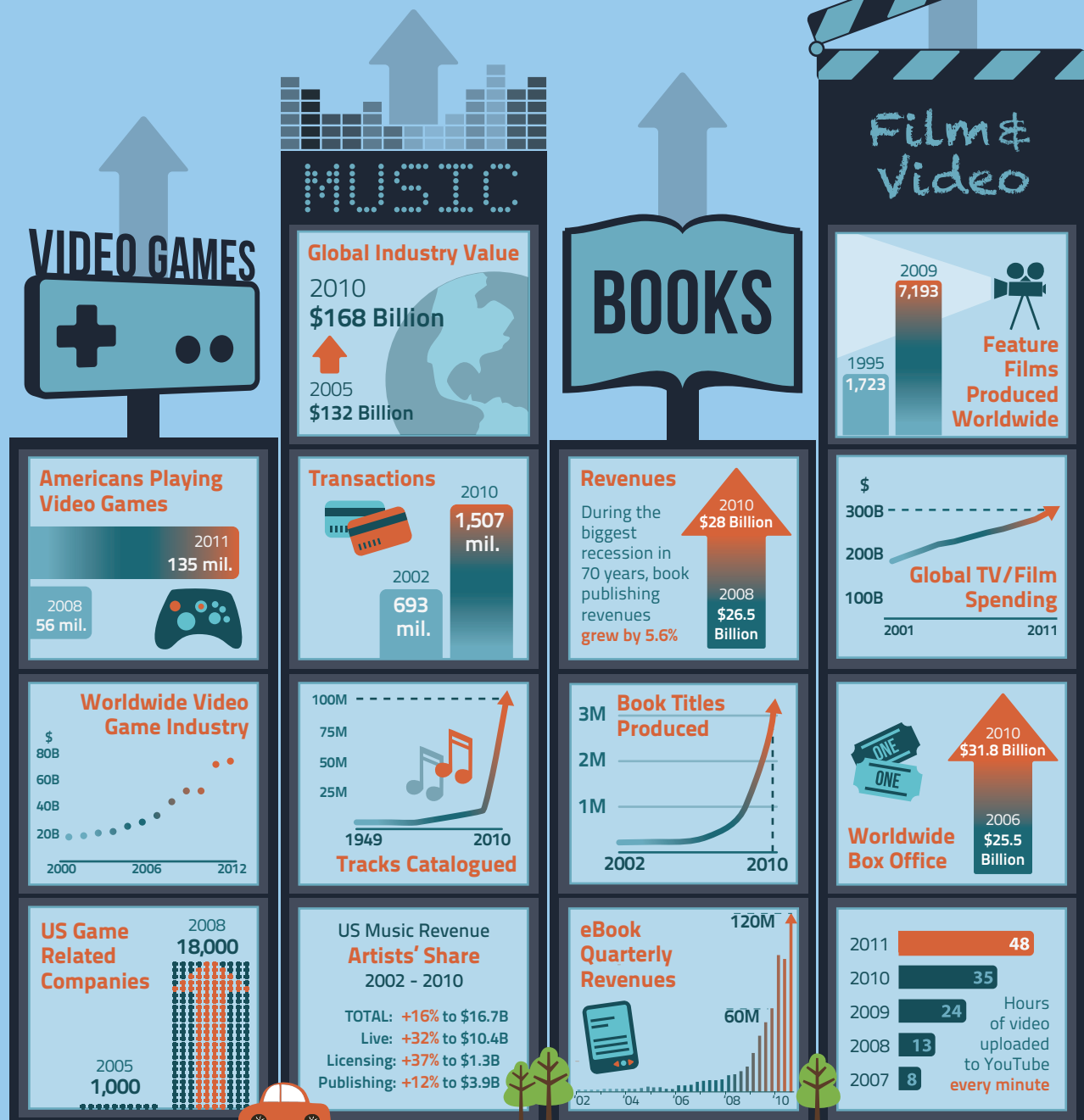


THE SKY IS RISING!

BY floor 64

Contrary to the dire warnings of the legacy entertainment industry players, the market is booming, with ever greater content choices for consumers, more options for creators, and many more opportunities for smart businesses & artists to make money.

THROUGH A DECADE OF ECONOMIC AND TECHNOLOGICAL UPEHAVAL, THE ENTERTAINMENT INDUSTRY **GREW 50%** WHILE CONSUMERS **INCREASED SPENDING** ON ENTERTAINMENT



To promote the **Progress** of the Science and useful Arts...

SOURCES: BLS, BookStats, Game Developer Research, Gartner, Gracenote, IBISWorld, IDATE, IDPF, IFPI, ISBN, MPAA, Nielsen SoundScan, Parks Associates, PRS, PwC, Schwann's Catalog, TESA, The UNESCO Institute for Statistics, YouTube.com

The Sky is Rising

A DETAILED LOOK AT THE STATE OF THE ENTERTAINMENT INDUSTRY



Computer & Communications Industry Association
1972-2012: 40 YEARS OF TECH ADVOCACY



Engine Advocacy

JANUARY 2012

MICHAEL MASNICK

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Executive Summary

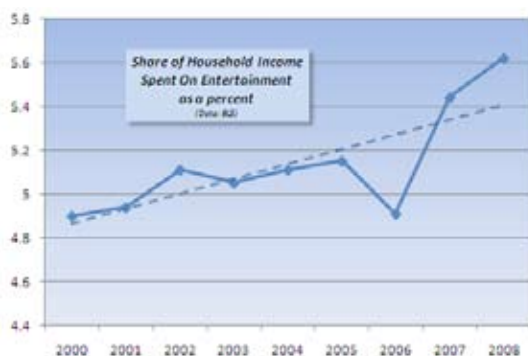
Has the internet decimated the entertainment industry, or are we living in a new renaissance for both content creators and consumers? Depending on who you talk to, you may have heard both stories.

This report explores the **true** state of the entertainment industry and concludes, quite simply, that the sky is not falling on the entertainment business, consumers or content creators themselves. Instead:

The Sky is Rising

In fact, what amazed us in going through every bit of data and research we could find, was how utterly consistent the results were: the wider entertainment industry is growing at a rapid pace (contrary to doom & gloom messages). Furthermore, more content creators are producing more content than ever before -- and are more able to make money off of their content than ever before. On top of that, consumers are living in a time of absolute abundance and choice -- a time where content is plentiful in mass quantities, leading to a true renaissance for them. This *does* present a unique challenge for some companies used to a very different market, but it's a challenge filled with opportunity: the overall market continues to grow, and smart businesses are snapping up pieces of this larger market. The danger is in standing still or pretending the market is shrinking. Therein lies the real threat: missing out on all that opportunity.

Indeed, you wouldn't know it, just listening to the entertainment industry talk about how much the entertainment industry is "dying," but data from PricewaterhouseCoopers (PwC) and iDATE show that from 1998 to 2010 the value of the *worldwide entertainment industry* grew from \$449 billion... to \$745 billion. That's quite a leap for a market supposedly being decimated by technological change.



Of course, the world economy grew over this period of time, but a particularly compelling bit of data shows that, in the US specifically, consumer spending on entertainment as a percentage of income has **continued to rise** significantly over the last decade. According to the Bureau of Labor Statistics, in 2000, 4.9% of total household spending went to entertainment. That number gradually increased over the decade -- and by 2008, it was up to 5.62%, an increase of nearly **15%** in the same decade as the internet went mainstream. In other words, for all the reports that people

just want stuff for free, and are not willing to spend on entertainment, the actual data shows that they're spending noticeably **more** on entertainment today than they did ten years ago.

Similarly, reports of job losses in the sector are equally hard to square with reality. Once again, looking at the Bureau of Labor Statistics data, employment in the entertainment sector grew nicely in the decade from 1998 to 2008 -- rising by nearly 20% over that decade. The BLS continues to predict

similar growth for the next decade as well. Perhaps even more importantly, during that same period of time, BLS data shows that the number of people who were *independent artists* grew at an even faster rate -- over 43% growth in that same decade. In fact, this may be a strong hint as to why you hear reports of industry "demise" from certain legacy players: because new technologies and services have made it much easier for content creators to find success without going through the traditional gatekeepers. It also raises questions for those who claim that the changing marketplace has been most difficult for independent artists. The data simply does not back that up.

Finally, if you look at just about any area of the entertainment industry today, the amount of new content being produced has grown at a tremendous rate. In 2002, less than a quarter of a million new books were available on the market. By 2010 that number was over 3 million. In 2001, the Gracenote database had data showing just about 11 million song tracks. By 2010, that number had passed 100 million. According to the UN, in 1995, there were about 1,700 films produced worldwide. By 2009, it was more than 7,000. Meanwhile, during this same period of time, the video game industry ballooned massively, leaving its niche status behind, and becoming a major part of the wider entertainment industry.

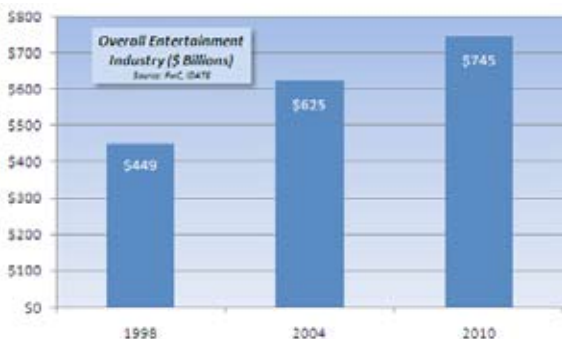
By any measure, it appears that we are living in a **true Renaissance era** for content. More money is being spent overall. Households are spending more on entertainment. And a lot more works are being created.

And yet, all we hear about is how the internet has decimated the entertainment industry.

Of course, for pretty much the entire history of the entertainment industry, there have been complaints about how almost any new technological innovation is a form of "piracy" that will represent the end of the wider industry. From John Philip Sousa insisting that "*These talking machines are going to ruin the artistic development of music,*" to the music industry fearing that radio had similarly destroyed the industry by decreasing the "life" of a song "from 18 months to 90 days," leading radio to "virtually plug up" the old system, to Jack Valenti's infamous prediction that the VCR would be to the film industry "what the Boston Strangler was to a woman at home," the industry has predicted its own demise each and every time a new technology has come along.

It's no different today, with the rise of the internet.

In the past, **every single one** of these predictions proved wrong. Instead, far from killing the entertainment industry, every single one of these innovations massively expanded the industry -- providing new and incredibly valuable abilities to create, distribute, promote and monetize their works.



The data in this report show that it is no different today. The internet has helped the wider entertainment industry grow and thrive, benefiting both consumers and content creators in massive ways.

This report seeks to dig in to the numbers to understand, more

clearly, what is truly happening in the entertainment industry. It looks closely at four sectors: film & video, music, books and video games, and discovers that each one has been growing quite nicely over the last decade. It explores how much of this growth is driven by the internet and new opportunities that the internet allows.

The comprehensive picture highlights a few key points:

1. For consumers, today is an **age of absolute abundance** in entertainment. More content is available in more ways than ever before. If we simply go by the terms of the US Constitution's clause from which copyright came, it seems clear that the "progress of science and the useful arts" is being promoted -- even as copyright is often being ignored or foregone. There is just a tremendous amount of content, a tremendous variety of content, it's more accessible to more people than ever before.
2. For content creators, it is an **age of amazing new opportunity**. Traditionally, to take part in the entertainment industry, you had no choice but to go through a gatekeeper, which served to keep the vast majority of people who wished to be content creators from ever making any money at all from content creation. Today, that is no longer true. More people are making more money from creating content than ever before -- with much of that coming via new tools that have allowed artists to use the internet to *create, promote, distribute and monetize* their works.
3. For the traditional middlemen, the internet **represents both a challenge and an opportunity**. There is no doubt that the internet has eaten away at some traditional means by which these businesses made money. But, as the data shows, there is more money going in to the overall market, more content being created, and many new ways to make money. That shows that there is a business model challenge -- and a marketing challenge -- but much more opportunity in the long run. The key challenge for business is in figuring out how to capture more of the greater revenue being generated by the wider entertainment industry. Legacy players certainly face a lot more competition (and fewer reasons that artists have to do deals with them) -- which can explain some of the public complaints about the "death" of various industries -- but overall, it's clear that by embracing new opportunities, there are plenty of ways to succeed.

Throughout the rest of this report, we explore the specifics of these three points in great detail, highlighted with brief "case studies" of content creators who appear to have figured out some of the key secrets to succeeding in this market -- capturing an increasing slice of the growing pie by really embracing what the technology has created. It's a story of a rapidly changing market -- but a story of success and opportunity at every turn for those who understand how to properly embrace the changes.

What comes out is undeniable -- despite some parties insisting otherwise. The amount of money and content in the entertainment industry has always trended upwards. The opportunity levels are tremendous. The real challenge is for creators and companies to figure out how best to capture that opportunity -- especially in the face of growing competition. But, absolutely nowhere is there any suggestion that the overall entertainment industry is at risk. Instead, it is clear. The sky is rising to incredible new heights.

Opportunities Abound: Enablers, Not Gatekeepers

One of the key lessons in the gradual shift in market power in the entertainment industry these days is that the power of the old gatekeepers is declining, even as the overall industry grows. The power, instead, has definitely moved directly to the content creators themselves, who no longer need to go through a very limited number of gatekeepers, who often provide deal terms that significantly limit the creator's ability to make a living.

Instead, what has happened is a major new opportunity has opened up, not for gatekeepers, but for organizations that enable artists to do the different things that the former gatekeeper used to do -- but while retaining much more control, as well as a more direct connection with fans. Three great examples of this are Kickstarter, TopSpin and Bandcamp.

At the close of 2011, Kickstarter announced that, over the course of the year, just about \$100 million had been pledged to artists through its crowdfunding platform. While not all of the pledged money goes to successful projects, the company projected that approximately \$84 million did, in fact, make it to those content creators whose projects were successfully funded. Kickstarter works by giving artists a way to let fans crowdfund the creation of new works. That is, rather than being a platform for directly buying a work already created, it lets artists offer different tiers through which fans can help fund a project, in the hope of reaching a funding threshold for the work to be created. Only after the threshold is met does the money change hands.

All sorts of creative works are funded via Kickstarter, and in 2011, over \$32 million was pledged to film & video, almost \$20 million was pledged to music, over \$5 million pledged to publishing, and nearly \$4 million pledged to games. And, of course, Kickstarter is just one of a number of similar platforms. However, this shows that not only are consumers willing to support many artists when given the chance, but that there are new business models that get around the traditional gatekeepers. One of the key reasons for going with a traditional player was to get that initial funding to create the art. But platforms like Kickstarter, IndieGoGo, PledgeMusic and others route around the old players.

TopSpin is an interesting player that provides tools to content creators (musicians, filmmakers, authors and more), to allow them to more easily create a direct-to-fan relationship via their website. This includes that ability to stream, sell or offer up downloads (sometimes with conditions), but also the ability to sell merchandise and things like direct concert ticket sales.

In the most recent data released from TopSpin, the average transaction price they saw was \$26. And when an offer included a ticket for a live event, the average shot all the way up to \$88. And the number appears to be rising. A year earlier, TopSpin noted that its average transaction price was about \$22. What this shows, again, is that people are willing to spend if artists offer the right thing -- and it suggests that fans are even more willing to spend higher amounts when they know the money is going directly to the artists, rather than into a large company who may never pay royalties. That suggests a big opportunity in artists going increasingly direct to fans, rather than completely giving up revenue streams to gatekeepers.

Finally, a third player in the space, Bandcamp, lets musicians set up simple content stores for their works (and also allows for streams, pay-what-you-want, free or conditional downloads). While not as big as Kickstarter, the company recently announced that, for just the month of December, it helped artists make over a million dollars. Perhaps the most interesting statistic there is that when given the option of paying-what-you-want for albums with a suggested price, an impressive 40% of the time, fans are willing to pay more than the suggested price.

Obviously, these new players are smaller than the old gatekeepers today. But the trend lines are important, as are what the data shows. The key point is that new businesses, which act as enablers rather than gatekeepers, are springing up to allow the artists to be central to the process, and not limit their ability to make a career out of their works. And those enablers can be effective for those who use them well.

Furthermore, the data from each of these enablers suggest that consumers are willing to spend, and they're often willing to spend more, if they feel that they're really getting something of value and there's a direct connection to the artist.

Case Study

Louis CK: Open, Human & Awesome

At the end of 2011, comedian Louis CK presented a perfect example of how an artist could release content and make money in new and exciting ways. He made a one-hour special of a live performance of his new stand-up routine, but rather than go the traditional route of making it into a TV special, a DVD or a CD, he decided to release it directly to his fans on the internet, for a simple \$5 payment.

He focused on making the process as absolutely seamless as possible: payment was easy (you didn't have to sign up for anything) and the files had no DRM to lock them up or make things difficult. You just paid and got the video.

But what was much more interesting was how he went about marketing this and getting people to buy. He chose to truly connect with people by being open, human and awesome.

The first part that made it work was that him being open. In launching the deal, he explained the situation, explained why he was doing things the way he was (and that it was an experiment) and explained why he hoped you would buy it. He didn't hide the fact that you could almost certainly get it for free online through unauthorized means. He just explained why he hoped you would choose otherwise. On top of that, he later was exceptionally open in explaining the results of the experiment -- highlighting not just how much he made (including a screen shot of the PayPal account), but also explaining his expenses and exactly how he was going to distribute the money. This kind of openness made people even more willing to pay.

Second, he was human. He didn't come across as corporate or fake. He came across as authentic and human. He did so by being polite and even relating some of his fears and thoughts as he went into the experiment. In addition, on the same day he released this video, he went on the popular discussion site Reddit, and ran a question and answer session (called an AMA -- for "ask me anything") where he chatted with tons of fans, all while explaining why he was doing what he was doing. The commitment to do that, and to answer all sorts of questions in a really human fashion, endeared people to him even more. This was entirely different than a traditional roll out with a big marketing campaign that obscures the real people behind the content. It also meant not treating fans like criminals, but as fans. He was always very appreciative of the fans in all of the interactions. As a way to compete with "infringement," this really helps because people felt a connection with a human being, rather than that they were being sold to by a faceless corporation.

Finally, there's the point that Louis CK is an awesome comic. This is an important point that gets missed in discussions of these business models: Don't Forget To Be Awesome (which is also the name of a small independent record label, who seems to get these things too). Louis has built up a well-deserved reputation over the years as a comic among comics -- one of the best there is. The reviews of the actual video were also quite high. No content is going to be successful if

the quality isn't there. You can have the best business model in the world, but if your content is no good, it's unlikely to work. In some cases, those who are complaining about failures of business models may actually need to look more closely at the content itself. But if the content is awesome, then you have one of the key ingredients needed.

The results for Louis CK were fast and obvious. Within 12 days, he had made over \$1 million from this experiment -- more than he'd made from any of his previous video efforts. On top of that, Louis CK continued his "open, human and awesome" strategy by not just sharing the results, but by announcing plans to both give his team large bonuses and donate about a quarter of the income to charities -- some chosen by fans who had suggested them online. Louis CK demonstrates a perfect case study of how you can be quite successful even in the face of the easy nature of infringement: make things cheap and easy, but also make sure to connect by being open, human and awesome.

Section 1: The Video Market

The industry surrounding video media is divided into distinctly separate categories: film/movies, television and the “catch-all” silo of online video. These video market categories correlate with the variety of production budget sizes (blockbuster films generally have bigger budgets than TV shows), business models (TV relies more on advertising instead of ticket sales), distribution logistics and other operational variations. Despite the differences between all these visual works, however, there is obviously plenty of crossover between them, as TV shows are re-written into movies, as movies are shown on TV, and as nearly all forms of video eventually end up online.

Starting with the film industry, it’s not too hard to see that the popularity of movies has grown steadily over its century-long history. Despite economic recessions, the movie industry generally continues to attract sizable audiences to theaters -- and the business has been called “depression proof,” owing to the fact that, even during the depths of the Great Depression, movie-goers numbered between 60 and 80 million Americans per week (when the US population was about 122 million). However, the industry did have its share of problems in the 1930s, but it survived and thrived with innovative marketing tactics, such as door prizes, matinees and midnight screenings, and discounted ticket prices to get people into theater seats.

More recently, the movie industry has also been dubbed recession proof, due to the box office ticket sales that have held up rather well in comparison to other industries. In 2008, DreamWorks Animation CEO Jeffrey Katzenberg said, “Both traditionally as well as recently, we have seen that our product is, at worst, recession-resistant and, more optimistically and historically, has actually been recession-proof.” Additionally, according to the MPAA, total worldwide box office ticket revenues have increased by 25%, from \$25.5 billion in 2006 to \$31.8 billion in 2010.

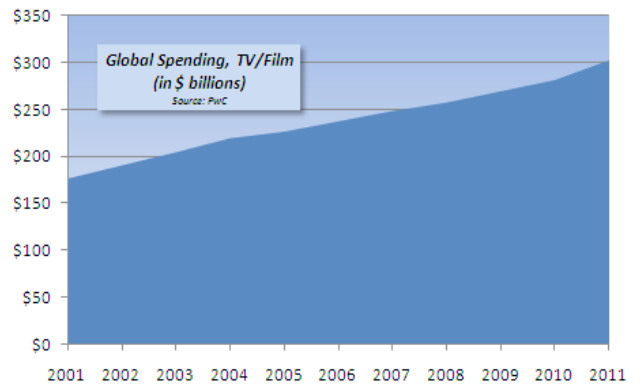
year	US & Canada (\$ Billions)	Worldwide (\$ Billions)
2006	9.2	25.5
2007	9.6	26.2
2008	9.6	27.7
2009	10.6	29.4
2010	10.6	31.8

According to PwC reports that include movie revenues beyond just box office ticket sales, the film industry has grown worldwide by almost 6% over the five-year period from 2005 to 2010,

exceeding approximately \$82 billion in value. For an industry that claims to be plagued by piracy, this steadfast level of growth during the Great Recession appears to justify the boastful statements of being recession proof.

Looking at the worldwide production of films, the UNESCO Institute for Statistics

(an organization that serves the United Nations) has been keeping track of various cultural events, such as quantifying the number of feature-length films produced, in a survey of over a hundred countries since 1995. Interestingly, the USA is not the largest producer of feature-length films and has not held that title for many years. (The US film industry is still the largest in terms of box office revenues, however.) India's Bollywood produces well over a thousand films per year, making it the most prolific film-making nation. (India comes in at third with box office revenues of \$2.2 billion in 2010 behind the US's \$10 billion and Japan's \$2.5 billion, and China has only recently surpassed the \$2 billion threshold.)



Next on the production list, Nigeria's Nollywood has taken second place in the race to produce movies, churning out nearly a thousand films per year aimed at a thriving home theater market. (Nigeria actually produced more films than India circa 2007, but India has since re-claimed its number one spot.) Obviously, the US movie industry has many more well-known films than any other country, but it comes in third on the list of movie-making nations with roughly 700 feature-length movies made each year. Overall, these production numbers don't suggest any kind of a slow down in the production of movies. In

fact, part of the reason for Nigeria's impressive movie figures is that the cost of film production is remarkably low -- less than \$100,000 -- and Nigerian movie-makers have been adept at keeping their budgets low while expanding their audience reach. And as the costs of digital video production continue to decline, the global film industry looks very healthy as more audiences can be reached more easily and more cheaply.

year	# of feature films produced globally
2005	5635
2006	5255
2007	6416
2008	7020
2009	7193

In addition to feature-length films, there are also a wide variety of shorter movies that are not so well accounted for. The most provocative example is the adult film industry which is often cited to be a multi-billion dollar market, but exact numbers for it are difficult to confirm. In 2001, Forbes published an estimate that assumed around 13,000 video releases were created every year and pegged the entire US porn industry to be valued at less than \$4 billion. The widespread piracy of these types of movies is putatively ubiquitous, but despite this copyright infringement, predictions for the demise of the adult film market seem to be dismissed easily, given that the demand for adult entertainment seems to be going strong.

Other films that deserve to be mentioned are independent films that don't generate mainstream box office ticket sales. In 2011, the Sundance film festival received around 4,000 entries, and independently-financed films are being produced with renewed vigor as production costs have dropped. Crowdfunding sites like Kickstarter or PirateMyFilm have encouraged more and more filmmakers to try to produce short films in unique ways -- such as movies filmed entirely with cell phones or using iPhones or made in under 2 days (or in less than 24 hours). Furthermore, independent films have found more and more outlets to reach viewers at home with services like Netflix, LoveFilm, FilmBaby, Fandor, etc. With the cost of both production and distribution falling dramatically, different options for watching movies are more widely available than ever before, which creates an environment where a low budget film can potentially become enormously popular. Examples like

Case Study:

Ed Burns' Newlyweds: Back To The Roots; Simple, Cheap & Good

Ed Burns was an extremely successful independent filmmaker, kicking off his career with the Brothers McMullen, which is considered one of the most successful indie films. Made for about \$25,000, it brought in over \$10 million -- and gave Burns a path to success in the traditional Hollywood studio system. In fact, he appeared in a few Hollywood films, but has continued to stick close to his indie roots.

While some "indie" filmmakers are indie-in-name only (still signing huge deals, but doing it outside traditional major studios), Burns has really been testing out all sorts of new ways of making, marketing and selling indie films. His most recent film really shows the amazing ability to make a high quality film on the cheap. The *Newlyweds* cost a grand total of \$9,000 to make -- with most of that money going to the actors involved. He used a basic DSLR camera that just about anyone can buy, but which looks incredibly professional. Outside of that, they used natural light wherever they could, and sought out locations that wouldn't cost money (such as asking a friend who owns a restaurant if they could film there as a favor).

One of the big questions that is asked about filmmaking in this day and age is how can big studios recoup \$200 million budgets. Burns has flipped that question on its head, and asked why must budgets be so big. In an era of cheaper and better tools, it's possible to make fantastic movies for much less money. It's then significantly easier to profit off of those movies.

The end result is a lot more people making a lot more films -- and more of those films making more people money. It may not lead to more \$200 million films, but it's unclear if the world really needs that many such films.

Paranormal Activity, *The Blair Witch Project* and *El Mariachi* might be rare, but they also demonstrate the very real possibility for movie makers to produce incredibly profitable films without a \$200 million budget. There may be some exaggerations regarding movie budgets, but memorable (and profitable) storytelling doesn't necessarily require an *Avatar*-sized budget.

In the early days of TV, a correlation between the growth of TV watching and the decline of movie attendance (and movie ticket revenues in the late 1940s) seemed to suggest that people preferred to stay at home in newly-formed suburbs to watch TV, rather than go to a movie theater. Obviously, that trend did not kill the movie industry, and TV didn't completely replace going to movie theaters. But TV watching has become the single most popular activity that Americans do in their free time, with Americans spending about half their leisure time (2.7 hours a day) with a TV. Pediatricians are even warning parents that there is some scientific evidence suggesting kids are watching too much TV. In a survey of young people (children aged 8 to 18), watching TV content is more than comparable to a full-time job -- with kids watching over 7 hours of TV per day, seven days a week. So, from a consumption standpoint, it looks like TV watching will remain a popular activity for at least another generation (if not longer).

In terms of global consumer spending, subscription TV services have risen with a compound annual growth rate of about 6% over the last several years (including the most recent recession), exceeding \$200 billion in 2010. According to other PwC figures, TV advertising spending has been slightly more volatile than TV subscription spending, but it still exceeded \$150 billion globally during the Great Recession -- and did so despite growing competition with internet advertising. Unlike the "recession-proof" film industry, the TV business isn't so immune from the effects of economic recessions. However, outside of advertising

budgets, consumers are still willing to subscribe to television services in significant numbers even when free over-the-air broadcasts are widely available.

Historically, there have been very few industries that are completely impervious to economic or technological changes, so it shouldn't be too shocking that the advent of digital video is starting to cannibalize parts of the overall video industry. The movie industry has legally categorized some forms of online video distribution as piracy, but legal and legitimate online movies do exist -- and are even sanctioned by some movie studios as they experiment with releasing movies with more home viewing options (such as Video On Demand or online streaming versions) simultaneously with (or before) theatrical releases. These digital distribution methods for movies and shows are still in their infancy, but the convenience for viewers creates valuable services -- which appear to be in growing demand as traditional television networks are beginning to provide their own online video strategies. Online TV shows are also starting to pull cable/satellite TV subscribers away from their set top boxes, but not in enormous numbers just yet. Still, the potential for online video is great enough that it can't be ignored, and many companies (both traditional media and not), like Apple, Verizon and HBO Go, are looking to offer more direct-to-consumer online video services.

Purely online video services are clearly not yet collecting revenues at the same scale as the traditional TV and film industries, but the size of this audience is unquestionably large. Recently, Vimeo's subscription service for online videos stated that it has reached 150,000 paying subscribers out of its tens of millions of unique viewers. Other online players like YouTube don't rely on a subscription model and have started generating advertising revenues upwards of \$400 million in 2010, and YouTube's audience is quite large with over 100 million unique viewers (conservatively) in a month. In 2011, YouTube also served up over a trillion views of its wide variety of online video content, and this online video giant is aiming to compete with traditional television networks. To attract even more advertisers, YouTube is planning to sponsor and provide more professionally-produced content to add to its already immense amount of amateur video. Impressively, YouTube received, from mostly amateurs, over 48 hours of video content every minute in 2011, up from users uploading 8 hours of video per minute in 2007. And from that vast amount of non-traditional video, series such as *The Guild* have gained popularity and success from this growing availability of low-cost video production and distribution. The line between amateur and professional video is even becoming difficult to define, as the children from the viral video "Charlie Bit My Finger" have gone on to become minor celebrities -- earning enough income for Charlie's family to afford a new house. Online videos are also a substantial traffic driver for social networking, with Facebook being one of the top ten online video destinations in the US. So, it is without a doubt that online video destinations will play an important and perhaps even a dominant role in future media consumption.

Overall, the evidence points to a very optimistic future for the video industry and all varieties of video creators. Costs for producing all types of video content are falling as video recording technology gets better and less expensive. It's also never been easier to distribute video content, since broadband connections are becoming more and more widely available, and the internet is cheaper for consumers to access. Movie makers of every kind should be able to benefit from the progress of technology. A TV show or movie can be produced for a fraction of the cost compared to a decade ago, so many more kinds of shows can be developed with less risk. There is a vast new army of amateur video producers who, as they hone their skills on short video clips, have every opportunity to create digital movies for a very large audience and to monetize their creations or obtain fan-funding for future videos. Viral videos can be made by professionals, too, and a growing number of filmmakers are experimenting with shorter promotional clips that can help them engage more with their

audiences. Watching videos has become one of the most popular activities to do, for nearly all age groups, so the demand for video content appears to be extremely solid. The movie industry may not be completely recession-proof, but there are very few industries that do as well as the movie industry when the economy sinks.

Case Study:
Kevin Smith's Red State: Profiting By Avoiding The Gatekeepers

Kevin Smith is a famous and successful filmmaker -- writer, director and actor -- who went in a different direction with a recent film, *Red State*. Historically, Smith is known for his humorous films, often targeted at young men. However, a few years back he had the idea for a horror/thriller film called *Red State*. Given his history in the comedy world, he found it more difficult than in the past to get financing for the film. At one point, he considered fan-funding the film, but changed his mind after some people said it would never work. He has said repeatedly since then that he made a mistake in not fan-funding the film.

He decided that he would not make the same mistake when it came to distributing the film. After building up some press buzz about the film, he promised to auction it off to a distributor (the traditional way films are sold) at Sundance. However, at the event, he "sold" the film to himself, and said that he, and his producer, Jon Gordon, had set up their own distribution company, and they would be distributing it themselves. But the key part was that he, himself, was going to tour with the film through theaters.

It's important to recognize a few things. Smith, over the years, has built up a large and loyal following not just with his films, but actively connecting with his fans in other ways as well. He was one of the first filmmakers to be very active online, setting up his own message forums, which he actively used to engage with fans. More recently, he took to podcasting, building up not just a single podcast, but an entire "online radio network" of podcasts, broadcasting all the time, and doing live shows and tours. On top of that, he's been a very active Twitter user, engaging directly with tons of fans.

Separate from that, he has built up a (well-deserved) reputation as a fantastic performer/story teller at the various question-and-answer events he has held over the years. Over the past few years, he has toured the world doing Q&A sessions (which often have high-priced tickets).

So, when it came time to promote *Red State*, he accurately recognize that he didn't need a distributor for traditional marketing or distribution. Instead, he could take the movie on tour himself, and use his huge (and loyal!) Twitter base to handle the marketing. Knowing that his fans already pay large sums to see him do a Q&A, he was able to bundle the two together, and do a film tour with a Q&A, meaning that his "per ticket" sale price was actually the highest in the business while the tour was ongoing. From there, while he sought to do a traditional film release -- which he admitted was more sentimental than anything else -- he also actively embraced any and all forms of video-on-demand, making sure that the movie was available in almost any manner that a fan might want to watch it.

The results were impressive. He barely spent a dime on marketing (he spent about \$9,000 on ads that were required for Oscar consideration, though he hated having to do so),

meaning that his movie had to recoup a lot less than any movie going a more traditional route. As he's mentioned, while most people know the cost to make a movie, they don't realize that just as much, if not more, is added on top in marketing costs, all of which need to be recouped before any profit is made.

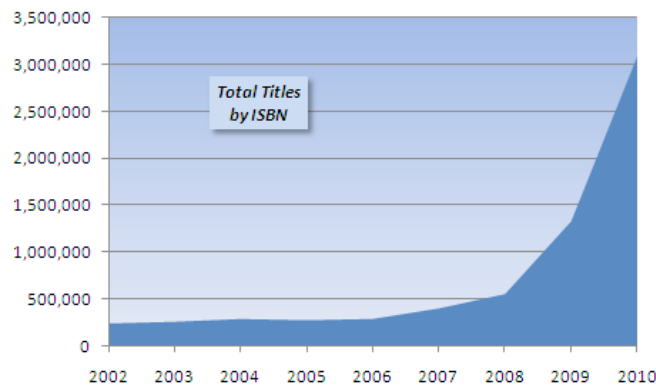
However, in Smith's case, he was able to fully repay his investors just from the initial tour and selling foreign rights. That means, within months of the film being completed, it was in the black, and all additional revenue was pure profit. This is almost entirely unheard of in the movie business. By doing things differently, he was able to create a very successful, profitable movie venture.

One footnote on this story: because of a legacy theater system that has also been resistant to adapting, many theaters shut Red State out from any sort of widespread theatrical release, in protest of him pushing the movie to video-on-demand before showing it in the theaters. Too often we see such legacy players prevent wider success.

Section 2: The Book Publishing Market

Historically, the consumer book industry has been relatively immune to economic downturns, according to PricewaterhouseCoopers' (PwC) Global Entertainment and Media Outlook, and the numbers seem to confirm that consumers continue to read, even when times are tough. From 2008 to 2010, the book publishing industry wasn't growing by leaps and bounds, but unlike a lot of other industries during that time period, it didn't fall.

Counting up all the books published in a year is no small task. The United States is, by all accounts, the largest market for books. The number of American publishers (including small, independent presses) was estimated to be about 3,000 in the 1970's. That number grew to over 60,000 publishers by the end of the 20th century. And over the past decade, the availability of print-on-demand technology has made it somewhat challenging to definitively state how many publishers exist, assuming we want to count self-publishing as a legitimate business activity. (We do.) The difficulty of determining how many publishers exist is especially acute, if the role of a publisher is simply defined by the ability to distribute text to a wide audience. Authors can (and have) become their own publishers as the technology to publish text has become incredibly affordable and widely available to anyone with the passion to write. As an extreme example, the progress of technology has allowed one Philip M. Parker to become a hyper-prolific "author", owing to his 100,000+ book titles, which he algorithmically generates from public data (and sells on amazon.com).



However, the number of book publishers is finite, so all is not lost. The ISBN (International Standard Book Number) provides a record of book titles that have been registered by an ISBN Agency, but not every book publisher obtains an ISBN. Still, this is the approach that BookStats used in its methodology to estimate the size of the US book market from 2008 to 2010. During

that time, 35,800 publishers registered with an ISBN and BookStats gathered information from 1,963 of those publishers.

In its first annual study of the US publishing industry, BookStats surveyed about a couple thousand publishers for figures such as their annual revenues and unit sales data. And from these numbers, BookStats created a model to extrapolate the entire US book market, based on the primary data provided by publishers who were willing to participate.

BookStats categorized its surveyed publishers (who collectively bring in over \$15 billion) according to the size of their revenues, then extrapolated to the wider market based on the record of total number of titles and publishers.

year	revenue (billions)	% change	units sold (billions)	% change
2008	\$26.5		2.47	
2009	\$27.1	2.3	2.51	1.6
2010	\$27.9	3.1	2.57	2.4

The result of BookStats' statistical estimates was that the book market grew in the US from 2008 to 2010, both in revenue and units sold. The amount it grew is not necessarily

impressive by itself, but considering that the financial crisis hit in 2008, it looks like the book market barely noticed the widespread economic turmoil in other parts of the economy.

But let's not simply accept BookStats' results without question. There are other publishing industry estimates out there, conducted independently, that should agree with these numbers (or not). The problem is that every statistical analysis is slightly different and defines the book market in its own way. Let's not worry about that too much for now, though, and just see if other numbers at least support this picture of a book publishing market that seems to ignore economic recessions.

As we mentioned earlier, PricewaterhouseCoopers also covers the book industry, but it does so by using some slightly mysterious methods. PwC relies on industry sources for historical data and then applies proprietary algorithms and mathematical models to factor in market influences such as population demographics, economic statistics, technological trends and other possible variables that could affect the industry. That said, it's not entirely clear how PwC arrives at its numbers, and more granular breakdowns of its figures are sometimes unavailable.

According to several PwC reports over the last few years, the global book publishing market was worth about \$100 billion in 2004 and has grown to almost \$110 billion in 2010. Considering that the Great Recession occurred during that time frame, that's actually a fairly impressive rate of growth of about 9% over 7 years with a compound annual growth rate of almost 1.5% (although the actual year-over-year numbers bounced around a little). For North America (not just the US), the book industry grew from about \$28 billion to a little over \$33 billion over the same period of time--increasing about 13% over 7 years. These figures are obviously approximate and likely subject to a significant margin of error. But these numbers agree with other estimates that the book

Year	North American Revenue (billions)	% Change	Global Revenue (billions)	% Change
2004	\$29		100	
2005	\$31	6.9	106	6.0
2006	\$31	0	104	-1.9
2007	\$32	3.2	110	5.8
2008	\$33	3.1	110	0
2009	\$33	0	108	-1.8
2010	\$33	0	109	0

publishing market has not shrunk, but rather has held its ground and expanded even while the global economy experienced historically bad times.

In other reports, the size of the global book publishing market has also been estimated to be around \$111 billion (80

billion euros) by organizations such as the International Publishers Association (IPA), up significantly from its estimate of approximately \$72 billion in 2006. That would be a remarkable growth rate (over 50%!), but the IPA has only recently started compiling comprehensive statistics on global publishing and its researchers admit that it's a difficult task -- largely due to the near-absence of statistics for sub-Saharan Africa and the Arab world. Ultimately, though, there seems to be consensus that the overall size of the book publishing market is steady in terms of publisher revenues and consumer spending. And, amazingly, this steadiness remains amid economic turmoil.

Interestingly, while these market estimates point to a remarkably stable environment for the book publishing industry, we should also put these numbers into context. The book publishing industry does not exist in a vacuum -- and books are in competition for consumer attention against a wide variety of other forms of entertainment, such as movies, video games and even outdoor activities. Additionally, we have purposely excluded other reading materials like newspapers, magazines, as well as the elephant in the room, the vast amount of textual information on the internet -- blogs, tweets, online comics and countless other websites. One might expect entertainment to be a zero-sum game, but somehow even in competition with numerous other activities that could take away from the book market, the book industry has remained incredibly stable.

In fact, despite all the stories that no one reads books anymore, there's been a curious increase in the number of books that were produced in recent years. (And don't forget, as we briefly mentioned earlier, BookStats estimated that the number of books sold in the US has also increased since 2008.) According to R.R. Bowker, the number of traditional book titles produced grew 5% in 2010 compared to 2009, and the output of non-traditional titles (such as print-on-demand books, self-published works and micro-niche publications) soared 169%. Bowker has been keeping track of ISBN registrations, and since 2002, the number of traditional books has grown by 47%. On top of that, the number of non-traditional books (those self-published books and print-on-demand works) exploded by over 8,400% from 2002. Looking at the absolute numbers, traditional books rose from 215,138 to 316,480 titles from 2002 to 2010. The astonishing part: non-traditional titles started at 32,639 in 2002 and numbered 2,776,260 in 2010 -- so now non-traditional titles outnumber traditional ones by more than 8 to 1. (It should be noted that audiobooks and ebooks are excluded from these ISBN counts.)

Perhaps it shouldn't be so surprising that, as the cost of self-publishing has plummeted over the years, the number of books produced by non-traditional methods would seem to increase exponentially. However,

year	# of traditional titles	# of non-traditional titles	total titles
2002	215,138	32,639	247,777
2003	240,098	26,224	266,322
2004	275,793	19,730	295,523
2005	251,903	30,597	282,500
2006	274,416	21,936	296,352
2007	284,370	123,276	407,646
2008	289,729	271,851	561,580
2009	302,410	1,033,065	1,335,475
2010	316,480	2,776,260	3,092,740

this initial exponential increase in production has not, as we discussed previously, necessarily translated into a book market with spectacularly high growth rates for revenues. On the other hand, the vast diversification of publications and appearance of micro-niche categories most likely create an industry that isn't as volatile or reliant on a handful of best-selling authors. From the standpoint of individual authors, the steep drop

in the costs to produce and distribute books has opened up innumerable opportunities. Authors with niche audiences can thrive nowadays, whereas they might never have been discovered -- or had their manuscripts simply rejected for publication in the past. Independent authors have eliminated some of the middlemen involved in book publishing, so even if the exponential growth of non-traditional books hasn't resulted in exponential revenue growth, the profit margins for individual authors can be higher than ever before.

Interestingly, the book market didn't stumble during the Great Recession, and it should be noted that this feat was performed even though the metrics in this industry rely heavily on the single revenue stream of just selling physical, printed books -- unlike other creative industries, which also earn significant revenues from sources such as advertising, licensing and hardware sales. Generally, movie licensing deals have not been counted in estimates of the size of the book market. (And some argue that movie licensing has not been particularly successful for the majority of rights owners of books.) Additionally, the sales of ebook hardware (e.g., the Kindle, Nook, iPad, etc.) are also not included in the book industry. However, these kinds of alternative sources of revenue are beginning to be explored -- especially as the ebook market matures and as publishers experiment further with business models. A salient example of a cross-platform book franchise is the upcoming online video game, Pottermore, based on the popular Harry Potter series. J.K. Rowling's publisher also has rumored plans for a social network and ebooks, to become on-going revenue generators for the Harry Potter franchise (in addition to merchandising and advertising opportunities).

The topic of ebooks is obviously an important sector of the book industry, but although there have been various electronic book devices commercially available since the 1990s, the popularity of ebook hardware is only just starting to really take off. And by just about every metric, the market for ebooks is soaring. Sales

Case Study:
JA Konrath and Barry Eisler:
The New Opportunities In Self-Publishing

These two authors of mystery thriller novels have been making quite a bit of news for their decisions to embrace ebooks directly. Both have been published by the big traditional publishers in the past (with Eisler's books being best sellers), but both have decided it's significantly more beneficial to just release ebooks directly on their own or, more accurately, with more modern partners who act more as enablers than as gatekeepers.

Not only do they have more control over the work, but they make more money. That's because, under the traditional model, the large publishers provide very small royalties to authors. Konrath and Eisler did the math, and realized that without having to give up 90% to publishers, they could price their books a lot lower, but still make more money per sale. By then making it easy and cheap to purchase their works, they could make more money in total.

In fact, in running various experiments, Konrath found that as he brought the price of his book lower and lower to around \$0.99, he made increasingly more money (and built up an even larger fan base). By further connecting with those fans, and even encouraging fans to get free copies of some of his books, he was able to build up an even larger loyal audience, who were more than willing to jump at the chance to support him directly, as he came out with each new book.

Konrath recently noted that he's sold over 700,000 ebooks, and in December of 2011 made \$140,000 from ebook sales. Without a publisher. There are clearly huge potential rewards for those who are able to embrace today's opportunities, while producing quality work.

*Case Study:
Paulo Coelho: What If Piracy Increased
Rather Than Decreased Sales*

Paulo Coelho is one of the most successful authors of all time, having sold over 100 million books. However, a few years ago, he became very vocal in suggesting that one of the best ways to increase his own sales was to “pirate” his own books. He ran an experiment, secretly putting up a Russian translation of his most famous work, *The Alchemist*, on The Pirate Bay. Prior to that, he had almost no sales at all in Russia. However, after seeing the book start to be shared widely online (in violation of copyright law), he noticed that his Russian sales started increasing dramatically, from less than 1,000 to over 100,000 in just two years, without any other marketing effort.

After seeing similar results elsewhere, he finally went public with this and convinced his publisher, Harper Collins, to be more comfortable with actually releasing official digital versions of his books for free.

Since then, Coelho has remained an outspoken supporter of using free distribution as a way to build up an even larger audience, and has yet to see his sales suffer in any way. In fact, the results have been just the opposite.

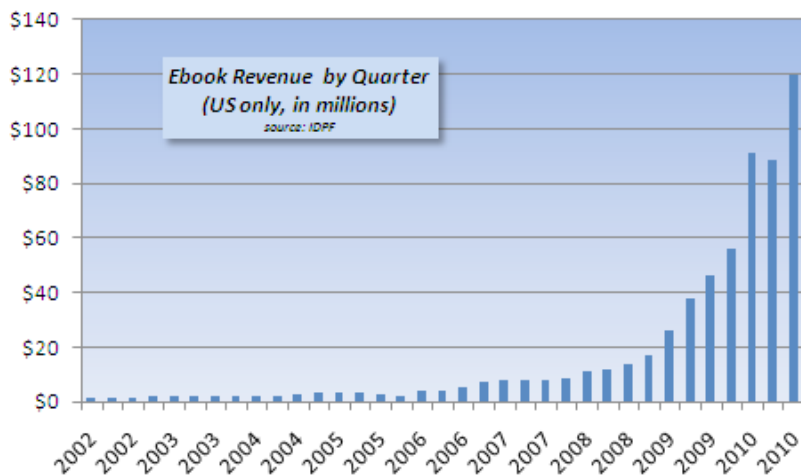
Of course, it’s also worth noting that during this time, Coelho has remained very engaged with his fans. Using Twitter, Facebook and YouTube extensively, he’s regularly in contact with many of his fans. He’s also created gatherings, and encouraged his fans to create a movie out of one of his books, piecing together different fan-created sections into an overall work. What he’s shown is that, when done right, these tools that are often blamed for destroying the industry, can be used to the advantage of the artists (and fans).

of ebooks have risen sharply over the last three years, according to BookStats, by 131.9% from 2008-2010. Total ebook revenues in 2010 were about \$1.62 billion. Unit sales growth for ebooks over the same period was 347.4%, and the share of the overall book market (in revenues) going to ebooks grew from less than 0.5% in 2008 to over 5% in 2010. This kind of rapid growth might appear to be good news for the book market, but the uncertainty over how the growth of ebooks might cannibalize traditional printed books has many publishers concerned about possibilities of a “Napsterization” of books.

So while the overall book industry has been relatively stable over many years, digital ebooks appear to be set for explosive growth. Some publishers view ebooks as a complete replacement for printed books, and others see ebooks and printed books peacefully coexisting. Regardless of the outcome, the transition from a market dominated by printed paper books to one consisting of a sizable amount of downloadable software will be a challenging one for publishers, since the decisions that they make about ebooks may potentially set long-lasting consumer expectations.

Large book publishers are justifiably correct to be concerned that their “single source” revenue streams are about to face increasing competition. As we mentioned before, other media industries have more diversified sources of income. But for large publishers, a disruption of the sales of printed books could upset their main revenue stream. Some publishers make an analogy to the music industry, saying that Apple convinced music labels to sell songs for 99 cents -- without regard to whether that price could sustain the music industry. So book publishers are understandably wary of deals that might undervalue their works. However, there may be a bit of a “sour grapes” attitude here, in that publishers might be reaching for unattainable pricing structures, and ultimately, consumers may balk at prices that are too high.

Fortunately for the book industry, there is still a little bit of time. Technology has not yet produced a “perfect”



replacement for a printed book. E-readers have batteries that can die, pages that aren't always viewable in sunlight, restrictions on how they can be shared, and up front hardware costs that are a significant barrier to entry for many consumers. These downsides to ebooks are not going to be completely eliminated anytime soon, so paper-based books aren't dead just yet.

That said, ebook sales revenues have recently surpassed the \$1 billion mark, and are projected to triple in coming years. That would make ebooks still only about a tenth

the size of the overall US book market, but the rate of growth of ebooks is astounding and can not be ignored. Also, the economics of ebooks points towards a future where publishers should consider their ebook strategy as their primary focus -- with printed books becoming akin to selling keepsakes. The logic behind this assertion is that the profitability of printing physical books has been declining, and even with print-on-demand, there is no technology on the horizon that can make printing on paper as cheap as storing, copying and displaying digital bits. An entire library of books can be held in a single hand on some digital device, and the technology that enables vast amounts of information to be readily available is not going to disappear.

The technology that enables widespread distribution of ideas and knowledge should not be viewed in a negative light. While traditional publishing revenues may be negatively affected by the growing demand for ebooks with lower unit pricing, the solution is not to restrain the growth of digital works -- but to encourage even more growth. This is one of the rare cases where the practical answer to lower profit margins can actually be to increase volume. The risks associated with producing ebooks are dramatically lower than managing a printing run of a paper book. Some have suggested that publishers need to fully embrace digital publishing by flooding the market with ebook titles -- making revenue wherever it is possible and growing profit with immense scale from selling low-cost ebooks and creating a convenient marketplace for consumers with an all-they-can-eat buffet. That suggestion may be a Utopian vision, but a half-measure approach of restricting some titles to printed editions creates a marketplace with potentially limited consumption from consumers having to navigate complex purchasing barriers. The anecdotal examples of Amazon.com and Apple providing convenient "1-click" shopping experiences gives some evidence that consumers gravitate towards simple pricing and delivery methods. Book publishers are already experimenting with various forms of ebook pricing models, so business models are currently being tested, and it seems likely that ebooks will continue their rapid growth -- especially as some of the questions around business models start to settle under recognizable patterns of what works.

In the book industry, there has been a history of stability for publishers and a fairly continuous streak of an increasing production of book titles. There is already an enormous and growing supply of book titles being produced, more than ever before, and there are both risks and opportunities to go along with this trend. The risks lie mostly with traditional publishers that are reliant on a production process with high upfront costs, which require massive sales numbers for a break-even point. However, as the costs of production and

distribution decrease, there are plentiful opportunities for self-publishing and non-traditional publishing. Traditional publishers will need to adapt to a market that may no longer contain a short list of predictable best-selling titles, but the diversification of book categories should make it easier, not harder, to sell more and more book titles.

There are additional factors that also point to a bright future for books. On a very macroscopic level, the world population continues to grow, and literacy rates are generally increasing. (There are concerted efforts to spread literacy all over the globe, and some developing nations may be able to take advantage of the lower infrastructural costs of ebooks in innovative ways.) As disposable income levels tend to increase, there has also been a correlated increase in media consumption, which includes reading books among other activities. In the US, there are roughly 62.4 million avid readers, who spend more than 5 hours per week reading. Studies have found that library patrons tend to read more and also purchase more books, so the possibility that the availability of “free books” could end the commercial market for books has at least some experimental evidence to the contrary. In general, the world is headed towards generating more books and more ideas with easier and cheaper access to information and media. The path to get to a world of ubiquitous books may not be easy for every author or publisher, but the aggregate market looks quite promising.

Section 3: The Music Market

Defining the music industry is tricky -- it can be defined in several different ways and each method can leave out significant segments of the market. For instance, various music organizations and government statistics don't count (or vastly under-count) contributors to the music industry, such as self-employed artists who might work part-time or musicians working for non-profit activities like schools, churches or other cultural venues. There are also several independent music distributors that aren't counted in mainstream music industry statistics. Ultimately, music is a pervasive part of life, and the music industry is not a centralized, monolithic business. The music industry is made up of several music industries -- ranging from the major labels to piano teachers. If the book industry looked almost too vast to account for, then the music industry could seem even more daunting.

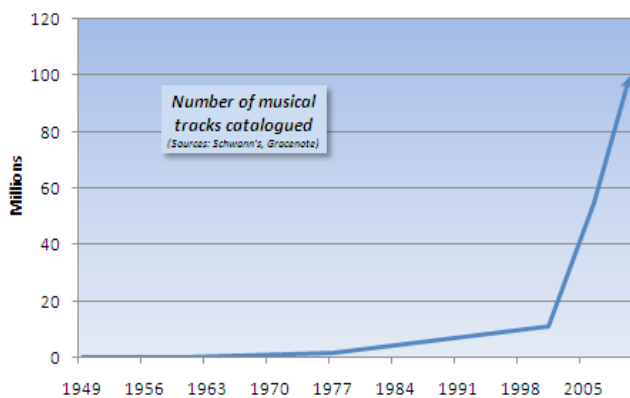
Unlike books, there isn't an analogous ISBN database for music tracks, but there are services like Gracenote, which provides a global media database for music (as well as videos, which we'll discuss separately). According to Gracenote's collected data, there are over 100 million songs from over 400,000 different artists. While that sounds like an impressive collection, it certainly doesn't contain every distinct musical composition ever recorded or composed, either. However, compared to similar musical databases, such as MusicBrainz or FreeDB, Gracenote's database is roughly an order of magnitude larger and has existed for over a decade. Gracenote also claims to cover a wide international distribution of music from over 200 countries in more than 80 languages.

year	number of tracks indexed by Gracenote (millions)
2001	11
2005	46
2006	55
2011	100

Over the last ten years, Gracenote has increased the number of music tracks in its database almost ten-fold, up from around 11 million songs in 2001. Now, that growth of the Gracenote database

obviously includes a lot of older music that has only recently been indexed, so its expanding index doesn't exactly serve as the ideal proxy for the increasing rate of production of new music. However, the trend still clearly looks like the amount of music available to consumers is steadily growing -- with little sign of slowing down. More artists are undoubtedly making more music today, but the metrics for proving it aren't aggregated in a centralized way. Generally, independent musicians aren't necessarily registering their works as they perform them, but that shouldn't take away from the trend that it's easier than ever to record and

play music and that the production of music is rising.



There are other music production statistics, such as the number of new album releases, available from Nielsen SoundScan. Very roughly, tens of thousands of albums are released each year, based on Nielsen's figures. Nielsen reported approximately 38,000 new albums were released in 2003, and that number grew to nearly 80,000 new albums by 2007. (This number also ballooned to 106,000 in 2008, but then fell back to 75,000 by 2010.) However, this only covers the US market, and there is some concern that these Nielsen numbers omit a significant number of independent music releases. For example, CDBaby.com founder Derek Sivers estimated that his company (before

he sold it in 2008) was producing music at 70,000 new albums in a year. More recently, TuneCore has argued that it produces a significant amount of music that Nielsen ignores -- an amount that could possibly double the size of the production of music in the US with 90,000 new releases in 2009. (On top of that, other independent music distributors are also not counted in Nielsen SoundScan's reports -- e.g., Jamendo, SoundClick.) Additionally, there are other problems with tracking the creation of albums. The whole concept of an "album" is eroding as the popularity of single tracks dominates the digital music market. (Tellingly, music industry trade groups have created statistics related to albums such as "track equivalent album" (TEA) numbers that attempt to count multiply-sold single tracks as the same as an album sale. Interestingly, album sales numbers could also be converted into single tracks sales, but that isn't a widely used metric.) Ultimately, though, the conclusion should still be that the production of music is growing and, at worst, being vastly under-counted.

year	overall sales transactions (million)
2000	845
2001	800
2002	693
2003	687
2004	848
2005	1,003
2006	1,198
2007	1,369
2008	1,513
2009	1,545
2010	1,507

On the consumption side, music is also being consumed at near record-setting levels. According to Nielsen SoundScan figures, the overall sale of music (including albums, singles, digital tracks, etc.) exceeded 1.5 billion transactions in 2010. That's up from 845 million transactions in 2000. These overall sales figures seem to rise and fall a bit over the years, but they don't necessarily drop during economic recessions.

Again, there are a few caveats with the Nielsen SoundScan sales data that should be mentioned. First of all, these are transactions without regard to the price of an item, so as we'll discuss later, this does not necessarily mean that consumers are spending more when they buy music. (In a move that will further complicate these metrics in the future, Nielsen has recently stated it will change its policy for counting transactions -- by completely ignoring transactions priced under \$3.49.) Secondly, as we mentioned

before, these numbers don't include a significant amount of independent music sales, including cash sales at local music events and concerts. Lastly, there have been accusations of SoundScan fraud by which these numbers are purposely manipulated in order for publishers to improve their sales reports and their rank on

Billboard charts. But presumably, this fraud does not constitute a majority of the music industry. Ultimately, while these transaction figures may be somewhat inaccurate, the trend of listeners consuming more and more music is still valid.

Another way of looking at the music industry is through the numbers that the IFPI (International Federation of the Phonographic Industry) publishes on what it calls “the broader music industry.” In 2005, the IFPI estimated the global music industry to be worth \$132 billion -- which included revenues from music in radio advertising, recorded music sales, musical instrument sales, live performance revenues and portable digital music player sales (among a few other income categories). By 2010, the IFPI estimated the market to be worth \$168 billion, but it had also changed how it categorized some of the revenues and added categories such as audio home systems, music-related video game sales and music revenues from TV advertising (in addition to a few other categories).

year	the broader music industry (billions)
2005	\$132
2006	\$139
2007	\$150
2008	\$151.5
2009	\$140
2010	\$168

So according to these figures, music production and consumption look like they’re generally healthy and growing. This shouldn’t be too surprising, given that the means to produce music has become cheaper and easier over the years. In the 1990s, recording studios were able to charge “tens of thousands of dollars” for just an hour of access to their high-end audio equipment. Nowadays, extremely good-quality recording equipment for audio can be purchased by consumers (or pro-sumers), and home studios can produce digital musical recordings for a fraction of the cost that musicians used to spend on professional recordings. Perhaps the sound quality isn’t as high as it used to be, but there’s no mistaking that the costs to

produce decent-sounding music have fallen dramatically. On the consumption side, music lovers are also enjoying the benefits of technological progress with better and cheaper ways to digitally store and replay music than ever before. The first portable MP3 players could hold several hundred songs, and that capacity has now grown to such ridiculously high levels that it’s almost unnecessary to advertise the storage capacity of digital music players.

But, despite the increasing production and consumption of music, the music industry doesn’t seem rosy to everyone. The revenues from recorded music, such as CD sales, have been falling steadily over the last several years. This shouldn’t come as a huge surprise, either. Historically, music has been sold on various kinds of physical media: vinyl records, 8-track cassettes, cassette tapes, CDs and other less well-known formats. Each of these formats has seen its peak, and each of them may someday cease to be sold entirely -- though that time has not come yet even for vinyl (as there are signs that vinyl records still have plenty of useful life left and their sales were up ~41% for 2011). Still, as the CD format wanes, the revenues from selling CD albums are diminishing, too. The problem, it seems, is that consumers are buying more single tracks now instead of entire albums and that consumers have an expectation that digital music tracks should be cheaper than purchasing plastic discs. The result is that the number of single digital tracks purchased is rising (initially with double-digit growth), but the revenues from selling single tracks isn’t matching those of the peak years of selling CD albums. This trend was apparent in 2007, as the volume of physical recorded music was dropping (also by double digit percentages). The problem here is that the major labels have been relying on CD sales as their main income stream and are only just starting to diversify their revenue and business models. Interestingly,

*Case Study:
Cee Lo Green: The New Music Success
Story Is Not In Selling Music*

Cee Lo Green is considered one of the most successful music artists on the scene today, but according to a recent case study in the NY Times, the sales for his actual album are on the low side for someone with such a high profile. However, the report also notes that this doesn't matter, because Green brought in over \$20 million in 2011, with the "smallest slice of the pie" coming from actual music sales.

Green and his publisher/management team at Primary Wave, have realized that the modern music world has huge opportunities in changing the marketing equation, rather than focusing just on music sales. That is, the company has focused on building up Green as a brand, in and of himself, which has opened up all sorts of opportunities from sponsorship and endorsement deals to TV appearances and a hosting job on the TV show *The Voice*. He's also working on a theatrical show for Planet Hollywood.

The key recognition here is that, while the music is important, the real opportunity is in the brand built around the music. The more you can do with a brand, the more money can be made. The music still needs to be good (otherwise the brand will suffer), but then the music just becomes part of the tool to help promote the brand. And you can't "pirate" a musician's brand without the musician. In fact, the wider the music itself is spread, the more valuable the brand can become.

a former executive at Universal Music, Tim Renner, has said that the major labels had a chance to diversify their income streams when "they had the money and could have built the competence by buying concert agencies and merchandising companies." However, this hindsight isn't necessarily the way forward for the major music labels now.

At this point, it may be helpful to understand the state of the music industry and its history in order to get some perspective on its future. In the last century, there was a music recession that lasted from 1979-1985 in which album revenues fell by the same percentage as they did from 1999-2006, so this segment of music business is not immune to economic downturns, but it did recover from that slump by the mid-80s. Certainly, the music business has changed since then -- and as we pointed out, CDs are no longer the most convenient or desirable format for music listeners nowadays. (And it seems like unwarranted pessimism to think that the entire music industry won't recover from the end of the CD era.) Some popular artists, like Sting, have recognized that the CD era is ending and are even moving towards making music apps.

In the past, the success of an artist was measured when an album "went gold" -- meaning that it had sold more than 500,000 copies. By 1999, the RIAA had even created a Diamond award for an album (or single) that sold more than 10 million copies. However, since then, there has been much more fragmentation in the sale of music, and the number of albums with thousands or millions of copies sold may be declining. As the variety of music produced became wider and wider, the consumption of music hasn't remained confined to mega-artists in just a few genres. Adding to the music categories of pop, R&B, country and rock&roll, there has been an explosion of new genres and sub-genres: hiphop/rap, electronica, punk, emo, etc. Independent labels are producing an immense amount of diverse music, and listeners have a larger buffet to choose from than ever before. Unfortunately for the major labels, that doesn't necessarily create a market that favors them and the traditional process of releasing music in a highly-choreographed way. According to Nielsen data, the number of music tracks that sold over a million copies was "only" 36 in 2007, and during that same year, the number of tracks

that sold less than a hundred copies was well over 3 million. Of those songs that sold less than a hundred copies, about 968,000 sold just a single copy (and remember that Nielsen omits a large number of independent artists). This suggests that producing music is becoming much more of an experimental process where millions of songs can be tested out -- and that high-cost investments to produce an album may not be a sustainable strategy for a producer. It doesn't mean the production of music is dying or being reduced to unpaid amateurs, but that the traditional process of A&R is changing so that musicians aren't being picked by music executives for "rock-star" success. The layers between the artist and the fan, namely the number of middlemen, is on the decline. The evidence for this is in the growth of crowdfunded music projects from sites like Kickstarter or SellaBand -- as well as the rise of ways for fans to more directly patronize their favorite artists.

Although the book industry has some time before e-readers really provide as much or more convenience than printed books, the music industry has no such luxury in the face of digital music. As soon as digital music was created, it gave listeners many more convenient ways to access music than formats like cassettes or CDs. However, the advantage that the music industry has over other creative industries is that music is a particularly pervasive product that can be associated with everything from soft drinks to cars to enterprise software/hardware. So the music industry has multiple opportunities to diversify its revenue streams.

While the music industry is generally associated with direct consumer spending, there are other ways for the music industry to diversify its revenue streams. The UK music industry's trade group BPI has even dubbed this expansion beyond consumer spending as "secondary

Case Study:

Jason Parker: One Working Musician Shows How People Will Pay

Jason Parker is a jazz musician in Seattle, who has been open about sharing just how he makes a living as "one working musician." He's tried various experiments, and been quite public about many of them. One case, involved testing out a "pay what you want" system. While "pay what you want" got plenty of attention back when Radiohead did it, many people have questioned if it really works for less-well-known artists. Parker had offered his existing albums for a \$5 download price, but switched to \$0 required with a "pay what you want" offering... and discovered that his sales shot up. Overnight, after making the change, he got more sales than he had in the previous three or four months combined.

On top of that, despite the fact that you could download it for free, many people paid. He said that over a three day period, he made more money than any time since the first three days after the album was released. Since then, he's gone on to make all of his albums available under this system, and has seen much higher overall sales. And while the old price requirement was \$5, he's now seeing an average price of \$8.50 on those albums -- and he's still consistently selling more than he was before.

This wasn't just online. He also tried an experiment with doing a "pay what you want" shows and CDs, and again found that many, many people were willing to pay, and he was often able to earn much more than when he had a set price. His CDs used to sell for \$10, but have averaged over \$12 when he lets fans set the price. On a recent tour, he saw the average price shoot up to \$14/CD. He noted that even the act of telling people that they could pay "whatever they think is fair" for the CD resulted in plenty of people just dropping a \$20 bill into his hands.

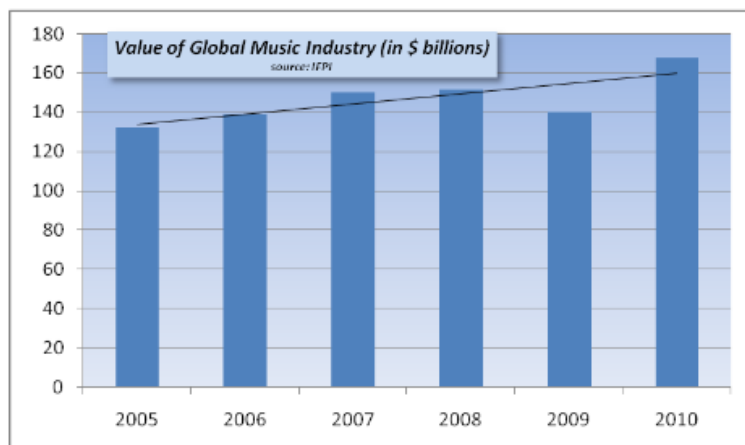
Of course, he notes that much of this is dependent on continually connecting with fans. Excellent music doesn't hurt, either.

revenue,” which includes all other incomes outside of physical music sales and digital music sales, such as advertising deals and licensing revenues from TV, movies and video games.

Additionally, live music and concerts have been doing pretty well as a business in recent years, in spite of the economy. From 1999 to 2009, concert ticket sales in the US tripled from \$1.5 billion to \$4.6 billion, according to Pollstar. Ticket prices and merchandise have become major sources of income for many popular rock stars like Lady Gaga, Madonna, Bruce Springsteen and for bands like U2. It’s not easy to duplicate the experience of a live show, so concerts have become a source of revenue for musicians and aren’t negatively affected by the availability of free downloadable music -- in fact, free music can encourage fans to attend live performances. There’s actual scarcity (not artificial scarcity) for live music, but on the other hand, rock stars don’t scale very well, either. So when Bono injured his back in 2010, the band stopped touring while he recovered. There really isn’t a way to replicate rock stars like Bono, and many fans will do (or pay) almost anything to see them. Recognizing this, the major music labels (and some other promoters) have started signing more “360 deals”

with artists to capture a fraction of the revenues of touring, merchandise and other non-traditional sales.

In other venues, more music is being discovered and sponsored by advertisers via contests like American Idol, The X Factor, The Voice and other popular TV shows with music-related themes. Several big retail chains (e.g., Starbucks) have also sponsored music events to help them better target specific demographic groups. There is even a market for using music to promote all kinds of consumer electronics. Apple is probably the most



prominent example of a tech company that uses music to promote the sales of its products, but there are also other examples, such as Seagate, which has sponsored music to be freely given to consumers to promote its brand and products. Bundling products and services along with music has been done without formal deals for a long time, and music industry execs sometimes (wistfully) point out that telecom service providers have long benefited from delivering free music downloads and from the increased demand for internet bandwidth from digital music -- though telecoms have only recently started to license music and pay royalties for music services.

Despite the major music labels being slow to adapt to the digital world, there have been and are plenty of music startups trying to capitalize on digital music services. Algorithms may be replacing humans in some parts of discovering new talent (or at least discovering talent more cost-effectively). There are more than a few companies trying to datamine music metadata in order to serve better music recommendations to consumers or to predict which artists will be popular with target demographic groups. For example, Stockholm-based X5 creates popular classical music compilations and has carved out a profitable business from licensing existing music and making it easier to discover music that might be hard to find for some listeners. While not every music startup can become a success (and it isn’t clear exactly how some music startups will succeed), there is clearly interest in investing in music businesses and music startups -- and that isn’t an indicator of a dying industry.

In 2003, the IFPI noted there were less than 50 licensed music services in the world, and that number has grown to over 400 now. Some venture capitalists assert that the risk associated with music licensing isn't worth their investment, but others argue the risk in music is a myth. The rules of investing are never that cut and dried and, obviously, the founders of music startups believe that the music industry is an attractive market to target. MOG's CEO stated that "providing music content is a smaller-margin business" but that the "addressable market is massive," and that the second biggest leisure activity behind watching TV is listening to music. Still, VCs like David Pakman have a reasonable argument that music licensing costs for startups can be too much of a burden, based on the general observation that the major music labels tend to kill off music startups with exorbitant licensing fees. Pandora, which went public in 2011, almost met its end in 2007 due to newly-imposed licensing costs for every song it streamed, but it eventually settled with lower fees after two years of negotiations and efforts to lobby Congress to save its music service from more expensive royalties. Napster, the original digital music disrupter, was actually shut down by the Recording Industry Association of America via lawsuits and a court order (though Napster was recently bought by Rhapsody and may now completely cease to exist as its service is merged with Rhapsody). In many cases, there seem to be significant barriers for music startups, but the toughest barrier doesn't seem to be a lack of consumer demand or prohibitive costs for music production. It's more likely that major music labels will sue music startups out of existence.

Overall, the music industry isn't based solely on the revenues of the major music labels. There are also new entrants to this market who don't rely on selling CD albums or concert tickets at all. Established tech companies are looking to provide music along with advertising and software -- and the free (or nearly free) cost of distributing digital music offers opportunities that are unique to music. But the emergence of new music businesses doesn't mean that selling digital music tracks (or music subscription services) directly to consumers is a bad business at all. There are some predictions that digital music sales will eventually exceed CD sales and continue to grow, so the current slump for recorded music revenues may simply be a temporary part of the natural business cycle. So on top of selling digital tracks directly to consumers, there are also nascent business models for music that involve more business-to-business transactions, such as corporate sponsorship of music or music licensing for software development. Music licensing for online videos is a growing market as more and more people watch videos that are accompanied by music. Music in video games is another business that could become significant and generate massive revenues. As Amazon's VP of Movies and Music Bill Carr said, "We're not tied to any one business model. If we were, we'd still be only a book retailer." The music industry is actually positioned to have a wide variety of income streams as more and more people gain increasingly convenient ways to listen to music.

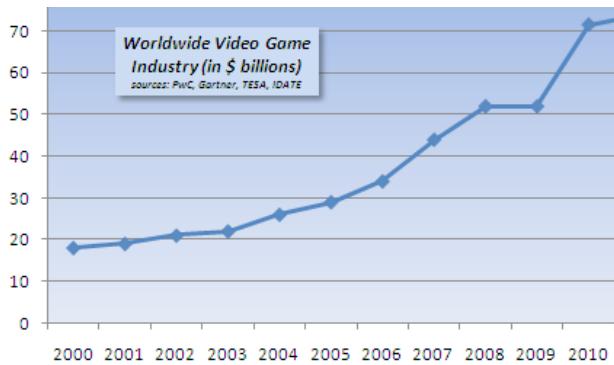
Section 4: The Video Game Market

The video game industry is by far the youngest of the creative arenas -- with the very earliest video games created in the late 1940s to early 1950s. The first commercial arcade video game, called *Computer Space*, was sold in 1971 with a manufacturing run producing 1,500 units of the coin-operated machines. Just one year later, Atari's *Pong* and Magnavox's *Odyssey* were competing to attract players to these game machines, and the industry was commercially established.

It's almost too obvious to say that the video game industry has grown substantially in the last 50 years, but the industry hasn't been completely without its problems. There was a minor market crash for home video game consoles in 1977 and a much larger contraction from 1983-1985. However, this slowdown for the video game industry did not actually coincide with the US economic recession of the early 1980s. During the early part of that recession, the video game industry was growing wildly (at an ultimately unsustainable rate). In the US, the home market for game consoles had reported profits of around \$3 billion in 1982, but it fell dramatically by 35% the following year. In 1983, there were numerous home video game consoles crowding the market, just when more general purpose home computers were becoming more affordable. Atari, the dominant game maker of the 80s, had peaked and overestimated the production run of its video game, *E.T. the Extra-Terrestrial*, which it had spent over \$100 million to produce. Fortunately, the video game industry didn't end in the mid-1980s with a glut of lackluster games with which players were disappointed. The Nintendo Entertainment System appeared in the US in 1985, and the home video game market rebounded. Additionally, handheld game devices came out in the late 80s, and the beginnings of online games also started to become popular by the 1990s. And as technology improved, even more innovations were developed for games in the 21st century.

Recently, video game titles have done quite well, with some of the most popular ones generating revenues similar to record-setting movie box office hits. The latest *Call of Duty* release exceeded \$1 billion in sales in just 16 days -- faster than *Avatar* hit the same milestone by one day. And despite the failure of E.T. as a video game, there have been several hit games based on movies. The Star Wars universe has spawned a long list of video game titles on many different gaming platforms over the years, from PCs to PlayStations to mobile phones and websites. However, it looks like EA spent nearly \$100 million to develop the recent *Star Wars: The Old Republic* game, and there are some concerns that this game may need to modify its business model, or it may be the last of its kind as a big-budget massively multiplayer online (MMO) game that relies on monthly

subscribers. Other popular MMO games rely on a free-to-play business model that attract a large audience who then need to pay for in-game digital items that enhance gameplay. *Pottermore*, the MMO game based on the Harry Potter universe, is a nascent example of such an MMO game, since it is still in beta mode with over a million players testing out the game. Overall, video games are more popular than they have ever been, and game makers are adapting to their audiences and creating games with broad appeal and monetization strategies that are innovative and resilient.



Globally, the amount that consumers spend on video games -- for hardware, software and accessories -- has grown impressively (more than tripling!) from about \$20 billion in 2000 to approximately \$70 billion in 2011, according to various reports from PwC, Gartner and iDATE. In just North America, consumer spending on video games has more than doubled from about \$10 billion in 2005 to over \$25 billion in 2011, as reported by the Entertainment Software Association (ESA). Other reports state that the revenues for video games topped \$33 billion in 2010, from over 3.2 billion game purchases. Undoubtedly, whichever numbers

are used, the video game industry as a whole has performed extremely well over the last decade, and there are several reasons to believe this trend will continue for the foreseeable future.

The demographics of video game players has expanded greatly beyond the traditional core of boys and young men. Additionally, one survey notes that the number of video game players in the US has more than doubled from 56 million in 2008 to 135 million in 2011. Worldwide, the population of gamers has exploded from 250 million in 2008 to 1.5 billion in 2011. Carnegie Mellon Professor Jesse Schell observes, "There are games now for pretty much every age, every demographic." According to a 2010 survey of social gamers in the US and UK, more women are playing social games (e.g. *Farmville* on Facebook) than men -- and the average age of these social gamers is over 40 years old. In fact, video games in general are being played by a more mature audience than the gamer stereotype might suggest, as the ESA reports that the average age of American gamers is 37 years old. (The ESA has also reported that 60% of all Americans over 6 years old play some kind of video game, and 29% of US gamers are over 50). Plenty of kids are playing video games, and the amount of time they're spending on video games has grown over the past several years as well -- from 26 minutes per day in 1999 to 1 hour and 13 minutes in 2009 -- according to surveys from the Kaiser Family Foundation. Kids are also increasingly playing video games on mobile devices, allowing them to squeeze more playing time into their busy days. Adult gamers play a sizable number of mobile games, too, with 55% of all US gamers playing on phones or handheld devices. So the video game industry has proven to be very nimble and able to follow players onto almost any consumer device and into nearly every aspect of consumers' lives.

The rapid pace of computer development makes it a bit difficult to track the growth of video games produced over the years. Video games are somewhat different from books or music or movies in that they require certain hardware -- and computer hardware can quickly become obsolete and hard to find. Entire game platforms can cease to be manufactured or sold, and if the proprietary hardware and software isn't preserved, it can be very difficult to try to port old video games to new machines. Still, there are some revivals of old games that have been brought to new gaming systems, but in general, the progress of video game development tends to leave

old games behind. In addition to games going out of style relatively frequently, since game platforms tend not to last much more than a decade, the number of game titles produced is complicated by duplication across platforms as some games are released separately on different consoles at slightly different times. One of the most popular platforms for games is Apple's iOS line of devices. Launched in July 2008, Apple's App Store had at least 6,000 games available to download by March 2009. A few months later in July 2009, the iOS platform had over 13,000 games. The next year in March 2010, there were over 30,000 games in the App Store, and some recent numbers put the number of games, just for Apple's iOS devices, at over 90,000 towards the end of 2011. So in just the last few years, the number of games on the iOS platform grew by about 1400%. Developers have been flocking to the iOS platform, and almost anyone can build fairly simple games for Apple's devices. And that is just a single platform, obviously there are other game consoles and PC game makers that have also produced many other games. Still, given that this proliferation of iOS games occurred during one of the worst recessions in history, there appears to be absolutely no slowdown in the creation of video games. However, as we mentioned earlier, when game development budgets rise to outrageously high levels, there may be cause for some concern for the genre of game that requires relatively high production costs. But as technology has made it easier and cheaper to develop games, it seems that the creation of video games continues to flourish and the demand for games is still quite healthy.

The game developer community has seen an enormous amount of change over the relatively brief history of the video game industry. Technological changes have been a constant in this industry and have prepared many developers to not rest on any laurels. The costs of game distribution have fallen steeply, just as they have for books, music and movies, but game makers haven't been so surprised by the economic and technological disruptions.

Case Study:

Valve: Infringement Is A Service Problem, Not A Legal Problem

Valve software is a video game developer and the maker of an amazingly popular digital distribution system for tons of video games, including many of the biggest games available today. Valve's CEO, Gabe Newell, has been adamant for many years that "piracy" was never a legal or enforcement problem, but merely a signal of customers being under-served. If anything, he has suggested, piracy is a form of market research of where there is demand that isn't being met.

A perfect example of this was in how Valve approached Russia. Many in the entertainment industry have declared Russia to be a lost cause, as infringement is rampant. However, Valve decided that it was a market opportunity and entered the Russian market with a convenient, well-priced offering. Newell noted that many in the industry warned that they'd never be able to make money in Russia. However, by offering a compelling, convenient and reasonably priced product, Russia has become Valve's second largest market, in terms of revenue, in Europe (just after Germany).

Furthermore, Valve has been quite active in experimenting with price. This has made the company realize that bad pricing is often a direct cause of infringement as well. In one famous experiment, Valve kept reducing the price of a game, and found that the total revenue they made increased significantly as the price decreased. A 10% decrease increased income by 35% -- which is a good start. But then Valve tried decreasing the price an astounding 75%, and saw revenue increase an amazing 1470%.

By offering a good product at a reasonable price, and realizing that infringement comes merely from customers who want something better, Valve has become a hugely successful behemoth in the video gaming market.

Case Study:
Minecraft:
Keep It Simple And Awesome

This simple-looking “open world” building game has become incredibly popular, and has made its creator, Markus Persson, quite wealthy at the same time. And it was all done with a focus on making the product worth buying. Persson has been quite clear that he doesn’t mind people getting “pirated” copies of his work. He’s said that the impetus is on him to add value to the game to make it worth buying. He has also noted that those who get infringing copies still help by advertising his game for free by word of mouth.

In the end, though, he’s made it simple and inexpensive to support his efforts, and the fans of the game have supported him all along.

While the game was still in beta (and offered at a cheaper price), Persson’s company was making well over \$100,000 per day on sales, even though it was quite easy to get unauthorized copies. Persson himself, under the name “notch,” has made a personal connection with tons of fans by interacting directly with Minecraft fans online. He recently publicly told fans that if they can’t afford the game, he hopes they’ll find an infringing copy, and then come back and pay him later. It seems to be working.

Persson has shown with Minecraft that as long as you connect with fans, make it easy to buy, and don’t treat fans as criminals, those fans are more than willing to pay to support your work.

Digital distributors have taken advantage of the ability to circumvent selling games in brick and mortar stores -- with examples like the game downloading platform Steam, which started in 2003 and now has over 35 million registered users and a peak of 5 million concurrent users. Independent game developers are, more often than not, under pressure to keep costs low and to develop games in modest offices -- or messy bedroom apartments. Independent games provide quite a bit of variety to the game industry and can be just as popular as more mainstream games. For example, *Minecraft* has sold over 4 million copies and has over 16 million registered users, and the game was originally created by a single programmer working part-time on it. An attempt to ridicule the success of *Farmville*, the game *Cow Clicker*, was greeted by some unexpected genuine popularity and demonstrated that social games could be remarkably simple and yet addictive. There are nearly endless examples of a single developer creating a game that meets with modest success, so the opportunity for game developers appears to be quite rosy even for individuals with scant resources. Clearly, not every game succeeds in popularity or profits, but the innovation in the video game industry has endured several technological shifts and encourages creativity for attracting players and for creating games. Technology platforms and business models for the video game industry can come and go, but the demand for entertaining games remains.

The video game industry has developed several ways to monetize their products. Initially, coin-operated machines required players to keep inserting quarters for cathode-ray tube entertainment. Then, consumers went to stores to buy boxes of software on cartridges, diskettes, CDs/DVDs, etc. Now, downloadable game software is widely available. But in addition, there are various game rental services, casual games and free-to-play games, and ways to sell digital goods and more engaging in-game experiences. Physical merchandise is yet another option (selling items like *Angry Birds* plush toys), and social games are gaining popularity among a broad audience. Game makers are also selling virtual ads, and the practice has become a standard way for games to earn additional revenues. The diversification of revenue streams for the video game market has been amazingly innovative, and there have been predictions that every part of our lives will eventually be turned into a game. “Gamification,” as the trend is called, has

cast a wide net over all human activities and could potentially encourage people to change their behavior to benefit the environment, to perform their jobs better, to lose weight, to buy products, or to perform almost any task imaginable. The use of video games to enrich our lives is nearly ubiquitous now, but there is still room for growth as games continue to expand into previously untapped demographics and niche markets. For example, some commercial enterprises are even developing games for employee training purposes, with Canon offering a game for its repair technicians to learn how to diagnose and fix its copying machines. In fact, various non-profit organizations are even soliciting for donations or raising awareness with games. The Dutch government even promoted a printing of commemorative coins with an online game.

Compared to other creative industries, the video game market is especially well positioned to take advantage of digital goods and the benefits of disruptive technologies. Game designers are adapting to a very wide audience and creating games that can entertain anyone with spare leisure time. Games are even encroaching into vocational education, so video games are no longer even restricted to leisure. As technology becomes cheaper and more widely affordable, it's unthinkable that more video games will not be included in the distribution of portable devices and common consumer electronics. Optimism for the video game industry appears to be well-founded, and as long as people desire to be entertained, it looks like video games will meet players wherever they are.

*Case Study:
Humble Indie Bundle: Making People
Want To Buy*

Recently, a new project called the Humble Indie Bundle has taken the video gaming world by storm. Started as an experiment, where a few independent video game makers agreed to bundle up a few different games and allow people to buy them on a "name your own price" basis, it's now become a huge phenomenon with new bundles released at regular intervals -- each one seeming to earn more than the last, often now able to earn millions of dollars from a single bundle offering.

The projects actually offer a few different innovations, all of which seem to excite fans and keep them buying. The first is that it's a pure "pay what you want" system. But, making it more interesting is that they make statistics available for people to see -- including the top 10 prices paid. This has actually created a form of "advertising," with some paying large sums for the sake of having their names listed on the leader board. There are also additional stats around which platforms are used, with the open source Linux users always leading the way (showing that those who prefer free software are certainly happy to pay for things they feel are worthwhile).

Another innovation was allowing some portion of the money to go to charities -- and allowing the buyer to determine how the money ought to be allocated. Yes, the buyer gets to determine how much money goes to charities and to which charities. A recent study suggested that people pay more in a "pay what you want" offering if there's a charitable component, and Humble Indie Bundle's success has certainly shown that to be the case.

A third innovation is in making everything simple. Rather than force users to pay with a single system, users can choose from a variety of payment systems. On top of that there is no DRM and buyers can re-download games that they purchased, at a later date.

By making things simple, allowing the consumer to set the price, and by having a nice charitable component, the Humble Indie Bundle has become a very successful enterprise as a way to distribute and sell video games.

Changing the Debate

Unfortunately, it feels like much of the debate about copyright law over the past few decades has been based on claims about the state of an industry that simply don't match up to reality. Rather than decrying the state of the entertainment industry today and seeking new laws to protect certain aspects of the industry, we should be celebrating the growth and vitality of this vibrant part of our economy -- while consumers enjoy an amazing period of creativity.

We hope that this report will help shift the debate away from a focus on a narrow set of interests who have yet to take advantage of the new opportunities, and towards a more positive recognition of the wide-open possibilities presented by new technologies to create, promote, distribute, connect and monetize. We're living in a truly amazing time for the entertainment industry, and it's time that our national debate reflects that reality.

In a time of disruptive change, it is important that any regulatory efforts be supported by actual data. Instead of reflexively trying to protect traditional entertainment businesses, this research should provide a starting point for many to rethink some of the assumptions that have been made in the past about the state of the industry.

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