**Feedback to CMA's Music and Streaming Market Study**

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This supplementary evidence to the CMA investigation is provided by Prof. David Hesmondhalgh and Dr Hyojung Sun who were two of the authors of the *Music Creators' Earnings in the Digital Era* report commissioned in 2020 by the Intellectual Property Office (IPO), which was published as part of the UK government's response to the House of Commons DCMS Select Committee's 2021 report on *The Economics of Music Streaming*.[3] This IPO report (Hesmondhalgh, Osborne, Sun and Barr, 2021) is frequently cited in the CMA Report.

We welcome the CMA's investigation into music streaming. It provides a wealth of valuable information regarding the contemporary recorded music industry. We would like to take this opportunity to provide perspectives and information that we hope you will take into further consideration. We would like to point to what we consider to be significant limitations in three aspects of the CMA Report:

- The CMA Report's treatment of the profitability of the major record companies
- Its treatment of the market power of major record companies with regard to promotion and marketing of music via playlists
- Its treatment of a number of issues in relation to music publishing

## 1. Profitability of major record companies

On a number of occasions in the CMA Report, a reason given for the report's view that limited competition in musical markets is not a cause for substantial concern and/or not worthy of substantial further investigation is "the lack of sustained excess profits of record companies" (for example, in the summary of three factors underlying this view in section 5.31).

We would like to draw your attention to our discussion of UK recorded music profits and costs, which can be found in section 4.2.3 and Appendix 2 of our report (Hesmondhalgh et al. 2021: 122-128, 218-223). This, as far as we are aware, represents the most detailed published discussion of revenues and costs in the UK recorded music industry in recent years, but is not mentioned, let alone discussed, in the CMA report. Nor is there any reference to, or discussion of, the written evidence submitted by economist Will Page to the DCMS Select Committee Inquiry, which provides an indication of very considerable increases in operating profit margins of

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[3] Dr Richard Osborne, Associate Professor in Music and Creative Industries at Middlesex University, was the third member of the team commissioned to produce the report. Dr Kenny Barr (Glasgow University) joined the team at a later point, and was a fourth co-author of the final report. Dr Osborne was on annual leave during the period in which responses could be provided to the CMA Report (we note that this response period was during the school summer holidays).

the three major record companies, from from 8.7% in 2015 to 11.8% in 2019. This evidence is summarised in Figure 4.9 in our report (Hesmondhalgh et al. 2021: 128). Instead, the basis for the CMA report's claims that the major record companies are not achieving sustained, excessive profits is provided in sections 3.30 to 3.32 in the report. This sets Return on Capital Employed (ROCE) against WACC (Weighted Average Cost of Capital). Presumably, the purported evidence that ROCE is only marginally higher than WACC, at least until 2021, is the basis of the claim made that profits are not "excessive".

This may or may not be the case, but our view is that the CMA Report in no way provides sufficient evidence to support this important claim. The report explicitly concedes that, as a result of a number of uncertainties (some of which are given in 3.31) the figures provided as the basis of this claim are "only indicative" (3.32). No transparent discussion of methodology is offered to explain how the WACC figures quoted were arrived at. Instead, the reader is referred only to highly technical sections of the Competition Commission (i.e., the forerunner of the CMA)'s Guidelines, published in 2013. And yet the details to which the reader is referred, in the Guidelines' treatment of "measuring profitability", in Annex A of the Guidelines, are both vague and highly qualified. That Annex specifically refers to the difficulties of calculating value for capital (an important element of the measures used by the CMA in its music streaming report) in the realm of service and knowledge-based industries – and clearly the recorded music industry falls into this category.

A key element of the report and its conclusions is thus dependent on highly technical accounting vocabulary, which is not explained in a transparent way for non-experts. But even for those familiar with the terms and concepts used, this key element of the CMA Report is characterised by important uncertainties and omissions of method and detail. This is extremely disappointing given the considerable emphasis placed by the Report on the claim that major companies' profits are not sufficient to justify further investigation of the sector.

Moreover, there is no comparison of the profits of the major record companies compared with those achieved independent record companies or streaming services, or indeed by musicians/music creators or management companies. There is good reason to think that major record companies achieve much higher levels of profit than those other sectors, suggesting in itself a considerable degree of market power, or at least one worthy of further investigation. Nor is there explicit discussion of what, in the CMA's view, might constitute sustained, excessive profits in these various sectors of the music industries or indeed in any other sector, whether in the cultural and creative industries or beyond.

## 2. Treatment of market power of major record companies with regard to promotion and marketing of music via playlists

The Report downplays the market power of major music companies with regard to promotion and marketing, which are absolutely central to market power in an industrial context where a vast abundance of product is made available to consumers – as is clearly the case with music in the age of streaming. The Report provides fascinating evidence that 42% of streams derive from user-created playlists and 20% of streams from playlists provided by music streaming services (in Chapter 3).

But while recognising the strong presence of content owned by the majors in playlists provided by the music streaming services, the Report dubiously draws from the 20% figure the conclusion that the majors' influence is limited. This is dubious because the key issue with regard to this aspect of market power is not what music is streamed but how people discover the music that they stream. And there is strong evidence that the playlists offered by the music streaming services (rather than those created by ordinary users) are the most significant means of discovering music on streaming (Cook, 2017; Eriksson et al., 2019; Prey et al., 2022). Research has also shown that access to popular playlists is essential for the commercial success of a song (Antal et al., 2021: 8; Hesmondhalgh et al., 2021: 91–93). The most popular playlists are those owned by the majors (Pelly, 2017; Sun, 2019). Studies have provided evidence of how major-owned playlists, such as Filtr (Sony BMG), Digster (Warner), and Topsify (Universal), dominate the playlist discovery and its subsequent impact on streams and income for music creators (Aguiar and Waldfogel, 2018; Antal et al., 2021; Mariuzzo and Ormosi, 2020). It would seem that huge numbers of consumers people discover music, especially new or recent music, from major-owned or on editorial playlists that contain a predominance of major output, and then add their favourite music to their own created playlists. While this issue merits further investigation, it is difficult to see how one could be sure that the majors' market power is limited.

This relates to another problem, concerning the CMA Report's view of the bargaining position of artists. The Report states that "the extent of competition for an artist depends on the popularity of the artist (5.92)" and it goes on to claim that "The stronger bargaining position of some artists appears to be reflected in improving royalty rates and terms… artists are being offered higher royalty rates and shorter contract terms than in the past (5.96)." But the somewhat increased royalty rate for new artists is not in itself sufficient evidence of any significant improved bargaining power for most music creators. How some musicians achieve greater popularity than others, in order to achieve this significant bargaining power, is still unclear. The increased royalty rates may for example be a by-product of the increasing revenues noted by the CMA Report. However, it undoubtedly takes place in a context dominated by the major record companies themselves.

## 3. Issues in relation to music publishing

The CMA Report concludes that "the majors' activities in publishing are unlikely to increase their bargaining position in a material way" (CMA Report, section 5.25). This is based on the Report's assessment of the profitability of the majors (which we have criticised in point 1 above) and on the division of streaming revenues, where the share of the publishing sector has somewhat increased in recent times (CMA Report, section 3.89, drawing on Hesmondhalgh et al. 2021).

As discussed in detail in Chapter 3 of our MCE report (Hesmondhalgh et al. 2021), publishers' share has indeed increased. But more context is needed to assess whether the current share is fair. The publishing share was set at 8% of gross revenues from online music service providers for on-demand music consumption, following a decision by the Copyright Tribunal in 2007. More developments have been made following the introduction of 'option three' licensing which increased the share to 12% in 2012. The low share of music revenues accorded to publishing was traditionally justified, in the analogue era, by the fact that record companies bore the costs for reproduction and distribution of physical artefacts. Following digitalisation, the risk and cost involved in reproduction and distribution have been significantly reduced and some of the cost is now born by the DSPs, yet record companies still achieve a much greater share of revenues than publishers.

This report claims that this larger share is justified because record companies now have to bear "digital global data management and marketing costs over longer effective artist lifetimes (CMA Report, p. 148)," but does not provide concrete evidence of those increasing costs. Increased A&R costs are sometimes given by record companies and their representatives as a reason why the current record share is justified for the record labels, but our report for the IPO found that "the decline in the costs of manufacture and distribution have not been offset by a matching increase in the costs of marketing and A&R" (Hesmondhalgh et al., 2021: 130).

In relation to the bargaining position of music streaming services with major record companies, the report concludes, "A major would still face the risk of losing potentially substantial revenues from a failure to negotiate a licensing agreement with a music streaming service and this would potentially reduce the earnings of artists signed to that major unless the major compensates its artists (5.13)." However, the majors have never failed to negotiate a licensing agreement with a service provider. In fact, there is a lot of opposing evidence, including Rhapsody, e-Music and Grooveshark, all of whom faced the difficulty of obtaining licenses from major labels and some of these services eventually closed down largely due to the lack of popular catalogue. As the CMA Report shows, all successful streaming services have access to full catalogue, without which no music service can survive and this attests to the market power that majors hold.

Lastly, we would like to offer some feedback on the earnings of composers/ songwriters, which the CMA Report concludes are not worthy of concern because composers/songwriters receive a much bigger share than recording artists or performers: "In 2021 the average royalty rate paid to artists by major record companies was 26% whereas the average royalty rates paid by major publishers to songwriters was 84%" (5.123). The CMA Report is right in saying that the increased number of co-writers of songs may explain the reduced earnings of individual composers/songwriters. The report however ignores other factors that relate to the earnings of composers/songwriters, such as the revenue split in which the record labels receive the largest share. The record labels also benefit from the current legal definition of streaming, which is classified as falling under the making available right, a right granted under UK and international copyright law that applies when content has been made available in such a way that it can be accessed at a specific time, and place, of the user's choosing.[4] Under this definition, streaming is understood as

[4] This right was introduced first in Article 10 of the WIPO Performers and Phonograms Treaty (WPPT) 1996 and adopted in the EU (which then included the UK) in the 2002 Information Society Directive. In the UK, it was enacted in 2003 by adding it to the Copyright, Designs and Patents Act 1988.

a reproduction (or a sale) justifies 52% of the streaming share. However, this is not without criticism. For a stream to be classified under the making available right, the listen should be interactive, chosen by a user at a certain time. As the streaming business evolved, playlists have become the most dominant form of music listening, and some of the playlists involve passive listening, which does not involve any interactivity from a user. In this case, many would argue that playlists could be more appropriately classified as akin to a broadcast. Such a reclassification would potentially result in increased income for composers and songwriters. Advocates of such a change argue that the major labels' market power has made it difficult to bring it about, even though it would be beneficial for songwriters. This important issue is surely worthy of greater attention than it was given in the CMA Report.

With regard to the CMA Report's view that "the majors' activities in publishing are unlikely to increase their bargaining position in a material way" (Section 5.25), we note that the recording sector makes more profit than the publishing sector, and so, for major companies with stakes in both recording and publishing, it is preferable to pursue a higher revenue share for recording than for publishing. This was manifested in our MCE report (Hesmondhalgh et al., 2021: 83–85) in the form of contrasting views between major publishers and the independent publishers, in which major publishers and the major labels are of one voice in emphasising the increased share given to the publishers, whilst independent publishers argue that the current share is not sufficient.

Finally, the CMA Report suggests the increased acquisition of rights serve as new means for some songwriters of earning income (3.57). Although it is true that the acquisition of song publishing catalogues may offer songwriters new earnings, it is a moot point whether this necessarily helps most songwriters in the long term. It tends to favour the most popular songwriters historically. We therefore believe it is not appropriate to use this as an example to demonstrate that the welfare of songwriters is not a problem in the current environment.

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