Industry Research
G00217238

Media IAS Online Music Forecast, 2011-2015: Social Media, Subscriptions and the Cloud

Published: 16 September 2011

Analyst(s): Mike McGuire, Stephanie Baghdassarian

As consumers opt for connected devices — media tablets, smartphones and connected media players — across world regions, their desire for access to and consumption of music and content is growing as well. Music labels, artists, publishers and new distribution intermediaries are developing new business models to address consumers' changing behavior.

Key Findings

- Online music revenue from end users will grow more than 31% by the end of the forecast period: from $5.9 billion in 2010 to $7.7 billion in 2015. By comparison, consumer spending on physical music (CDs and LPs) is expected to slide from around $15 billion in 2010 to around $10 billion in 2015.
- Online music subscription services, such as Spotify, will be the main growth sector in this market, showing fivefold growth from 2010 to 2015. A la carte sales will drive the bulk of overall revenue.
- The highest growth rates will be in regions such as Latin America and the Middle East and Africa, which have not historically been strong in paying for tracks or albums from online services or stores (although perhaps stronger in paid-for ringtones from their service providers).

Recommendations

- Online music service providers (retailers or subscription service providers) must continue to invest in compelling shopping or consumption experiences that provide search, discovery, recommendation and taste-sharing capabilities. These efforts must be tightly integrated with efforts to extend service, via applications, to popular devices.
- Service providers or online retailers need to find ways to integrate the right balance of social media tools into their solutions: to either drive purchase transactions or reinforce the value of subscription services. Communications service providers (CSPs) could mine opportunities for tracking consumption, assuming they can avoid concerns around privacy and "net neutrality" issues.

Table of Contents

List of Tables

List of Figures

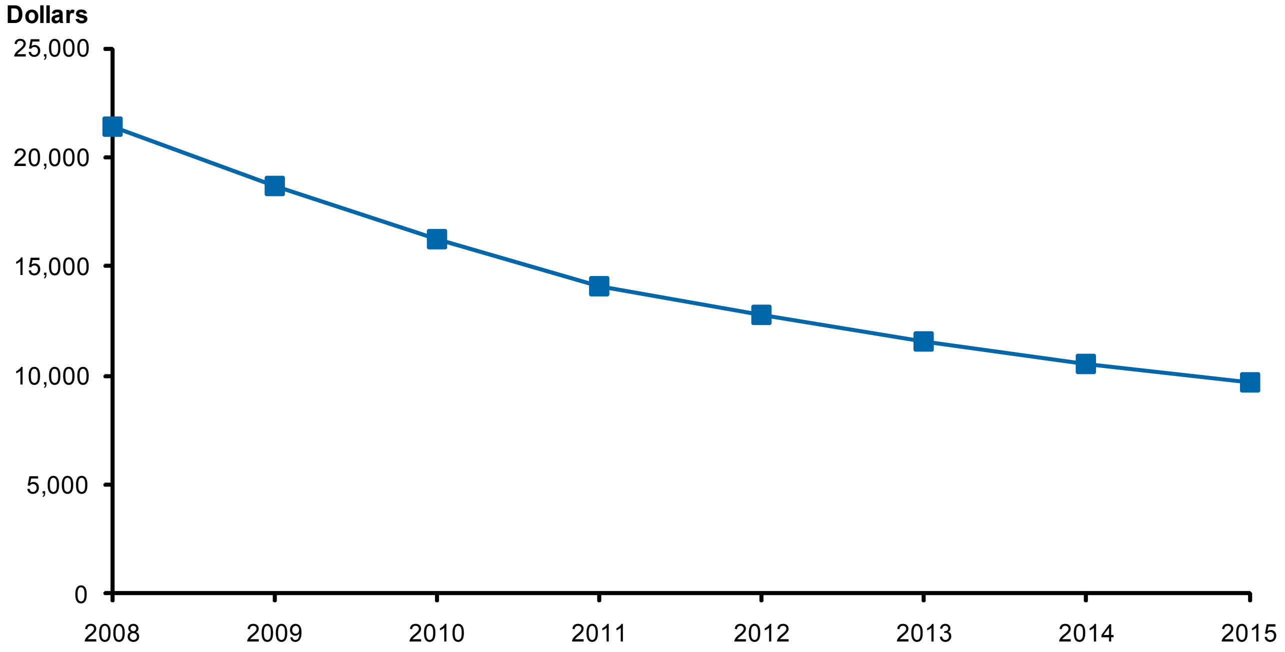
Analysis

Introduction

As the first media sector to feel the full impact of two major forces — the Internet and technology-empowered consumers — the music industry has staggered through the first decade of the 21st century, and entered the second bedraggled financially and facing a powerful set of intermediaries, which are creating borderless global ecosystems that defy the industry's previous notions of control and monetization.

The primary stakeholders in the music industry — artists, music labels, publishers and retailers/ service providers — are facing wrenching changes and a somewhat uncertain future. But the next four to five years, as portrayed in our forecast portends solid growth — if you ignore the continued decline of CD sales described in Figure 1.

Figure 1. Physical Music Sales (CDs, LPs, etc.) 2006-2011



Source: PricewaterhouseCoopers Global Media Outlook, 2011-2015

The downward trajectory of CD sales is still a significant source of discussion and business tactics within the industry. We are not addressing it directly in our forecast. Gartner is focusing exclusively on consumer spending for online sources. The online sector within the music industry is where the strategic focus needs to be (and it finally appears that is the focus) as it has emerged from a somewhat shaky start in the 2000s to become the growth engine of the music industry.

In this research, we highlight the Gartner online music forecast, the key drivers and inhibitors, and provide recommendations for key stakeholders.

Forecast Data

Industry bodies, such as the International Federation of the Phonographic Industry (IFPI), report that revenue for the total recorded music market has been on the decline for 10 years. CD sales, the largest revenue stream for the industry, have eroded, while (in parallel) the online music revenue share is rapidly increasing.

After digital downloads, streaming music services — referred to in this forecast as subscription services — are the clear driver in the online music industry for the coming years. Gartner estimates that subscription services will account for nearly one-third (29%) of end-user online music spending in 2015 (see Table 1).

Table 1. Online Music End-User Spending by Type of Service, Worldwide, 2008-2015 (Millions of Dollars)

	2008	2009	2010	2011	2012	2013	2014	2015
Subscription Services	203.6	252.7	353.3	532.1	808.9	1,210.6	1,700.8	2,218.4
Download Services	2,709.0	3,107.3	3,367.9	3,629.8	3,847.4	3,952.2	4,003.2	4,050.3
Personalization Services	1,823.4	2,016.0	2,166.8	2,172.8	2,141.2	1,958.3	1,723.1	1,460.9
Total	**4,736.0**	**5,376.0**	**5,888.0**	**6,334.7**	**6,797.6**	**7,121.2**	**7,427.1**	**7,729.6**

Source: Gartner (September 2011)

This forecast looks at revenue generated from online music, and includes end-user spending from:

- Subscription services — From any device, and whether the service allows streaming of music tracks (owned or not owned by the user) available from the provider's server or from the user's selected location (such as a PC or media center).
- Download services — In which consumers pay per track, or per album, from online retailers such as Apple's iTunes and Amazon. Unlike subscription services, most a la carte direct sales do not use content protection or digital rights management (DRM) to control how consumers use the content. This means that consumers can move the content from device to device. Online store operators and third-party service providers are creating online cloud storage lockers that will enable consumers to back up their collections to a cloud account, greatly simplifying device-library management for consumers.
- Personalization services — The ringtones and ring-back tones that consumers pay for to use on their mobile devices. Typically, these can be acquired directly from service providers and synched to the mobile phone over the air, or can be acquired via a PC or connected device and then synched to the mobile phone.

Some Thoughts About Cloud Storage

One important court case and some service provider maneuvers are bringing more focus to nascent "cloud music" market, a market Gartner believes will comprise two distinct flavors: personal cloud entertainment services, which, in the case of music, include subscription services such as Spotify, MOG, Rhapsody and Rdio; and cloud storage lockers, such as those offered by Google and Amazon, and Apple's forthcoming iCloud offering. These features allow consumers to create cloud-based backups of their digital music files, no matter their origin (ripped CD or social CD ripping for file-trading systems).

While Amazon's and Apple's implementations are tightly tied to their online music stores, Google's, thus far, is a stand-alone service (actually it's more like a feature of a nonexistent music service than it is a stand-alone service). With Google and Amazon, users can get applications for their smartphones or media tablets that enable the streaming of files in their cloud locker. According to press reports, Apple will enable the same capability with its Match service ($24.99 per year) that will hold up to 25,000 song files. Now, the difference is that Amazon and Google force the user to literally upload copies of their music libraries to the cloud account. Apple, however, has reportedly struck deals with the labels and rightsholders so that the iCloud service, via its forthcoming Match feature, can scan the user's main iTunes music library, and if iTunes has licensed the same songs/albums, iTunes will populate the user's Match account with those songs/albums, instead of going through the network-intensive step of moving files between the user's PC and the cloud. Gartner believes this is the kind of offering one can do by engaging directly with the labels.

However, a recent court decision in the case of a suit brought by label EMI against MP3tunes has apparently cleared the way for cloud-locker services such as those from Google and Amazon to allow consumers to store their music files in a cloud account without requiring licensing deals from rightsholders. EMI filed a copyright infringement suit against MP3tunes for, among other things, allegedly facilitating copyright infringement by the service customers. While there were many issues in the case that were not decided, the judge found that cloud storage locker service providers are not responsible for the alleged copyright infringements of their users, so long as the service provider removes infringing content at the request of the copyright holder (the "safe harbor" exemption in the Digital Millennium Copyright Act). For all cloud storage locker providers, Amazon and Google included, this removes one legal uncertainty for their services. Whether or not labels and publishers will challenge those companies in court about the streaming capability remains an open question.

As the shift from physical to digital music content quickens across the world, different regions are at different stages (see Table 2).

Table 2. Online Music End-User Spending by Region, Worldwide, 2008-2015 (Millions of Dollars)

	2008	2009	2010	2011	2012	2013	2014	2015
North America	2,332.9	2,462.2	2,531.8	2,565.5	2,589.9	2,606.3	2,621.8	2,635.8
Western Europe	925.7	1,086.0	1,236.5	1,393.6	1,543.1	1,637.9	1,723.1	1,808.7
Asia/Pacific and Japan	1,351.1	1,612.8	1,825.3	1,995.4	2,202.4	2,350.0	2,510.4	2,666.7
Rest of the World	126.2	215.0	294.4	380.1	462.2	527.0	571.9	618.4
Total	**4,736.0**	**5,376.0**	**5,888.0**	**6,334.7**	**6,797.6**	**7,121.2**	**7,427.1**	**7,729.6**

Source: Gartner(September 2011)

- Online music in North America is maturing, so double-digit growth rates will be harder to maintain, and we expect to see solid, but flat, growth over the next five years. In the meantime, the territories being covered in the "Rest of the World" category will see very strong growth and will increase their share of the world's market from 5% in 2010 to 8% in 2015.

- Western Europe, Asia/Pacific and Japan will see similar growth, although not for the same reasons.

Top-Line Assumptions

- Gartner believes that the growth opportunities in online music are driven by the popularity of connected devices — mobile phones capable of playing back music files and/or accessing online streams. Gartner believes that, while antipiracy efforts will continue, the music industry is realizing that experimentation with business models and legitimate alternatives to file trading are better long-term investments to fuel much of this growth.
- North America is the most advanced market. Since the U.S. is the single biggest market for online music, Gartner assumes that growth rates here will slow, while less mature markets will see growth in online music revenue as Internet access and connected device penetration rates increase.
- Western Europe, Asia/Pacific and Japan have a different profile in terms of the types of online music options that consumers prefer. Historically, consumers in Western Europe have preferred downloading and streaming options. Consumers in South Korea and Japan have rapidly adopted mobile streaming and downloads — ahead of PC-based streaming or download options. South Korea, India, China and Indonesia have all seen the success of mobile personalization. These broad regions will grow their share of the market during the next five years.
- As far as the type of music is concerned, download-to-own services are more mature and still deliver more revenue than other online or mobile music models. We expect that their growth will slow down as more consumers begin to turn to subscription services that are leveraging the popularity of consumer smartphones, media tablets and, in the future, devices such as TVs with Internet connectivity built in. These services will leverage their ability to combine paid access to streams, a recent shift in licensing priorities by the music labels that will enable subscription services to let paying subscribers cache content on the device (these services use DRM to protect the cached content) to enable offline access. We include advertising-supported Internet radio services with this class of offerings — for example, Pandora, which offers advertising-supported and monthly subscription options (although our focus is on the end-user spending, rather than on the advertising revenue).
- We also assume that personalization content (such as ringtones and ring-back tones) will lose importance during the forecast period, as mobile devices become smart enough for users to use their own tracks as ringtones, rather than paying for specific files to deliver the services. The success of ring-back tones has been seen mostly in Asia and parts of Africa, and thanks to the smartphone's features, these are less easily replaced. The slowdown in the personalization segment is, therefore, related to cultural preferences and the evolution of smartphone penetration at the country and regional levels.

More specifically, Table 3 highlights the opportunities for online music — from demand and supply perspectives.

Table 3. Opportunities in Online Music Revenue Generation

Demand Side	Supply Side
Music consumption still ranks high in consumer surveys — What has declined is what consumers are ready to pay for when it comes to music consumption in the form of bundles of content on CDs, for example.	**Legitimate online music applications and services proliferate —** The number of legitimate online music services and stores is currently greater than 400 worldwide, according to the IFPI. Increasing numbers of players are partnering to put these services together and to address the various segments of consumers: from music solution providers to the device manufacturers and Internet service providers.
Consumers are making the shift to online — Digital sales and revenue from online music services and stores was the only sector that grew during 2010, both on a global basis and in the U.S. (the largest market for prerecorded music sales and revenue). However, as noted in Figure 1, while CD sales are declining, they still generate the most revenue for the industry. It might seem that only a few stragglers still bother with CDs, but the online music market is still in its adolescence.	**The shifting attitudes and practices of music labels toward DRM —** While DRM has been removed from virtually all download services, it is still being used to protect application-based services. However, the consumer usage models of these services are far more flexible than they were in the early days of online music.
Proliferation of connected devices — Music consumption in the past decade has moved from dedicated devices, such as CD players, radios, vinyl turntables or dedicated MP3 players, to being an Internet-capable media type that can be consumed across a host of dedicated and general-purpose devices with Internet connectivity. In particular, the popularity of smartphones and the anticipated popularity of media tablets have created a whole new set of ways for consumers to discover and consume music. Longer term, the evolution of connected TVs and open set-top boxes (such as Roku and Apple TV) promises the ability to extend music subscription services, such as Deezer, MOG, Rdio and Rhapsody, to TV screens and living room audio systems.	**Multiple monetization opportunities —** The re-emergence of subscription services demonstrates both the entrepreneurial spirit of the executives launching these services, and the stubbornness of music labels and publishers in making the subscription model and all its benefits (to labels, publishers and rightsholders) into a steady, predictable revenue stream from users who cannot easily redistribute the content.
Social media and social networks — The advent of these networks extends the promotional opportunities for music labels and artists; adding another layer of tools for online music services and stores to leverage in their efforts to grow their customer bases. Music labels, artists and artist management teams are all looking to leverage social media tools	**Cloud technology investments —** Major companies with significant brands, deep technology assets and expertise are investing in online music services as part of their broader media service developments. Google, Amazon, Apple and Microsoft, to cite a few, are all investing in online music, either directly or indirectly. Apple in particular, given its dominance of download sales, is usurping the cloud concept to extend the value

Demand Side	Supply Side
and social networks to create new monetization opportunities. However, the true business value to music industry stakeholders of social media and social networks is still unclear. One of the more persistent questions Gartner receives, at least on the Media IAS team, is "What's the (business) value of a Facebook like?" for social gaming, offerings such as Farmville seem to draw a fairly clear picture on the business value. For music, however, it's still a fuzzy picture. Companies such as RootMusic are building platforms aimed at helping artists manage and monetize their social network presence on services such as Facebook. But we are still in the early days of this sector's development, so expect to see much more activity in this space.	of the iTunes store and its ecosystem of devices. One important licensing hurdle Apple cleared was in securing a "redownload right" from labels and publishers, which enables iTunes users to synch content to their devices via their iCloud accounts without having to physically connect the devices to their computers. Google and Amazon offer their own versions of cloud storage and lockers. Amazon's is linked to its download store, but Google's, at the moment, is merely a cloud locker that enables the user to stream songs from their accounts to their Android devices or to their computers via the Google Music Manager application.
	Music industry attempts to streamline licensing processes — The most recent effort is the Global Repertoire Database. Some music publishers, and service providers, such as Apple, are collaborating to develop a system that will streamline the licensing of content across multiple regions. However, these efforts are likely to take many years. Equally important has been the slow, but steady, recognition (by the music labels and publishers) that efforts to streamline the licensing process need to be complemented by a significant change in attitude from the labels and rightsholders — to relax some of the more stringent and expensive licensing terms and requirements that characterized the early days (2000 to 2008) of the online music market.
	Technology-driven innovation — Search, discovery and recommendation technologies are proliferating, and music labels, artist managers and artists are looking to technology companies and developers to provide crucial measurement and infrastructure services (for example, single-sign-on using social network IDs to access online and mobile services), audience engagement and metrics.

Source: Gartner (September 2011)

On the other hand, the market for online music services also faces many challenges to its development, including:

- **"Free" content —** Piracy and person-to-person file-trading, while not currently in the headlines as much as in the recent past, remain problematic for the music industry. A significant number of consumers will always try to obtain music (among other content) for free, creating a constant inhibitor to any forecast on revenue. However, the overlapping worlds of social media, social networking and online music seem to be creating new and compelling content experiences for which consumers are willing to pay.

- **Tracking and accounting for music sales and consumption —** Licensing and publishing challenges will continue to inhibit the ability of services to cover regions quickly. For online music services, or the music-based applications that depend on licensing content and then playing it back to consumers in some manner, the licensing challenges only *start* with the labels and publishers. Beyond those groups are the performing rights organizations (PROs).
- **Key stakeholders in transition —** Music labels, publishers and PROs are in the midst of significant ownership transitions (between labels and publishing arms), while PROs (which differ from country to country) are at various stages of automating the processes used to track consumption and pay out to their clients. Together, these factors will add time and complexity for new service providers.
- **Tension caused by the inherent asymmetry of information about consumers and their behavior —** As the music industry looks to monetize online distribution and social networks — or at least define the business value of social networks — one of the key challenges will be the acquisition, management and analysis of consumer behavior around the discovery and acquisition of music and music-related content or transactions. In this regard, the industry is making some efforts, but there are still some very basic datasets the labels and artists can't readily access. For example, getting information from online services about their audiences — beyond sales and subscriber numbers — remains a challenge. Companies such as Topspin are developing platforms and processes that band management and artists can use to track and assess their online presence and social graphs. Gartner expects this tension to increase, not decrease, over the short term.

Conclusion

As online distribution revenue starts to overtake physical revenue — which will happen beyond our forecast horizon of 2015 — Gartner believes the stakeholders in the music industry will continue to realign their businesses to maintain their places in the value chain. Consumers are likely to continue to take advantage of the applications, devices and services that provide them with multiple ways of discovering, consuming and communicating about music. Moreover, as more and more music-related transactions, such as concert ticket sales and merchandise, see most — if not all — of their business moving online, online music services, downloads or subscription services will have to find ways to make those related transactions available to their customers.

The essential element — the thing that will affect the fortunes of any number of stakeholders in the music industry, is how each sector addresses consumer data (behavior patterns, and how consumers find and share data about music and information). This issue in particular will likely remain a point of contention among labels and artists and the online music services. However, Gartner believes that an important step to consider — that might lessen this tension — would be for stakeholders to agree on some low-level, broadly beneficial standards, such as extensions of OpenID, to minimize the number of times a consumer has to proffer an ID/password for multiple social media tools. Gartner believes prospective service providers, such as communications service providers, should consider how they can apply the authentication and subscription- and account-management practices (built up over decades) to these sorts of challenges.

For music labels, artists and publishers, challenges abound. However, there remain real opportunities to reinvent the business based on consumers who are adopting connected devices (that marry playback and purchase acquisition capabilities in a single device) and who are showing they will pay for content in multiple ways. These sorts of changes offer the potential for many new types of service and business models aimed at allowing music fans to manage and access their music libraries while also integrating social media and content payment options. In particular, CSPs should focus business development investigations into the potential for providing managed services options — such as cloud storage — as part of their consumer-facing services. However, CSPs must balance these potential opportunities with a careful examination of how any deployment addresses consumer concerns over privacy and "net neutrality" issues.

Methodology

Forecast Components

This forecast relies on one top-level global online music end-user spending forecast, subject to two further splits:

- **Online music end-user spending by type of music —** Breaking down subscription services (serving streams and cached tracks on devices), downloads and personalization services. It has to be noted that personalization services include ringtones and ring-back tones (but not monophonic ringtones, which tend to disappear). These get reported by the music industry, even though they are about customizing mobile devices, rather than about entertainment.
- **Online music end-user spending by region —** Showing a Western Europe, Asia/Pacific and Japan, and North America breakdown, and a fourth category grouping together the rest of the world's regions.

Top-Level End-User Spending

Based on historical data reported by the music industry (mostly IFPI and the main record labels), we established a global online music market size for the end of 2010 and previous years. We then applied a forecasting model, taking into account assumptions on how the global recorded music market will decline and how the digital share will grow during the next five years.

Type of Online Music

The 2010 split between the various types of online music is the result of initially breaking out personalization services based on data reported by the music industry (IFPI). The next level of split, between download and streaming services, is estimated based on the number of services available in each category and the maturity of these services. Downloads have been on the market for longer and are available from bigger players; the main one being Apple, with its iTunes store.

Based on our assumptions (as defined in the main section), we decreased the share of personalization services across the forecast period, looking at a decrease not only in the share, but also in the absolute value. The download services' share of the market has also been decreased, while maintaining growth in the absolute end-user spending value for those services.

Regional Split

To establish the regional split for online music revenue, we used various historical data reports from music industry players, together with other data points, such as:

- The U.S. is the single biggest market, followed by the U.K.
- Japan and South Korea are generating online music revenue, but essentially from mobile devices. Personalization services are also very popular in Asia/Pacific.

Based on our assumptions, in terms of the maturity of online music services across regions and the propensity toward music piracy, we forecast growth opportunity at the regional level — also looking at Internet penetration and the sheer size of those regions in terms of population.

Recommended Reading

Some documents may not be available as part of your current Gartner subscription.

"Online Music Trends: Social Media, Subscriptions and the Cloud"

"Predicts 2011: Media Incumbents and Insurgents Fight for Online Dominance"

"How U.S. Consumers Use Search and Discovery Tools to Find Music on the Internet"

Regional Headquarters

Corporate Headquarters
56 Top Gallant Road
Stamford, CT 06902-7700
USA
+1 203 964 0096

Japan Headquarters
Gartner Japan Ltd.
Aobadai Hills, 6F
7-7, Aobadai, 4-chome
Meguro-ku, Tokyo 153-0042
JAPAN
+81 3 3481 3670

European Headquarters
Tamesis
The Glanty
Egham
Surrey, TW20 9AW
UNITED KINGDOM
+44 1784 431611

Latin America Headquarters
Gartner do Brazil
Av. das Nações Unidas, 12551
9° andar—World Trade Center
04578-903—São Paulo SP
BRAZIL
+55 11 3443 1509

Asia/Pacific Headquarters
Gartner Australasia Pty. Ltd.
Level 9, 141 Walker Street
North Sydney
New South Wales 2060
AUSTRALIA
+61 2 9459 4600