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**An Overview of the Financial Impact of the Canadian Music Industry**

**Executive Summary**

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## **Executive Summary**

Assessing the true value of music is more than a dollars and cents accounting of the sectors that make up the “music industry”. Music is a central, pleasurable part of everyday life, and intrinsically is not conducive to valuation in narrow monetary terms. But even the accounting exercise of tallying revenues and costs in the music industry is not straightforward. A number of questions immediately arise. How should the music industry be defined? Does the music industry include just the production and sale of recorded music and revenues from live performances? Should the definition be more encompassing and perhaps include users of music, such as broadcasters, and facilitators of the creation of music, such as musical instrument producers and distributors? Is the sale of devices that record music part of the “music industry”?

This study represents a first step toward measuring the direct economic impact of the Canadian music industry. The industry is defined broadly to include the production and sales of recorded music, music publishing, live performances, the use of music in radio broadcasting, and musical instruments and lessons. Existing data from publicly available sources, as well as previously private data and new data collected through original surveys, information gathered with the assistance of industry associations, key informant interviews, and information provided by some of the music rights collectives are presented to begin a sketch of the monetary size of the Canadian music industry. While the primary focus of this study is on the economic impacts of the music industry, it merits noting that non-monetary impacts of the industry, particularly as revealed through the proposed surveys and interviews, are also presented.

The study should be seen as a work in progress. There are some critical components of the music industry for which data are not available and which this study was not able to generate. With the best efforts of all of those who shared their data and experiences in order to advance the study, it is clear that there are some important limitations to the data that underlie this study. Feedback on where the analysis falls short, where data sources have been missed, or where data have been misinterpreted is most welcome.

### ***Musicians and Composers***

The music industry begins with the creators of music -- musicians, songwriters and composers. Some musical artists are able to make a living working in music on a full-time basis. Fewer still achieve substantial earnings, and accumulate sizable wealth, from their talents. But for many musicians, a career in music may not be a full-time vocation and may also not be particularly remunerative. There has been very little information available on the work arrangements, earnings and expenses of musicians, songwriters and composers, at a national level, in Canada. This section of the report provides some of this information for a sample of Canadian musicians.

Data on musicians were collected using a web-based survey conducted by POLLARA, with the cooperation of the Canadian arm of the American Federation of Musicians. Informing the design of the survey were interviews with artist managers who provided background on categories of musician revenue sources and expenses, as well as a number of other issues addressed by the survey. The survey was web-based and was conducted during December 2006 and January 2007. In total, 700 musicians, songwriters and vocalists responded to the survey.

The musicians who responded to the survey were primarily American Federation of Musicians (AFM) members, all of them in Canada. It is important to note that a Canadian musician is not required to be a union member to perform or record. While there does not appear to be information available on the number of musicians who are not union members, key informants who provided information for this study suggested that non-union members would number in the thousands. That the survey largely addressed AFM members is a potentially important caveat for interpreting the survey results. Because of a lack of information on non-unionized musicians, there is no basis for evaluating whether the results for the sample of unionized musicians is representative of all musicians.

It should also be noted that, based on the earnings information, there were not any “superstar” musicians in the sample. Nonetheless, the survey results will hopefully provide some perspective on the circumstances of an important segment of the Canadian musician community.

The Musicians Survey paints a portrait of Canadian musical artists as being active in a wide array of endeavours (e.g., live performances, recording, studio work, licensing activities and advertising and commercial work, among others). The talents of Canadian musicians also span a multitude of musical genres.

Live performances represent the single most important source of income for musicians in the sample, accounting for 48.5 percent of the average \$24,837 of total revenues earned by Canadian musicians. On average, Canadian musicians incurred \$8,346 of expenses, a quarter of which (\$2,112) was due to transportation costs and a further 17.8 percent (\$1,486) accounted for instrument purchases.

For the average musician in the sample, their music career is a part-time vocation, consuming 27.8 hours in a typical week. Sixty-five percent of musicians have other jobs in which they work for pay. The annual earnings from this other employment averaged \$20,758.

About 71 percent of musicians view unauthorized file sharing as either a major threat (37.6 percent) or a minor threat (33.3 percent) to the music industry, while 15 percent believed it to be no threat at all. Some 37.6 percent of respondents generally agreed that unauthorized file sharing was bad for artists, while 14.1 percent agreed that unauthorized file sharing isn't bad for artists. Almost a third (34.4 percent) of musicians in the sample viewed unauthorized file sharing as both good and bad for artists. Sixty-seven percent of musicians in the sample believed that copyright owners should have complete control, 27

percent believed the artist should have some control and 1.4 percent believed the artist should have very little control over the use of an artistic work.

Canadian musicians expressed optimism about the future. Eighty-four percent of musicians reported being either optimistic (62 percent) or neutral (22 percent) about their future prospects as a musician. Only 16 percent of musicians described themselves as pessimistic.

### *Live Performances*

Many of the music industry professionals with whom we spoke over the course of this study emphasized the growing importance of live performances, not just as a source of income, but also as one of many tools for building a fan base. This is especially the case in an era where radio play, according to some, has become a less effective tool for new musicians to attain popular recognition or for music fans to discover new music.

As described in the previous section, the Musicians Survey revealed that Canadian musicians depend on live performances for a sizable share – almost one-half – of their music-derived earnings. This section provides information on three key aspects of the live musical performance business. First, the role of agents and the financial arrangements of live performances are described. Second, data from the consumer survey of Canadians' assessment of their expenditures on live performances is presented. Finally, the gross receipts from live performances in Canada are estimated based upon SOCAN live performance copyright tariff revenues (and other sources).

Most Canadian musical artists rely upon themselves for management, but at least some use the services of agents to assist with booking live performances. Booking agents typically receive commissions equal to 10 percent of whatever the artist receives. Canadian booking agent revenues are estimated to be in the \$11 million to \$13 million range, with agent profits equal to between 10 to 15 percent of revenues.

The Consumer Survey undertaken by POLLARA asked Canadians about the extent of their attendance of live performances. Forty-eight percent of Canadian respondents, and an identical proportion of Ontario respondents, indicated that they had attended live shows or live concerts that were primarily musical, including live theatre shows and operas.

Respondents were also asked how much they had spent on live musical performances in the past 12 months. Those Canadians who had reported attending live performances spent an average of \$273 in the past 12 months, slightly less than the \$299 reported by Ontarians who had attended live performances. Averaged across all Canadian and Ontario respondents (i.e., including those who had not attended live performances as well as those who had attended live performances), expenditures on live performances were reported to be \$122 and \$131, respectively.

Consumers' recall of their expenditures on live performances over a 12 month period is prone to inaccuracy. Extrapolating the figures on live music performances based upon the average reported expenditures to the population level results in implausibly large total expenditures. One potential source for estimating at least a (sizable) share of some live performance ticket sales is to use information on SOCAN domestic licensing fees. Statistics Canada also provides some information that can assist with estimating classical music concert and musical theatre revenues.

Gross revenues from live musical performances in 2005 are estimated at \$752.8 million, the bulk of which (\$353.4 million) was derived from general concerts, with the remainder accounted for by classical music concerts (\$312.0 million), musical cabarets (\$80.9 million) and exhibitions (\$6.5 million). While not estimated in this study, there are considerable secondary expenditures for food, beverages, merchandise, parking and a range of other goods and services complementary to the enjoyment of music in these venues.

### ***The Recording Industry***

This section of the report brings together information on trends in Canadian recording industry sales, expenditures and profits from three sources: Nielsen SoundScan Canada unit sales data; Statistics Canada's Sound Recording Survey; and new data for major record labels provided by the Canadian Recording Industry Association (CRIA).<sup>1</sup> Unfortunately, a survey of independent Canadian record companies undertaken for this study generated too few responses to provide reliable information on the independents.

The circumstances for Canadian recording companies, as a whole, have changed markedly in recent years. Over the 1998 to 2007 period, CD sales peaked in 1999 at 62,763,500 units. Unit sales of CDs declined by 26.3 percent between 1999 and 2003. Unit sales rebounded modestly in 2004, but still remained 21.1 percent below 1999 levels. Unit sales fell in 2005 from the 2004 level, and continued to decline at accelerated rates to 2007. In 2007, CD sales totaled 41,801,900 units, a 9.6 percent drop from 2006 sales, and 33.4 percent below the 1999 peak for this period. Unit sales for 2007 were below those for the previous low over the period, 46,243,000 units, in 2003.

Retail sales of recordings in Canada declined by 51.2 percent over the 1998 to 2006 period, from \$1,441.5 million in 1998 to \$703.7 million in 2006.

Since the entry into the Canadian market of the Apple iTunes store at the end of 2004, sales of digital albums have been growing. However, digital album sales are not yet fully offsetting the decline in physical CD unit sales. In 2006, 1,029,000 digital albums were sold in Canada, along with 14,887,600 digital singles. Nielsen SoundScan converts digital singles into digital album-equivalents by assuming that there are 10 songs per

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<sup>1</sup> CRIA purports to cover about 96% of all recorded music sales in Canada, including indie sales (they are the primary sales channel of indie sales).

album. Consequently, the 14,887,600 digital singles represent 1,488,760 digital album equivalents. In total,  $[1,029,000 + 1,488,760 =]$  2,517,760 digital albums and equivalents were sold in 2006.

Physical album sales in 2006 totaled 45,205,700 units. When added to digital sales,  $[45,205,700 + 2,517,760 =]$  47,723,460 albums and digital equivalent albums were sold in 2006. By this approach, digital sales accounted for  $[2,517,760 / 47,723,460 =]$  5.3 percent of all unit sales in 2006.

Following the same methodology, digital sales as a proportion of all unit sales increased to 10.3 percent in 2007.

The causes of the decline in CD sales have been hotly debated. A recent study by Liebowitz<sup>2</sup> considered a number of factors that might explain the decline in United States record sales including (at page 21), "... album prices, income, music quality (measured by concerts and radio listenership), markets for substitutes and complements, the opening of new listening venues (portability) and "librarying" – the act of replacing replenishing album collections as formats change, such as replacing prerecorded cassettes with CD's." Liebowitz also assessed the impact of the pre-recorded video market on music sales. Liebowitz argues that these factors played little or no role in the decline of CD sales.

Professor Liebowitz also examined the literature on the impact of file sharing on record sales in the U.S. and concluded that, "The weight of current evidence strongly supports a view that file sharing diminishes the revenues of the recording industry."<sup>3</sup>

While not everyone agrees on the causes, it is evident to most that the traditional recording industry in Canada has been in an extended period of decline. Sales of physical forms of music have declined and digital sales of music have increased, the increase in digital sales has, to date, been insufficient to offset the fall in physical sales.

#### Statistics Canada sound recording survey data

Core recording revenues of the Canadian industry as a whole (i.e., both Canadian and foreign-controlled recording companies) grew between 1992/93 and 1998, from \$658.9 million to \$961.9 million, followed by an erosion in core recording revenues to \$762.1 million by 2003. The Canadian recording industry also saw revenues from industry-related activities increase from \$752.2 million to \$1,193.4 million in 2000. Industry-related revenues declined to \$985.4 million by 2003. Total revenues, including revenue from non industry-related activities, increased from \$828.2 million in 1992/93 to \$1,323.9 million in 1998, but total revenues were reported to have fallen in each of the 2000 survey (to \$1,319.3 million) and the 2003 survey (to \$1,029.7 million). EBITDA increased from \$147.8 million in 1992/93 to \$250.0 million in 2000, declining to \$123.5 million in the 2003 survey. The EBITDA margin generally declined between the

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<sup>2</sup> Liebowitz, Stan J., "File Sharing: Creative Destruction of Just Plain Destruction? *Journal of Law and Economics*, vol. XLIX (April 2006), 1-28.

<sup>3</sup> See [www.utdallas.edu/~liebowit/](http://www.utdallas.edu/~liebowit/).

1992/93 survey and the 1998 survey (from 17.8% in 1992/93 to 15.5% in 1998), increasing to 18.9% by the 2000 survey. In 2003, EBITDA as a proportion of total revenues equaled 10.7%.

Data for 2005 and 2006 which, due to changes in the Statistics Canada survey methodology, are not comparable to the earlier data, suggest continuing downward pressure for the Canadian recording industry as a whole.

Total operating revenue for Canadian- and foreign-controlled companies combined fell from \$747.3 in 2005 to \$690.6 million in 2006, a decrease of 7.6 percent. Operating expenses fell 3.4 percent over the same period. Operating profits fell from \$102.2 million to \$67.5 million, while the operating margin shrank 3.9 percentage points, from 13.7 percent to 9.8 percent.

#### Major label data

The financial profile of the major recording labels in Canada diminished markedly over the 2001 to 2006 period. Total sales (total sales include sales from all sources – CDs, cassettes, DVDs, digital, distributed label fees and royalty income) fell from \$666.0 million in 2001 to \$624.4 million in 2003. Sales rebounded in 2004, rising to \$653.4 million, but fell dramatically in 2005 to \$522.1 million. Sales improved modestly in 2006, rising \$16 million to \$538.1 million. By 2006, major label sales had fallen by 19.2 percent from the level achieved in 2001.

The decline in sales was also reflected in decreased expenditures in Canada by the majors, as well as slowing net new capital asset additions. In 2001, expenditures totaling \$321.4 million, representing 48.3 percent of sales, were paid directly to Canadian suppliers and staff members. By 2006, Canadian expenditures had fallen to \$221.3 million, a 31.1 percent reduction from the 2001 level. Canadian expenditures were 41.1 percent of sales in 2006.

Additions to capital assets fell by 83 percent between 2001 and 2006, from \$7.5 million to \$1.3 million.

#### ***Music Publishing***

A recent study prepared for the Canadian Music Publishers Association (CMPA) and L'Association des professionnels de l'édition musicale by Paul Audley & Associates Ltd. and Circum Network Inc. (hereafter the "music publishing" study) provides very comprehensive information on the roles of music publishers and copyright collectives in Canada. In addition, the study provides detailed financial information on Canada's music publishing industry.

This chapter summarizes the study and adjusts the figures from the original study to provide an estimate of the financial impact of some of the major, but not all, music publishing activity in Canada.

Canadian music publishers earned over \$103 million in revenues in 2004. The two largest categories of royalty revenues, mechanical rights and performing rights, accounted for \$49.2 million and \$43.8 million, respectively. “Other” revenues of \$10 million were primarily derived from synchronization (\$7.6 million). Music publishers’ expenses amounted to 86.1 percent of total revenues.

Recently published Statistics Canada data for the music publishing industry for 2005 and 2006 show that operating revenues increased by 8.0 percent from \$107.4 million in 2005 to \$116.0 million in 2006. A 15.8 percent increase in operating expenses resulted in a 32.1 percent decrease in operating profits, from \$17.6 million to \$11.9 million. The operating profit margin fell from 16.4 percent to 10.3 percent.

The relative magnitude of the sources of music publishing revenues is likely to have changed from the 2004 study. Mechanical rights royalties are very likely to have declined, in line with declining unit sales of compact discs. Digital reproduction rights revenues (i.e., royalties collected on downloaded singles and albums) are likely to have only partially offset the decline in physical mechanical rights royalties.

The private copying regime was in its infancy during the period relevant to the original music publishing study. Consequently, it might also be reasonably expected that private copying tariff revenues have increased in both magnitude and relative importance to music publishers.

### ***Music Consumption***

This section of the report presents recently collected data on music buying as represented by a sample of Canadians. While specific information on expenditures must be treated with caution in light of challenges faced by survey respondents who are required to recall information from an extended period of time in the past, consumers’ responses offer some perspective on tastes and buying habits, as well as future intentions to purchase music.

The data on Canadian consumers are from a survey conducted by POLLARA. The Music Consumers Survey was administered via telephone between August and September of 2006. The survey collected information on the consumption of recorded music, musical instruments and training and attendance and expenditures on live performances. While this section of the report focuses primarily on the information about music consumption collected through the survey, information collected on the consumption of other music-related products and services is presented in other sections.

The Canadian consumers in the sample were asked how often they listened to various genres of music. The most popular genre, classic rock, was frequently (i.e., as often as possible) listened to by 32.1 percent of respondents, while 20.5 percent reported that they never listened to classic rock. For the following music genres, at least 50 percent of survey respondents listened either frequently or occasionally to: Classic rock (62.6 percent); adult contemporary/soft rock (57.4 percent); and rock performers (51.6 percent). Opera and dance music were never listened to by 61.1 percent and 59.2 percent, respectively, of the sample of consumers.

Almost three-quarters of respondents purchased at least one CD or music DVD in the twelve months prior to being interviewed; however, fewer than 20 percent had purchased a downloaded music file. Respondents also reported purchasing ring/mastertones for their cellular telephones: just under 20 percent of cell phone owners purchased a ringtone or mastertone. About 30 percent of respondents purchased gift certificates for music. Only about 10 percent of these purchases were redeemable with on-line music services.

This section also provided some information on the amount of money that consumers spent on recorded music products. However, because of the difficulties associated with recalling amounts spent on past purchases, these figures cannot be reliably used to estimate the music purchases of the Canadian population.

### ***Commercial Radio Broadcasting***

Commercial (and public) broadcasters make considerable use of music in the provision of their services. Perhaps the most obvious use of music for broadcast purposes is radio, though other broadcasters are also extensive music users. Other broadcasters who use music include basic and cable television, as well as pay audio services for home listening or as background music in restaurants, taverns and other public spaces. There are also relatively new and emerging broadcasting technologies, such as internet radio, satellite radio, WiMax, and even podcasting, which have the potential to be both complements and substitutes for terrestrial radio broadcasting. Together, the technologies serve to expand the use and reach of music.

Although radio stations may be playing more music today, it is apparent that Canadians are listening less to radio than in the past. Nonetheless, commercial radio broadcasters have demonstrated remarkable resiliency, as reflected in their financial performance, even in light of new and competing technologies such as MP3 players, satellite broadcasting and webcasting to name a few.

With total revenue growth of 5.7 percent compounded annually over the period 2001 to 2005 (from \$1.070 billion in 2001 to \$1.039 billion in 2005), and a total cost compound annual growth rate (CAGR) of 4.3 percent (from \$857.6 million in 2001 to \$1.015 billion in 2005), the profitability of the Canadian commercial radio broadcasting industry improved over the period. Earnings before allowance for interest, taxes, depreciation and amortization (EBITDA) increased from \$212.0 million in 2001 to \$317.3 million in 2005,

a CAGR of 10.6 percent per year. Expressed as a percentage of revenue, EBITDA profits were equal to 23.8 percent of revenues in 2005, up from 19.8 percent of revenues in 2001. Earnings before interest and taxes (EBIT) increased at a CAGR of 12.8%, from \$171.2 million (or 16.0 percent of revenues) in 2001 to \$277.0 million (or 20.8 percent of revenues).

Although the Ontario commercial radio broadcasting industry experienced slower revenue growth over the 2001 to 2005 period than did the Canadian commercial radio broadcasting industry as a whole, it experienced slower growth in expenses as well. So, at approximately 20 percent of revenues, Ontario broadcasters experienced EBITDA margins that were similar to those of all Canadian commercial radio broadcasters. EBITDA margins expanded to 27.2 percent of revenues in 2005, compared to 23.8 percent for Canada as a whole. EBITDA of Ontario commercial radio broadcasters increased from \$81.7 million in 2001 to \$135.3 million in 2005, a CAGR of 13.4 percent. EBIT increased from \$65.5 million (or 16.3 percent of revenues) in 2001 to \$120.8 million (or 24.3 percent of revenues), a CAGR of 12.8%.

Music continues to be a critical input to commercial radio broadcasting. Despite the apparent longer-run trend of less time spent listening to radio, especially by younger Canadians, differences in music listening preferences continue to provide efficiently segmented audiences that attract the interest of demographically targeted advertisers.

The financial performance of commercial radio broadcasters in Canada has remained strong, with revenues, profits and profit margins all expanding over the 2001 to 2005 period.

### ***Musical Instruments, Recording and Live Performance Equipment, and Music Lessons***

Although largely overlooked in music industry studies, Canadian sales of musical instruments, recording equipment and public address and lighting systems now rival those of recorded music.

This chapter provides statistical information on the economic and financial profile of this key infrastructure sector of the music industry. Also provided is some information, taken from the survey of Canadian music consumers, on purchases of music lessons and musical instruments.

While some of these music products are destined for the professional market, sales to professional musicians alone would not be sufficient to sustain the industry. The music products industry relies on the non-professional market – primarily young people who are learning to make their own music, either as part of a school program, or outside of the school system through private instruction. Also, as the population ages, the music products industries expect to see the continuation of a trend toward the older demographic groups reinvigorating their interest in recreational music making. Recent

experience in the industry has seen older Canadians either picking up an instrument for the first time or, perhaps more commonly, returning to a musical instrument that they had explored when they were younger and had either lost interest or lacked time in light of other pursuits. As more of their time becomes their own again, many older Canadians have moved from passive listening to participating in making their own music.

Canada is the seventh largest market in the world for music products, with retail sales exceeding \$900 million in 2005. While professional musicians account for some of these sales, the industry relies on individual “recreational” musicians for the bulk of sales. Measured on a *per capita* basis (i.e., retail sales of music products divided by population), Canada ranked second in retail sales of music products. On average, each Canadian spent over \$29 on music products in 2005, second only to Americans, who spend almost \$32 each. The average per capita spending on a global basis in 2005 was \$7.68 expressed in Canadian dollars (or \$6.34 U.S.)

The music products industry has been experiencing steady growth over the past decade. In 2005, the retail sales of Canadian music products suppliers totaled just over \$924 million (expressed in Canadian dollars), rivaling retail sales of recorded music.

Canada is a significant importer of music industry products. According to the Music Industries Association of Canada (MIAC), approximately 10 percent of retail sales are attributable to Canadian-based manufacturers, or about \$94 million dollars in 2005. Further, Canadian manufacturers exported in the range of \$80 million to \$100 million of music products to the rest of the world.

#### Consumption of musical instruments and lessons

The musical products industry relies on individual music enthusiasts, more so than professional musicians, for their customer base. The Consumer Survey administered by POLLARA collected information on the purchase and rental of musical instruments. Specifically, the survey asked Canadians whether, during the past year, they had bought or rented a musical instrument for themselves or someone in their family. Twenty-three percent of all Canadians, and 24 percent of Ontarians, reported having purchased or rented a musical instrument, with 30 percent of those who did purchase or rent a musical instrument indicating that the instrument was for someone else in the family. The remainder purchased or rented the instrument for either themselves or both themselves and others in the family.

About thirty percent of those who reported spending on musical instruments were not able to recall how much they spent. About 40 percent of all Canadians, and an equal proportion of Ontario respondents, spent less than \$300 on instruments, while 33 percent of Canadians and 28 percent of Ontarians reported expenditures in excess of \$300. Those Canadians who bought or rented musical instruments in the past year reported spending \$664 (\$608 in Ontario).

Many of those purchasing musical instruments also purchased sheet music and other support materials to accompany their musical instruments or lessons. The average expenditure by all Canadian musical instrument buyers/renters was \$59. The average expenditure on these items for Ontario instrument buyers/renters was \$39. It merits emphasis that almost 40 percent of all Canadian, and Ontario, musical instrument consumers reported having spent nothing on sheet music and support materials in the past year.

It has proven extraordinarily difficult to find information on how much Canadians spend on musical instrument lessons and/or voice lessons. Consequently, the Consumer Survey asked respondents to indicate whether they had purchased music lessons or singing lessons for themselves or for someone in their family during the last year. Fifteen percent of all Canadians and 13 percent of Ontarians purchased such lessons, with about 62 percent of both all Canadians, and only Ontarians, reporting that they purchased the lessons for just themselves or for both themselves and other family members. The remaining 38 percent of lesson buyers purchased the lessons for another family member.

Those Canadians purchasing music/voice lessons for themselves spent \$578, compared to the \$512 spent in the last year by Ontario music lesson purchasers. Among those purchasing music lessons for other family members, the average amount spent was \$439 (\$326 in Ontario). Thirty percent of Canadians who purchased music or voice lessons, and 40 percent of Ontarians, reported paying nothing for those lessons.

The Consumer Survey provided information on the purchase of musical instrument and voice lessons for themselves and family members, the purchase or rental of musical instruments and the purchase of support materials, such as sheet music. While the amounts Canadians reported spending for each of these categories must be treated with caution due to the difficulty of recalling such expenditures, the information suggests that a considerable proportion of the Canadian population is actively engaged in making, or learning to make, music.

It should be noted that the majority of costs associated with music education in schools and post-secondary institutions are unlikely to be captured in the responses of survey participants.