must evolve from 'push' to 'pull'. Our focus is to embrace this power and become completely consumer focused. By listening to and responding to our consumers and to our artists we aim to unlock the incredible potential for music in the digital environment."**
>
> **Mark Hodgkinson, Executive Vice President of Global Marketing, EMI Music**

"The volumes we are reaching are mirroring the heyday of single CD sales in the late 80s. The singles business is alive and well in Japan."

Rob Wells, Senior Vice President Digital, Universal Music Group International

Section 2:
A New Deal for Consumers

More choice and the spread of portable devices are driving music demand to an all-time high

Digital stores offer consumers a far greater virtual shelf space than the largest traditional brick and mortar stores. This means that a broader range of repertoire, including specialist, vintage or hard-to-find recordings is now available to fans.

Record companies have seized this opportunity, with the classical music sector in particular benefiting from this new channel to reach consumers. In November 2007, Deutsche Grammophon introduced a classical music download service for classical music in 40 countries, the DG Web Shop. The service offers 2,500 DRM-free albums, 600 of which are no longer available in CD format. Consumers can choose between entire albums, collections of albums and box-sets – or individual movements, complete works, and individual pieces.

The same marketing flexibility has revived the availability of archived recordings of renowned classical artists. EMI Classics, which has some 100,000 recordings in its catalogue, joined with iTunes in March 2007 to give consumers access to the entire EMI discography of the iconic cellist Mstislav Rostropovich.

Digital-only releases of classical music are also being pioneered, allowing consumers to buy a new classical album much sooner after its first performance. In November 2007, EMI Classics released Sir Simon Rattle's recording of Mahler's Ninth Symphony with the Berliner Philharmoniker as a digital-only release.

There is evidence that making catalogue work available is appreciated by consumers. Universal's Digital Reissue Programme has to date yielded more than three million total downloads since its launch in January 2006. So far, the label has made 18,000 previously deleted tracks available again to consumers, from artists including Noir Desir, Robert Miles and Nana Mouskouri.

A significant further batch of deleted tracks from Universal Music's catalogue is scheduled to go online during 2008, with numbers rising to 60,000 tracks by the end of the year.

"The music industry is way ahead of other media, broadcast and online companies in getting our content out there – yet ironically we are behind when it comes to getting paid for it."

Simon Gunning, Senior Vice President of Digital, EMI UK and Ireland

"Music on the go"

Portable digital music devices have revolutionised the way consumers listen to music. The explosion in sales of portable music devices continued in 2007 with new players coming on to the market.

Although the iPod is today the leading portable music player, many other brands, from Microsoft's Zune to Nokia's and Sony Ericsson's music phones, are established as well. Nokia sold almost 220 million music-capable mobile phones globally in the first three quarters of 2007 – nearly twice the total number of iPods (120 million) sold up to the third quarter of 2007.

There is growing convergence between the mobile phone and the portable player. A new breed of devices launched in the end of 2007 – the iPod Touch, iPhone and the new Zune player, with wi-fi functionality allowing internet browsing and music downloading on the go – are blurring the boundaries between online and mobile consumption.

The expansion of wi-fi technology, coupled with 3G, is beginning to allow a much broader music experience. In October 2007, Starbucks and Apple announced a partnership that allowed users of the iPhone and iPod Touch to download songs playing in Starbucks shops directly to their portable devices via wi-fi.

Apple hopes to sell 10 million iPhones in 2008. Sony Ericsson has announced plans for a broader music store, offering five million songs, a move that closely follows entrances from both Nokia and Vodafone's Music Store (powered by Omnifone) in the UK.

Recorded music boosts US$130 billion sector

A few years into the digital revolution, it is clear that, for all the challenges of rewarding creators and producers, the overall volume of music consumed is greater than ever before. In the US, according to Nielsen SoundScan, overall online and physical sales grew by 15 per cent in 2007 to 1.4 billion units. International studies show that listening to music remains one of the top activities among teenagers and adults.

Surging demand for recorded music has helped boost a wider supply chain: music publishing revenues rose in 2007; radio advertising revenues grew by three per cent in the year (PWC) and portable digital player sales were up 15 per cent in 2007. In total, IFPI estimates this broader sector at a value of over US$130 billion. The recording industry's investment in new talent and marketing is helping to drive this wider music economy, even though the benefits do not extend to sales of recorded music.

Music has also helped boost growth in the ISP, telecom and hardware industries. Broadband revenues in 2007 totalled an estimated US$100 billion, while consumers spent US$18 billion on portable players (Understanding & Solutions).

A study from Nokia has shown that the youth market for mobile phones in India has grown annually by 300 per cent in the last few years, with music accounting for 40 per cent of mobile phone companies' revenues in the country. There are now 50 million households in India with an internet connection and 75 per cent of these are expected to have broadband by 2010, with music a major driver.

Source: Public Opinion Strategies Survey, US, April 2007

iPhone

Nokia Music Phone

Zune Music Player

Investing In Artists

Digital is driving new opportunities in A&R and marketing

Record labels invest up to 20 per cent of their revenues in discovering and nurturing new talent. This discipline is known as artists and repertoire, or A&R. Marketing and A&R are the core functions of record companies. New digital communication channels and social networks have increased, not diminished, the importance of good A&R and marketing.

Max Hole, Executive Vice President at Universal Music Group International, says many artists want the benefit of working with others who share and match their vision, energy and enthusiasm. "Someone," he says, "who can open a door to the producer, the recording engineer, the songwriter that they love." In addition, artists do not always have the necessary specialist skills to take care of the business side of their careers – skills which record companies offer.

There are more than 1.2 million rock acts and 1.7 million R&B acts alone clamouring for attention on MySpace. This overwhelming number of new bands and music available to consumers also highlights one of the key roles for record companies in the digital space. The need for filtering, selection, marketing and recommendation is greater than ever.

"The only bad thing about MySpace is that there are 100,000 bands and no filtering. I try to find the bands I might like but often I just get tired of looking."

15 year old student, IFPI focus group research, July 2007

If artists were to pitch themselves on the internet without creating an impression elsewhere they would be highly unlikely to catch the attention of a label A&R expert to give them their break. That is not to say the world of A&R is unchanged.

Snow Patrol

Mike Smith, Managing Director of Columbia Records, says "Ten years ago I would hear about a potentially great act and spend all day on the phone to everyone I knew. Eventually somebody would have a tape and I'd send a bike across town to get it. I'd listen to it and then try and track down the manager, get on the phone to him and arrange to see the band live. Now, if someone mentions a potentially great act I check them out on YouTube or MySpace. You're immediately listening to their music, seeing what they look like and you have all of their contact details in front of you."

Calvin Harris was one of the biggest new music discoveries of 2007 in the UK and was touted as a discovery of the MySpace generation. But his success is also down to good A&R, says Columbia's Smith: "I want to know that I am buying into a major artist with real depth and you can't find that out just by looking at them on the internet and seeing how many friends they have on MySpace."

The big break is still what aspiring acts want, according to Max Hole who says that "artists want someone to love their group, create opportunities for them and give them a cheque so that they can stop being part-time waiters and start doing their music full-time."

Hole also notes that artists with a developing reputation in their home territory can often use the A&R and marketing expertise of major record labels to break through internationally, and cites the example of the British band Snow Patrol. The band was making limited progress on a UK independent label, and a new deal with Universal Music gave them a platform to reach audiences at home and abroad, especially in the US, where the result was a top five track on the Billboard Hot 100 and a million-selling album.

"A record company has always been there to be the venture capital of a band's career, to discover the talent and to finance that career. I don't think that will change in the future."

Ludwig Werner, Chairman, Bonnier Amigo, Swedish independent record company

"Artists want someone to love their group, create opportunities for them and give them a cheque so that they can stop being part-time waiters and start doing their music full-time."

Max Hole, Executive Vice President, UMG International

Section 3: The Explosion of Channels, Formats and Business Models

Five years ago music distribution formats were numbered in single figures – today, they number in the hundreds

In the digital era, record companies are licensing music across a multitude of platforms, in scores of different formats and with hundreds of different partners. New revenue streams are evolving as labels work with social networks, direct-to-consumer sites and brand partnerships

A-la-carte download services

A-la-carte downloads remain the dominant digital business model, with iTunes leading in the online sector. In the US, iTunes surpassed Amazon and Target in 2007 to become the third largest music retailer (NPD MusicWatch).

Other big brand names also came into the download market in 2007, notably Amazon, with its online music download store in partnership with all majors and many independent labels, and the announcement of Nokia's new 'Comes With Music' service.

Subscription services

Subscription services have grown steadily, particularly in the US. Revenues from subscription services, such as Napster and Rhapsody, grew by 63 per cent in the US between the first half of 2005 and the same period of 2007. Napster has a subscriber base of 750,000.

However, these services remain niche in other markets, held back by various factors, including their lack of interoperability with the dominant music player, the iPod, and under-investment in marketing and promotion. If these problems can be addressed, the potential for subscription models is enormous.

New initiatives emerged in the end of 2007. Advocates of these services point to their high level of "stickiness" once consumers first try them. A mass market channel combined with a compelling consumer proposition could potentially change the outlook on the subscriptions market.

"I like the fact that you pay a set fee for all the music you want with Napster, but I can't use it with my iPod."

20 year old UK student, IFPI focus group research, July 2007

Omnifone launched MusicStation, a new mobile subscription service designed to work on a wide variety of mobile handsets worldwide. It is already running in the UK, Hong Kong, Sweden and South Africa and there are plans to roll it out in many more countries in 2008.

MusicStation offers consumers access to a library of over 1.4 million tracks from all majors and many independent labels for a small weekly fee, with no extra data transfer charges. It backs up a users' library so that if a consumer mislays their handset they do not lose their music collection. In the UK, the service comes bundled into a range of existing price plans or is available on a Pay As You Go basis at £1.99 per week.

OMNIfONE™
Global mobile phone applications

At the end of 2007 there emerged a new subscription model based on the concept of 'bundling' music with other services or devices – be it an ISP subscription, a mobile phone or a portable player. While the music comes virtually 'free' to consumers under this model, record companies and artists get paid out of the sale of services or devices. These partnerships also create opportunities for more marketing and promotion of music services in the bundled offer.

Subscriptions 5%

Mobile 47%

Online 48%

Source: IFPI, first half 2007 industry revenues

" MusicStation is the first mass-market and easy to use unlimited mobile music download service, with a great choice of repertoire for a very reasonable cost – that's the holy trinity of making subscription services work."

Rob Lewis, Chief Executive, Omnifone

In December 2007, Nokia announced a new subscription venture, in partnership with Universal Music, to offer millions of songs to Nokia phone users. The "Comes with Music" programme is due to launch in the second half of 2008 and will offer 12 month access to Universal's entire catalogue to consumers who buy selected Nokia music phones. Ownership of downloaded tracks will not be restricted to the 12 month period, so users can keep their downloads permanently. Nokia is negotiating with other labels to extend the music catalogue on offer.

Also in late 2007 Universal partnered with French ISP Neuf Cegetel, whereby for a monthly fee of €29.90 the ISP offers high speed internet, fixed line telephony, HD TV service and an unlimited music download service with Universal's catalogue. In a similar deal EMI partnered with Alice, an ISP owned by Telecom Italia, in December 2007.

Consumers offered more non-DRM download services

Lack of interoperability between services and devices has been a significant barrier to the development of the digital music sector. Interoperability has long been a key goal of the record industry, which has worked with its industry partners to develop technological solutions enabling fully interoperable DRM.

Unfortunately, despite the potential for such solutions, some major technology providers have so far been unwilling to participate. Faced with this lack of progress, all the major record labels decided to offer non-DRM download services, either permanently or as part of a trial period to supplement their existing offerings. They joined independent labels in expanding the opportunities for online retailers to sell tracks without DRM.

The DRM-free model is one way to avoid the interoperability problem. It allows consumers to buy music from any store, take their tracks wherever they want and play them on any device.

The use of a non-DRM model led to new services such as Amazon entering the already-established digital music market. Amazon's new service sells music in a format that is compatible with a vast number of portable players, including the iPod. It offers a catalogue of over two million songs for US$ 0.89-0.99 and albums for US$ 5.99-9.99.

DRM today is still a key element of the digital business, with DRM-free and DRM-protected download offerings co-existing in the market. Many business models, particularly based on subscriptions (where users pay a monthly fee for unlimited access to music), super-distribution (allowing fans to share music with their friends) and time-limited downloads (such as those offered by ad-supported services), cannot exist without DRM and record companies remain committed to these alternatives.

Services specialising in indie music first offered DRM-free downloads. eMusic, which operates in the US and Europe, offers a subscription service that allows consumers to own the tracks they are authorised to download, even when their subscription ends. MP3 tracks can be played on multiple devices, including the iPod. The service targets heavy music buyers over the age of 25 and specialises in a non-mainstream catalogue comprising over two million songs. To date, eMusic has attracted more than 400,000 subscribers worldwide.

EMI was the first major record company to adopt a DRM-free strategy, with the launch of DRM-free superior quality downloads as an alternative offering through the iTunes store in May 2007. Universal also announced DRM-free download trials in 2007, which will be reviewed in January 2008. Warner Music launched DRM-free offerings in late 2007, while Sony BMG landed its DRM-free Platinum Music Pass series of digital album cards in January 2008. The music of all the majors and a number of independent labels now feature on several non-DRM services, including Wal-Mart and Amazon.

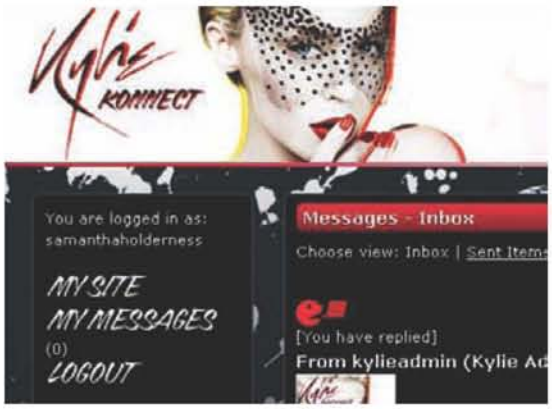
Advertising-supported services

Advertising-supported music services are a small but potentially significant revenue stream for record companies, which some see as the logical strategy for reclaiming a younger generation of consumers habituated to a culture of "free" music. According to Jupiter Research file-sharing currently dominates music acquisition among younger consumers. In 2007 over a third (34 per cent) of internet users aged 15–24 illegally file-shared music. This is three times the rate of legal service usage among this age group.

Ad-supported services offer consumers free access to streamed or downloaded music while artists and record companies are compensated by revenues generated by advertising. The best examples of this are the recent deals between some record companies and social networks such as MySpace, Bebo, YouTube, LastFM and Imeem. These deals are mostly based on licensing agreements for streaming music and music videos for a share of advertising revenues.

Questions remain however as to the potential for ad-supported models as some believe the addition of ads on free services will divert consumers elsewhere, and there are continuing concerns over copyright infringement. So far the model has worked best in growing the video-on-demand business.

Progress was made in 2007 to create a global rights body to act as a centralised licensing service for independent record companies whose music is used on sites such as YouTube and who wish to negotiate deals with services. The body is known as Merlin and runs as a sister organisation to the global independent record labels body WIN.



Record labels go direct to fans

Record companies are rolling out 'direct to consumer' initiatives, allowing consumers to access a range of artist products directly via their website. This new wave of artist sites offer the opportunity for fans to connect with the artist, purchase content and communicate with other fans.

Universal Music has created getmusic.com.au in Australia as a one-stop shop for consumers who want to buy tracks, merchandising or concert tickets. It also provides news, competitions and forums for music fans to have their say. In the run-up to Christmas 2007, Universal ran artist-centred campaigns using the "get" branding, such as "get Fergie" and "get Fall Out Boy" to drive awareness of the site.

Boutique sites have also proved successful for artists as diverse as U2 and Girls Aloud. U2.com offers exclusive music tracks, behind the scenes interviews, fan reviews, limited edition merchandising and invitations to become involved in the campaigns that U2 are active in. EMI also supports many artists' websites, including Lily Allen, Gorillaz, and The Kooks. Artists increasingly look to labels to provide such specialist support services.

Warner Music and Premium TV, a specialist digital services provider, have launched Rhino TV, a specialist digital hub for consumers. The site offers an interactive, free-to-access music experience that enables visitors to manage and share their favourite tracks as well as purchase content. Through a searchable archive, users can search thousands of hours of music-related video.

Experimental new pricing models also took shape in 2007, their impact as yet unproven in the marketplace. One such system was tested in October, when the British band Radiohead set a precedent by offering downloads of their new album 'In Rainbows' directly on their website under an "honesty box" system. Fans were given the option to pre-order the album download at a price of their choosing (minimum charge of £0.45) or pay £40 for a premium boxset which included two CDs, two vinyl records plus artwork and booklets.

Top and Middle:
Australia's Get Music website

Bottom:
Girls Aloud

Source: Circuits of Cool/Digital Playground, July 2007

Brand partnerships

With the decline in traditional forms of advertising on TV and radio, music offers a great opportunity for international brands to reach consumers online. The widespread appeal of music can help brands penetrate markets and gain credibility among specific segments. Record companies have created teams specialising in identifying brand partnership opportunities via digital platforms.

Sony BMG launched its Musicbox video network in 2006. Musicbox is comprised of a series of ad-driven online video players that are deployed across Sony BMG's network of nearly 600 artist and label websites. Fans can send links to friends, or embed the player on their blogs, MySpace pages, Facebook or other community sites. This creates an ancillary network, providing exposure for Sony BMG's artists while adding value to brand partners such as AT&T, Honda, Chase, Puma, Starwood, MSN, and L'Oreal.

In July 2007 EMI announced a digital premium campaign with Burger King. Consumers were able to search for, sample and download a free song from a specially created microsite after inputting a unique code obtained with purchases at the restaurant. A multi-year, multi-platform deal between Rihanna and CoverGirl, saw Rihanna acting as the spokesmodel for CoverGirl's new lip gloss.

Partnerships with brands are also helping drive catalogue sales. An advertising campaign for Cadbury's Dairy Milk chocolate containing Phil Collins' 1981 single In The Air Tonight propelled the single to the top 15 chart in the UK in September 2007. The advert logged hundreds of thousands of hits on YouTube.

"The record industry used to be focused on the record and all the rest was promotions. Now it's a more balanced business where you have records, TV shows, merchandise, touring revenues and so on."

Jean-Bernard Lévy, Vivendi Chief Executive

CoverGirl campaign featuring Rihanna

Section 4: Copyright Theft – The Impact and the Response

Unlicensed music and the unfair competition it imposes on legitimate services is the biggest challenge for the music business today

The greatest problem in "monetising" digital music has been its ubiquitous availability unlicensed and for free. Tens of billions of illegal music files are traded annually worldwide at an estimated ratio of 20 illegal downloads for every track sold. This has had a major impact on the development of legal services, holding back growth in the whole digital sector.

The Institute of Policy Innovation study 'The True Cost of Sound Recording Piracy in the US Economy' projected losses from illegal downloading worldwide to US record companies at US$3.7 billion (August 2007).

Other research has focused on the specific impact of illegal downloading on buying behaviour. Italy's Luigi Einaudi Foundation in 2007 found that 30 per cent of P2P users bought fewer CDs and DVDs, while only six per cent said they bought more CDs. In Australia, research undertaken for ARIA (February 2007) shows that 57 per cent of P2P downloaders rarely or never purchase the music they download – pointing to straight substitution of legitimate sales. Numerous studies in different markets confirm the finding that the effect of illegal downloading on CD buying is overwhelmingly negative.

Digital piracy in Latin America has expanded rapidly. It is estimated that 2.6 billion illegal music files are downloaded in Mexico and another 1.8 billion in Brazil per year (Ipsos research). Online piracy has hit the core music buying population in the region – research in Mexico shows that 64 per cent of music downloading is carried out by consumers in the wealthier ABC economic categories, with similar findings in Brazil. In 2007 the Mexican market dropped by an estimated 25 per cent and Brazil fell by an alarming 50 per cent in the first half of 2007.

Japan Confronts Mobile Piracy

The success of Japan's mobile music business has had a flip side. Research in 2007 by the Recording Industry Association of Japan (RIAJ) found that mobile piracy was already becoming a very significant problem. The research highlighted the following:

- More than a third (37%) of mobile internet users frequently obtain illegal music via their mobile phone. This figure rises to 65 per cent among the younger demographic.
- Nearly 400 million illegal music files were downloaded in a year.
- Nearly 80 per cent of users who obtain illegal music files are doing it with no sense of guilt.

The industry has been quick to respond to the threat. In 2007, RIAJ developed special technology which allows the tracking of illegal uploading. Service providers are now receiving a number of "cease and desist" notices relating to infringing content and four criminal prosecutions have already resulted against illegal uploaders.

RIAJ is launching the biggest-ever education campaign about mobile piracy in March 2008, with support from government, mobile operators and music right holders' organisations.

In Europe, Spain and the Netherlands have a huge online piracy problem resulting in underperformance of their legitimate market sector. According to Jupiter Research, over a third (35%) of all internet users are now regularly file-sharing infringing music in Spain and 28 per cent in the Netherlands. A new study by the Spanish Ministry of Culture (October 2007) shows that five million Spaniards, or 13 per cent of the population, have downloaded music illegally in the past year.

China, with nearly as many broadband users as the US and little effective enforcement, is one of the biggest sources of illegal downloads in the world. A legitimate music market of only US$74 million – less than one per cent of global sales – is choked by a digital piracy rate of over 99 per cent.

The country is hosting some very large unlicensed music delivery services that deeplink to unauthorised song files and derive advertising revenue from doing so. Such services account for the majority of online music piracy in the country. Large, listed companies such as Baidu and Yahoo China all offer such unauthorised services that are available throughout the world and particularly popular in Asia.

Securing proper enforcement against internet piracy in China is one of the recording industry's top priorities. In December 2007, a Beijing court confirmed that Yahoo China was acting illegally by facilitating mass copyright infringement. This verdict sets a precedent for similar services across the country to heed.

"The fact is that in a commercial culture that doesn't protect intellectual property, today's violator is tomorrow's victim. There are no long-term winners from growing intellectual property theft."

Peter Mandelson, EU Trade Commissioner

Responding to Copyright Theft

Industry efforts are disrupting piracy networks

Digital music piracy is fragmenting into new forms as technology enables many new forms of illegal file-sharing, including sharing via instant messenger, blogs, local network sharing, Bluetooth mobile sharing and e-mail sharing. In addition, users can directly download from illegal internet sites specifically designed to be used by mobile phone users. These sites are particularly located in countries such as Japan where flat rate 3G is available.

Despite fragmentation, P2P file-sharing still accounts for the large bulk of digital piracy and, given the volume and the role it plays in distribution to other piracy engines such as blogs and cyberlockers, is still the primary target of industry anti-piracy actions. Third party surveys estimate that up to 80 per cent of all ISP broadband capacity is taken up by P2P file-sharing.

- **Large-scale uploaders using networks such as Gnutella**
- **"Hubs" or servers which connect millions of file-sharers on services such as DirectConnect and eDonkey**
- **BitTorrent trackers such as the Sweden-based Pirate Bay**
- **Pre-release piracy, where leaks often occur weeks before the official release date, denying artists and producers revenues at the most crucial period in the lifecycle of the recording.**

Despite the scale of the problem, enforcement is helping contain piracy. Figures from Jupiter Research show that while the number of regular file-sharers in the major European markets rose by 35 per cent between 2003 and 2007, broadband subscriptions in these markets rose more than four-fold in that same period. In total, 17.6 per cent of internet users in Europe regularly file-shared in 2007 – a figure that is roughly the same as in 2003.

In the US, the number of people using P2P file-sharing services was largely flat in 2007, but larger numbers of music files were downloaded illegally. The posting of hyperlinks to unauthorised music on blogs and other websites has re-emerged as a problem.

IFPI's actions intensified in 2007. A series of actions were taken against P2P networks, including the closure of seven major servers on eDonkey in October following court injunctions in Germany. There were similar eDonkey server closures in the Netherlands and France following IFPI's legal actions.

These actions, combined with a systematic "notice and take down" programme, significantly disrupted one of the top three illegal file-sharing networks. The number of files on the centralised eDonkey network dropped by 40 per cent to just over 400 million between January 2007 and December 2007.

Takedown notices have been sharply increased in the US as well. University students account for a very large share of illegal file-sharing and have therefore been heavily targeted with lawsuits brought against those who refused to settle out of court. Universities have been encouraged to take proactive measures against on-campus P2P use, with notable improvements shown in some schools where measures were taken.

This impact is verified by research. In November 2007 NPD found that over a third of P2P users (39%) said they could not find the songs they wanted on P2P networks. The second most common negative P2P experience was the inability to download from search results (32%).

"Copyright law protects all copyright holders, big or small. It's a corner stone of modern civilised society. People should stop attacking it – it's there for the protection of all of us, writers, producers, musicians, playwrights etc. big and small."

Anthony Hall,
Pure Mint Recordings,
UK Independent Label

Tackling Pre-release Piracy

Album leaks well before official release are a growing threat

Pre-release piracy is a fast-growing area of the recording industry's anti-piracy work. Record companies look to IFPI's global team of investigators to stem the proliferation of pirate copies in the crucial weeks around the official album release.

A new album makes a large share of its revenues in its first few weeks, so the stakes are high. Leaks usually happen between three weeks and five days prior to release. Pre-release copies are most commonly leaked on to BitTorrent sites and then spread onto P2P networks blogs, forums and website links.

IFPI's Anti-Piracy Unit tracks the distribution online of newly-released albums, systematically removing thousands of illegal copies from the internet every day, targeting offenders and paving the way for legal action or prosecution. Teams are monitoring hundreds of albums at any one time of day. The unit's success stories include albums by household names that have been leaked onto the internet by individuals in the legitimate supply chain, such as journalists, commercial DJs and even leading figures in fan clubs.

"A major pre-release leak can mean the difference between an album being a top-ten hit or an also ran. Producers today know that if they don't take the right steps at the right time to protect their releases, then the internet is going to be literally swamped with illegal copies of their new release."

Jeremy Banks, Head of IFPI's Anti-Piracy Unit

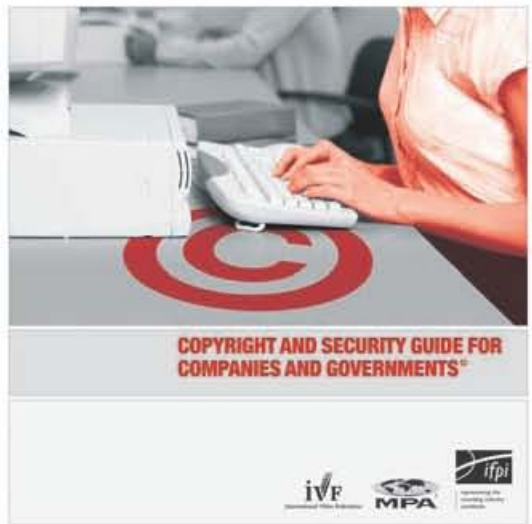
Blogs are another common route for pre-release piracy. There are hundreds of thousands of active music blogs that often feature copyright infringing music. Many of these tracks are hosted in online "cyberlockers" which the people who post them hope, mistakenly, will protect their anonymity.

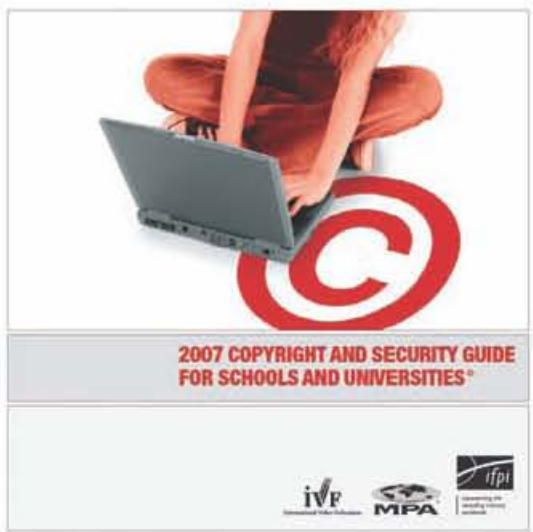
Pre-release leaks reflect the determination of the so-called "ripping groups", highly organised and secretive groups made up of technically proficient internet users, for whom purloining and distributing a pre-release hit is a badge of honour.

In 2007 over 350,000 warning notices were sent out regarding over 550,000 infringing URLs. It is estimated that the resulting number of illegal non-P2P files removed as a result of these notices and other actions totalled around 120 million.

In October, investigations by IFPI and its UK affiliate BPI led to British and Dutch police shutting down the OiNK website, the world's biggest source of illegal pre-release chart albums, in an operation coordinated between the UK and the Netherlands and assisted by Interpol.

OiNK specialised in distributing albums leaked on to the internet, often weeks ahead of their official release date. More than 60 major album releases had been leaked on OiNK in 2007, making it a primary source worldwide for illegal pre-release music. The site, with an estimated membership of 180,000, had been used by many hardcore file-sharers to violate the rights of artists and producers by obtaining copyrighted recordings and making them available on the internet.





IFPI guides aimed at helping business and academic institutions tackle piracy

Section 5: Time for Governments and ISPs to Take Responsibility

Today, getting ISPs to help protect creative content is the music industry's top priority

Internet Service Providers (ISPs) are the "gatekeepers" of the internet and have a vital role to play in curbing copyright abuse. They have the technical ability to do so, and increasingly the commercial incentives as well. The full cooperation of ISPs could lead to a very significant change in the music sector's ability to tackle copyright infringement while reducing the amount of litigation needed to deal with online piracy.

In November 2007, the most significant development yet in this process occurred when Nicolas Sarkozy, the French President, announced a potentially revolutionary new agreement under which ISPs in France commit to disconnect persistent copyright infringers on their networks. The move followed a number of significant advances in other countries during 2007.

The French President's move confirms that disconnecting the accounts of serious infringers is feasible and reasonable for ISPs. There is no doubt ISPs have the means to address copyright infringement, just as they can control other forms of illegal material passing through their networks, such as spam and viruses. In most cases this is merely a question of enforcing their existing customer terms and conditions: most ISPs include a provision prohibiting use of the service to infringe copyright on pain of losing service.

The French model of warning and disconnection could be implemented by governments in other countries as well. Disconnection of repeat infringers is already enshrined in the copyright law in the US, Australia and Singapore. The model has attracted interest in the UK and Sweden: in the UK, the 2006 government-commissioned Gowers Review of Intellectual Property proposed a voluntary 'Best Practice' agreement by which ISPs would disconnect users engaged in piracy. The report recommended that the government consider legislation if this voluntary cooperation was not working by the end of 2007.

A groundbreaking deal for ISPs: President Sarkozy and Denis Olivennes

In Sweden, a report by the Justice Department investigator Cecilia Renfors, proposed a change in Swedish law to oblige ISPs to take action to terminate the contracts of certain users who repeatedly use their connection to infringe copyright. This obligation could be enforced in court by right holders.

In addition to disconnecting user accounts, filtering is a feasible and reasonable way for ISPs to tackle copyright infringement. Many ISPs already implement technology to manage traffic across their networks for their own self-interest: for example most ISPs filter email traffic to remove spam, and many ISPs slow down traffic on P2P networks at busy times to reduce bandwidth costs. There are technologies available that enable ISPs to automatically filter traffic and prevent exchanges that infringe copyright.

The court ruling in the SABAM v Tiscali case in Belgium in September 2007 set an extremely important precedent. It not only confirms that the ISP should take proactive steps to block infringing content; it also confirms expert evidence on a range of feasible blocking and filtering solutions available to ISPs.

In the US, AT&T's recent commitment to work with the film and music sectors on anti-piracy technologies marks a sea-change in approach by one of the major ISPs.

IFPI and its affiliates are discussing with ISPs in many countries a system for curbing mass copyright infringement on their networks. Many countries are now progressing towards concrete steps by ISPs in this area. However, the recording industry is prepared to use the courts where voluntary collaboration fails. In some countries, notably Denmark, the Netherlands and France, IFPI has reluctantly but successfully used litigation to require ISPs to disconnect the accounts of users responsible for infringing services.

"The Internet must not become a high-tech Wild West, a lawless zone where outlaws can pillage works with abandon or, worse, trade in them in total impunity."

Nicolas Sarkozy, President of France

Increasingly, ISPs have a commercial incentive to work with the recording industry. Illegal P2P file-sharing may have helped drive broadband subscriptions in the past, yet today these activities, particularly in respect of movies, are hogging bandwidth. Independent estimates suggest up to 80 per cent of internet traffic is generated by P2P file distribution, the vast bulk of which is unauthorised use of copyrighted music and movies.

In this way, online piracy is not only hurting ISPs' existing business by hitting the efficiency of their networks – it will increasingly hurt their future business, as ISPs compete to share in the revenues from copyrighted digital content such as music, film and television.

Governments Must Effectively Enforce The Law

A flourishing digital music business needs a proper legal environment and a proactive commitment to respect for copyright. This is the challenge for governments and enforcement authorities. Piracy havens damage the music sector globally.

Located in the heart of the European Union, Swedish-based The Pirate Bay is one of the world's biggest engines of copyright infringement, enabling millions of users to download illegal copies of music, film and other content. It has become a global icon for the violation of copyright and is translated into more than 30 languages.

Organisations representing creators, performers, producers and publishers across the music, film and publishing sectors in Europe are looking for the law to be effectively enforced against The Pirate Bay. They warn of the danger that Sweden, normally considered to be a strong upholder of EU standards and a promoter of culture, should instead be seen as the haven for a cult of copyright infringement that has achieved global reach.

Swedish police raided The Pirate Bay in 2006 and in January 2008 prosecutors are preparing to file a criminal case against the site's operators. In the meantime, the service continues to promote the mass infringement of copyright of recorded music, films and even books.

In China, record companies trying to develop a legitimate digital music sector are having to do so against the backdrop of rampant levels of internet piracy, while the country's major internet companies have to date missed the opportunity to prove that they can be responsible partners in this process. Court cases involving two of the country's internet giants, Yahoo China and Baidu, have acted as a warning to internet companies throughout China that are illegally distributing copyrighted content.

Record companies had attempted to forge a legitimate partnership with Yahoo China but were forced into litigation due to the company's refusal to stop large-scale infringement on its music delivery service. This is a bespoke service separate from its general search engine, and it enables and induces users to search for, play and download infringing music tracks for free without ever leaving Yahoo China's website. In a landmark court ruling in April 2007, Yahoo China was ruled liable for illegally providing links to copyright infringing music files. The ruling was upheld by the Beijing Court in December after the company appealed the finding of liability.

The recording industry firmly believes that Yahoo Inc – one of America's best-known and most influential internet companies – can and should act to stop Yahoo China's calculated and commercially-driven infringement of the music industry's rights. Yahoo Inc is represented on the Board of Yahoo China's parent company, Alibaba Group and has a 44 per cent stake in Yahoo China through its investment in the Alibaba Group.

Russia has been a particular haven for internet piracy. In 2007 a combination of industry legal action, government pressure from the US and EU and withdrawal of payment services by credit card companies, led to the closure of the rogue site allofmp3.com. Despite success against this high profile brand, numerous lower-profile pirate services exist within Russia, aided by a weak intellectual property law enforcement culture.

P2P is "Choking Bandwidth"

P2P usage is having a significant impact on internet traffic. P2P networks are producing more internet traffic than all other applications combined and this could impact ISP infrastructures, damaging consumers' internet experience. While P2P accounts for up to 80 per cent of all internet traffic, only 20 per cent of internet users worldwide use P2P services (ipoque).

A report by analyst firm Nemertes Research Group published in 2007 found that internet access infrastructure will likely cease to be adequate for supporting demand within the next three to five years, particularly in North America.

The investment required by ISPs to "bridge the gap" between internet demand and capacity ranges from US$42-55 billion, or roughly 60-70 per cent more than ISPs plan to invest. Limited capacity, the report suggests, could stifle innovation in internet-based services – a new YouTube, for example, would not be able to flourish.

" I think the failure of ISPs to engage in the fight against piracy, to date, has been the single biggest failure in the digital music market."

Paul McGuinness, Manager of U2

Section 6: Creating Value in the Digital Sector

At the heart of the digital revolution is the challenge of creating value from digital content

Many sectors such as the newspaper, travel, television, film, telecommunications and games industries are grappling with dramatic changes in their business landscape.

Competition from a deluge of free information services has hit news publishing hard. Local newspapers are seeing a sharp loss of advertising revenues, particularly classifieds and property, to the internet. National newspapers are developing themselves as "brands" across different media. Online revenue growth is now a top priority at many newspapers, but digital's share of total revenue in this sector is still far behind the music industry.

In the US, online advertising on newspapers' websites rose by 21 per cent year-on-year in the third quarter of 2007 to US$773 million, according to the Newspaper Association of America. Yet this figure represented only 7.1 per cent of total newspaper advertising revenues and the rise in online advertising is not offsetting the fall in print advertising, which fell by nine per cent to US$10.1 billion in the same quarter.

The TV industry is seeing its audiences move in droves to the internet. Broadcasters are trying to revive interest in programmes through sharing and recommendation clips on social networking sites such as Bebo, in return for a share in advertising revenues.

Outside the entertainment industry, migration of commerce online has been held back by the inherent problem of internet payment. Of all payments serviced by credit card company Visa, only 12 per cent constitute electronic commerce, illustrating the relative size of ecommerce transactions compared to the offline market.

The challenge of "monetising" the digital world affects even sectors apparently at the most cutting edge of technology. In October, the online company eBay admitted it had substantially overpaid, by nearly a billion dollars out of US$ 1.7 billion, when it bought the telephony service Skype. In November 2007, Rupert Murdoch told News Corporation shareholders that there was still a lot of work to do in educating advertisers about the potential of MySpace, the social network the company bought for US$580 million in 2005.

Piracy is proving a huge threat to many forms of digital content. Research by the Helsinki Institute for Information Technology in Finland showed that P2P piracy is mostly affecting the rental of films, the purchasing of CDs and viewing of TV programmes.

The publishing industry is also affected, with copies of JK Rowling's 'Harry Potter and the Deathly Hallows' leaking on the internet prior to its official launch in 2007. Film piracy is also beginning to prove a major problem, with Solutions Research finding that nearly one in five US citizens has a pirated film on their computer and that 80 per cent of people who download films only use peer-to-peer (P2P) file-trading sites and not legitimate services.

Will traditional forms of consuming newspapers, television and books survive?

This cartoon by Wesley Bedrosian accompanied the article 'The Hidden Risk of File-Sharing' by Joseph de Avila, published in the Wall Street Journal, 7th November 2007.
(Cartoon published with permission of the artist)

Section 7: The Hidden Dangers of Illegal Downloading

Unlicensed internet services risk spyware, adware, malware and even identity theft. Yet these dangers are often unknown to downloaders

The security risks of downloading unlicensed music have been well-publicised, but awareness of them still appears low.

An academic paper by Eric Johnson, 'Inadvertent Disclosure – Information Leaks in the Extended Enterprise' (June 2007), examined inadvertent disclosures through P2P networks and found that:

- 'Unrecognised to many of [P2P] users is the serious security threat these networks pose to both corporate and individual security.'
- 'Confidential and potentially damaging documents have made their way onto these networks. The research also shows that criminals actively search P2P networks hoping to find information that they can exploit.'
- 'Our analysis clearly reveals a significant information risk firms and individuals face from P2P file sharing networks. '

According to Symantec, the main vehicle for spreading viruses and malware today is email, but distribution via P2P is also in the top ten list of main propagation vehicles. In the first half of 2007 15 per cent of all potential infections were propagated by eDonkey.

Specialist technology security company, McAfee, looked at the risk levels of searching the internet. Its report, "The State of Search Engine Safety (June 2007)", highlights that searches of keywords involving P2P services, such as Limewire, are among the most likely to generate results that activate spyware and viruses once clicked on.

New research also points to the dangers of other forms of infringing downloading. An experiment run by Benjamin Googins, a senior researcher at the international IT software management company CA, showed that a single download from an unauthorised MP3 site resulted in the installation without permission of trojan downloaders, spyware and pop-up ads having a severe impact on his computer's performance.

Consumers are paying a price for these kinds of risks. Americans spent at least US$8 billion in computer repairs, parts and replacement over the past two years as a result of viruses and spyware alone according to Consumer Reports.

Research exposes piracy in the workplace

Companies face significant security risks when employees file-share on corporate networks.

Research conducted by Ipsos-MORI for IFPI in the UK in November 2007 indicates that one in ten office employees are using the workplace to download music, two thirds of them illegally, exposing their employers not only to computer network risks, but to legal risks too.

Nearly half of those who download music illegally in the workplace (43%) know that their employers have a policy on copying, sharing and downloading music – suggesting they disregard rules set by their bosses.

The problem appears to be concentrated among younger workers. The survey indicated that one in five under 25s illegally download music at work. It only takes one person to download an infected file and expose the company to huge risks.

The problem is not restricted to the UK. Research by the Information Systems Audit and Control Association (ISACA) explored the internet behaviour of US employees and found that 15 per cent of respondents indicated they had used P2P at work at least once, with 35 per cent of white collar workers saying they had violated their company's IT policies at least once.

In Europe, McAfee commissioned a pool of IT managers with research firm ICM across 1,049 IT professionals in the UK, France, Germany, Italy, the Netherlands, Poland, Spain, Sweden, Austria and Switzerland and found that music downloaded from the web came top of a list of perceived threats to security. Despite this, two-thirds of European IT managers admitted that they don't block music downloads to work machines.

Recent moves towards encrypting P2P traffic could increase the overall security risks if it is used illicitly on corporate networks. Encrypted P2P prevents security measures such as IT network firewalls from screening the transferred traffic for the threat of viruses or spyware. IFPI urges companies to note this potential threat and take the necessary steps to protect their IT networks.

IFPI has produced and distributed free copyright and security guides for companies and for academic institutions that can be downloaded from www.ifpi.org. Organisations seeking advice on how to improve or implement their policies on copyright should contact IFPI.

Workplace Piracy in the News

- In September 2007, Citigroup confirmed that it was investigating a data breach where the names, mortgage information and social security numbers from 5,200 customers were inadvertently leaked by an employee using the Limewire P2P application.
- Also in September 2007 a confidential report by consultancy firm Booz-Allen Hamilton for the Federal Transit Administration on the US bus and rail networks leaked on P2P, resulting in a major security lapse.
- In June 2007, Pfizer said the names and social security numbers of 17,000 current and former employees were leaked after the partner of an employee downloaded file-sharing software onto a company laptop.
- In July 2007, a Congressional committee in Washington heard testimony from experts that inadvertent file-sharing on P2P networks could pose a significant problem in terms of breach of confidential data and could threaten national security.

Section 8:
Promoting the Value of Music

IFPI and its affiliates run numerous education programmes around the world

Education is a key priority for the recording industry. In 2007 initiatives were launched in partnership with education professionals, designed to give teachers and parents as well as young people the tools to understand the importance of copyright, intellectual property and the value of creativity. The music industry cannot break the "free music mindset" alone. Government cooperation is essential, especially to make copyright education a higher priority for core national curriculums, in an era when sectors relying on intellectual property rights will be important for job seekers.

Some countries are leading the way. The Australian Copyright Unit of the Ministerial Council on Employment, Education, Training and Youth Affairs is working with the recording industry to develop a syllabus within schools to bring music into classrooms and learn about intellectual property. Other projects such as "QuickStart" in the UK have seen government work with industry to pilot a programme where children run their own record labels in order to grasp the fundamentals of copyright through an operating business model.

Resources for schools and young people

"La Musique et ses Métiers" ("Jobs in Music") is a French exercise book aimed at nine to 13 year olds and is released as part of an existing series of educational booklets called 'les Incollables'. It features cartoons and pictures, pages, quizzes and games about 'the history of music/ instruments', 'where music is today', 'digital music', 'sound engineering', 'the studio', 'the ubiquitous nature of music' and 'the economy of music'. Branded Pro-Music/PlayBac, it is sold in libraries and bookshops throughout France.

The parents' guide "Young People, Music and the Internet", used in 21 countries was adapted for the Australian, Icelandic and Japanese markets and is soon to launch in mainland China. A new version written by international children's charity ChildNet with advice for teachers as well as parents is being developed for 2008.

A new interactive teacher's resource for secondary schools called Music for Free? was launched in Australia in 2007. Other existing resources from around the world have included Austria's Value of Music, Canada's Listen Up 2, Argentina's Everything Begins with a Song, Poland's Be Original, Japan's 'Happy music cycle' /'Respect our music' and the United States' Music Rules!, Learn b4 u Burn, Beat Street Assembly programme and Face the Music: Copyright, Art and the Digital Age Resources.

The Mexican recording industry enrolled fans in its 2007 anti-piracy campaign Guardians of Music – asking them to spot copyright infringing music by their favourite artists on the internet. These fans have become, in effect, a taskforce reporting illegal content wherever they find it. Mexican artists have explained how what the "Guardians" are doing matters to them. More than 40 artists have participated in different activities with fans, generating coverage in the mass media. See http://www.amprofon.com.mx/guardianes.php?item=menuGuardianes&contenido=videos.

The Japanese recording industry (RIAJ) has become the first to tackle public attitudes to mobile music piracy, launching a new artist-led campaign for mobile phone users with the three biggest mobile carriers called "Please Protect Mobile Music."

The French industry association SNEP established a discussion forum aimed at establishing a dialogue between the record industry and a targeted core of online commentators. Called Face/Face, it caught the interest of the French online community, many of whom genuinely wanted to exchange rational points of view with people from the industry. It attracted 500 members and approximately 5000 messages over a period of three months.

Australian 'Rock the Schools' Tour with the band SkyBomber. School tours take place around the world to bring together industry professionals, bands and students in discussing the application of copyright in the digital age and how it protects creativity.

Piracy Kills Music – a Norwegian information and awareness campaign with an animated film, a free CD with tracks from Norwegian artists and anti-piracy information and a website for young people, schools and colleges. See www.piracykillsmusic.no.

Hungary's interactive comic strip (http://szerzoijog.sulinet.hu) aimed at students surfing the web at schools on Hungary's educational networks ("sulinet" and "eduweb).

Chile's copyright campaign labelled "Piracy is a crime" included an attractive commercial portraying cartoon characters being chastised for promoting piracy. The commercial was debuted in a well-attended press conference, played in over 80 percent of the movie theatres in the country and aired in two of the main networks with heavy rotation for a month.

Examples of consumer campaigns from Japan, France and the Australia

Digital Music Services Around the World

* Launched in 2007

ARGENTINA
10musica
Farolatino
Ubbimusica
Zapmusic

AUSTRALIA
BigPondMusic
ChannelGo
ChaosMusic
iTunes
JB Hi-Fi
MP3.com.au
NineMSN
Optus Zoo Music
Sanity.com.au
Soundbuzz

AUSTRIA
A & M Weltbild
AonMusicDownload
Die Presse Musikladen
eMusic
iTunes
Libro*
MSN Music
Mycokemusic
News Networld
One4Music
Preiser
Soulseduction

BELGIUM
Belgian Music Online
EMI Downloadshop
eMusic
Extrazone
Fnac
Free Record Shop
iTunes
Jamba
MSN Music Club
Music Brigade
Music Minutes
Prefueled
Q-Music Downloadshop
TempoMusic
TuneTribe
Warner Music Benelux
Ringtone Shop

BRAZIL
Americanas.com
Antena1
Baixa Hits*
Brazil Telecom
BrTurbo
Ideas Music Store*
iMusica
MSN Music
Musig
Oi
Som Livre
Sonora
Submarino
TIM Music Store*
UOL Megastore
Vivo*
Yahoo! Music

BULGARIA
M.Dir
Music.gbg

CANADA
Archambault
Bonfire@Futureshop
eMusic
iTunes
MuchMusic
MyMusic
Napster
Puretracks
SympaticoMSN
Telus Online Store
Yahoo!Music
Zunior

CHILE
Mall Music
Wow

CHINA
9sky
A8
AigoMusic
QQ
Top100

DENMARK
3 Hi3G – Planet3
Bilka Musik
Box
B.T. Musik
CDON
Inpoc Musik
iTunes
MSN Music
Musikhylden
Prefueled
TDC Musik
Telia
Urban Musik

FINLAND
Biisi
CDON
eMusic
IttaSanomat Musiikki
MSN Music
NetAntilla
Pepsi MaxMusic
PHNet
Pop City

FRANCE
E-Compil
eMusic
FnacMusic
iTunes
Magasin U
MSN Music
MTV
Starzik
Tiscali
Virgin Mega
Wanadoo

GERMANY
AOL Music
eMusic
Freenet
iTunes
Media Online
Medion
MSN Music
Musicload
Napster
One4Music
Saturn

GREECE
eMusic
Go mp3
iTunes
mpGreek
Musicnow
Tellas Music
Virgin Mega

HONG KONG
08Media
Eolasia
iMusic
Moov
Music Station
NWTmusic
Soundbuzz

ICELAND
Grapewire
Tonlist

INDIA
CrimsonBay
India Times
Soundbuzz

IRELAND
7Digital
easyMusic
eMusic
Eircom
iTunes
Wippit

ITALY
Azzura Music
CD Rai
eMusic
iTunes
Libero iMusic
Messaggerie Digitali
MSN Music
MTV IT
Net Music Mediaworld
Radio Deejay
RossoAlice
Tiscali
Unitedmusic
Vitaminic

JAPAN
Excite Music Store
goo Music Store
HMV Digital
iTunes
LISMO
Moocs
Mora
MSN Music
Napster
OCN Music Store
OnGen
Rakuten Music
Download
Yahoo! Music

LUXEMBOURG
eMusic
iTunes
TuneTribe

MALAYSIA
Bimbit
Bluehyppo

MEXICO
Beon
Tarabu

NETHERLANDS
Countdownload
Download.nl
eMusic
Freedownloadshop
iTunes
MusicMinutes
MusicStore
Planet
Tiscali
ToostMusic
TuneTribe

NEW ZEALAND
Amplifier
Digirama
iTunes
Ripit*
Txttunes*

NORWAY
CDON
Dagbladet
iTunes
Moox
MSN Music
MusicOnline
P4
Prefueled
SOL
the24
TV2

PHILIPPINES
Fliptunes

POLAND
eMusic
iPlay
Melo
Onetplejer
Soho

PORTUGAL
eMusic
iTunes
Musicaonline
SAPO

RUSSIA
AudioFind
Fidel
mp3.ru
Music Akado
Musicbay*
Nextload*
qton*
Soundkey
Stereokiller*
Yanga
Zakachay

SINGAPORE
Acme Mobile
Apic – Iguana Mobile
Jamba
Mobile1
Orangegum
Pacific Internet
Singnet
SingTel
Soundbuzz
Starhub

SLOVENIA
eMusic
Zabavaj

SOUTH AFRICA
MSN Music
Musica
SAMP3

SOUTH KOREA
Bugs
Cyworld
Dosirak
JukeOn
Maxmp3
MelOn
MTV
Mukebox
MusicOn
Muz
Oimusic
Tubemusic
Wavada

SPAIN
Carrefour
eMusic
iTunes
Magnatune
MSN Music
MTV
MU4US
Terra Pix Box
Wanadoo Jukebox

SWEDEN
Ahlens
Bengans
CDON
eMusic
Gunvor
Homedownloads
iTunes
MSN Music
Musicbrigade
MusicStation
Poplife
Skivhugget
Telia

SWITZERLAND
Ex Libris
i-m Music Download
iTunes
Jamba
MSN Music
Napster
One2Joy
Orangemusic
Soundmedia
Sunrise MusicWorld
Weltbild
ZED

TAIWAN
Ezpeer+
KKBox
MU-MO

TURKEY
MUZI
Powerclub
TTNET*

UK
7Digital
Bleep
eMusic
FOPP
HMV Digital
iTunes
Ministry of Sound
MSN Music
MusicStation
Napster
Tesco
Tiscali
TuneTribe
Wippit

USA
AmazonMP3
Digital
eMusic
iTunes
MusicGiants
MusicMatch
Napster
Puretracks
Rhapsody
Soundbuzz
Univision
Wal-Mart
Yahoo! Music
Zune Market Place

This listing is not exhaustive and is for illustrative purposes only. For full listing see www.pro-music.org

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worldwide

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Published by IFPI, January 2008

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