

COMPANY CASE

Radiohead: pricing strategy and the music industry.

In 2010 the average price of a music CD fell below €8.75 for the first time in the history of the industry. This all-time-low highlighted the challenges faced by artists and record companies that have already seen revenues undermined by significantly cheaper digital downloads and widespread online piracy. In the past decade the average price of a CD has fallen by 28 per cent, or about €3.60, from €12.75 in 2000 to €9.15 in 2009, according to figures from the BPI, an influential music industry trade body. 'The falling price of CDs just adds to the woes of record companies,' said James Bates, media partner at the consultancy Deloitte. 'The cost of producing the music is still approximately the same, so the slide in prices puts a lot of pressure on margins.' Mr Bates pointed to supermarkets that often sold CDs at a loss to boost footfall as one factor in the downward pressure on prices. So, is the music industry in terminal decline? Some industry insiders think so. As far back as 1994, Thom Yorke, the lead singer of Radiohead, an English band from Abingdon in Oxfordshire warned apocalyptically of its being 'simply a matter of time - months rather than years - before the music business establishment completely folds'. His advice to young bands: 'Don't tie yourself to the sinking ship, because believe me, it's sinking.' Later, in October 2007, Radiohead shook the industry to the core with their radically innovative pricing strategy. Radiohead, an internationally critically renowned band, took the unusual step of telling fans that they could pay as much or as little as they liked for the band's new album *In Rainbows*. In a break from well-established industry tradition the UK band (famous for hits such as 'Creep', 'Paranoid Android' and 'Karma Police') told its fans 'it's your choice' and that they could pay what they wanted to download the album. This wasn't the first time that a band had opted to charge nothing for a download, but the move was significant because Radiohead are one of the world's biggest bands. Downloading fans could choose to pay as little as €0.50 (the credit card handling fee) or as much as they liked. However, the band also offered a €60 package, which included two CDs, two 'old-fashioned' vinyl albums and an artwork-filled booklet. The boxed set was sold only on its website, allowing the band to control its price. Bryce Edge (one of the band's trio of managers) admitted, 'We can't control how much Tesco will sell [a typical CD] for, nor can the record companies.'

Radiohead was free to sell its album directly from its official website because it is no longer tied to a record label. The previous six releases by the band had been through the

traditional tie-up with a record company. After 16 years with EMI, however, Radiohead split with the record company shortly after it was taken over by the private equity group Terra Firma.

Initially, official sales figures were not released by the band. However, news filtered out that 1.2 million downloads occurred on the day of the release of *In Rainbows*. Industry insiders also responded with widespread reports that Guy Hands, chairman of Terra Firma, had met the management team of Radiohead to discuss bringing the group back to EMI Music. Furthermore, although Radiohead's decision to sell direct to fans was seen as a blow to the traditional music industry, it quickly emerged that the Radiohead management team were in discussions with the four large record companies - Universal Music, Sony BMG, Warner Music and EMI - for help with the traditional CD release. Subsequently, in late 2007 in Europe and early 2008 in North America, *In Rainbows* was released as a traditional CD and reached the number one slot on both sides of the Atlantic. The CD went on to sell over 3 million copies worldwide.

The success of this initial 'pay-as-you-choose' or premium payment for the box set followed by traditionally priced formal CD release pricing strategy was widely acknowledged. Indeed, the decision to release *In Rainbows* online and to allow buyers to pay as little as they like was lauded by some analysts as a ground-breaking model for an industry struggling to compete with free illegal downloads. While some predicted that only the most fanatical of music fans would choose to buy a CD when the download was (almost) free, Radiohead's management were confident that music buyers would recognise the value of both forms of release. 'If we didn't believe that when people hear the music they will want to buy the CD, then we wouldn't do what we are doing,' Bryce Edge told *Music Week*, the UK's industry magazine. Speaking shortly after the online launch, Mr Edge argued that as many as half of those who registered for the download had paid more than the minimum €0.50 transaction fee, but he described the initiative as 'a solution for Radiohead, not the industry', and defended the superior quality of CD recordings. 'You can't listen to a Radiohead record on MP3 [the digital music file standard] and hear the detail; it's impossible,' Mr Edge said. 'We can't understand why record companies don't go on the offensive and say what a great piece of kit CDs are. CDs are undervalued and sold too cheaply.'

Indeed, others in the music industry were less than happy with this new pricing business model. 'While the band, its fans and artists alike are celebrating what looks like a success for Radiohead's bold move in releasing their new album using the "pay what you'd like" model, I think everybody has overlooked one very important aspect of this, and it doesn't bode well for the future of the music industry,' said Michael Laskow,

CEO of TAXI, the world's leading independent A&R (Artist and Repertoire) company. 'Radiohead has been bankrolled by their former label for the last 15 years. They've built a fan base in the millions with their label, and now they're able to cash in on that fan base with none of the income or profit going to the label this time around. That's great for the band and for fans who paid less than they would under the old school model. But at some point in the not too distant future, the music industry will run out of artists who have had major label support in helping them build a huge fan base. The question is: how will new artists be able to use this model in the future if they haven't built a fan base in the millions in the years leading up to the release of their album under the pay what you'd like model?'

In 2007, the year of its release, global revenues in recorded music were €14.27 billion. Three years on, Radiohead were back in the studio. In the meantime the music industry's problems have worsened. In 2009, global recorded music revenues dropped to €12.5 billion, while by 2011, global recorded music revenues fell by 8.4 per cent, about €1 billion, to €11.69 billion according to the annual Recording Industry in Numbers report by international music industry body the IFPI. Overall physical sales, the term used in the industry for sales of products such as CDs, fell by 14.2 per cent year on year to €7.65 billion. Digital revenues grew by 5.3 per cent year on year to €3.38 billion to account for 29 per cent of all recorded music revenues. However, the rate of digital revenue growth has halved year on year as the industry continues to struggle with piracy and winning consumers over to legal download models.

On Valentine's Day (14 February) 2011, Radiohead announced the release of their eighth album *The King of Limbs* (named after a 1,000-year-old oak tree in the Sævernake Forest in the UK). Four days later the album was released via their website. However, this time around, the management of Radiohead tweaked their pricing strategy. Rather than allowing fans to set their own price for digital downloads, this time, the album download was only available for a fixed price. While the download pricing undercut the typical price for a new album from a big artist on digital services such as Apple's iTunes, the band shied away from the 'honesty box' payment system of 2007. In part this decision was based on clear statistical facts. One month after the launch of the 'pay-as-you-choose' album in 2007, comScore, Inc (a leading firm in measuring the digital world) published a report that found that while *In Rainbows* did sell millions of albums and proved that established acts could survive without record labels, three out of five people downloading the album had not paid anything for it. Specifically, of the 1.2 million people who downloaded the album in the first month of release, 62 per cent did not pay anything. According to comScore, downloaders from the US paid on average €4.41, a full euro more than non-US downloaders (who paid on average €3.41). Seventeen per cent of downloading fans paid under €2.94 while only 4 per cent of downloaders paid more than €8.82. Nevertheless, Radiohead stuck with the release of traditional CD and 12-inch vinyl six

weeks later and a special 'newspaper', premium-priced deluxe package with two vinyl records, a CD and numerous sheets of variously sized artwork (at around €35). This prompted Ed O'Brien (guitar and backing vocals) in 2011 to claim that this approach meant that 'We sell less records, but we make more money'.

Talking of Radiohead's pricing strategy, Cliff Fluet, lawyer at Lewis Silkin, said: 'What they are doing is having tiered pricing points and creating new products for fans and evangelists. It's a very smart move.' Gregor Pryor, lawyer at Reed Smith, said: 'In *Rainbows* was a trial. The album was released at a time when people were still uncertain what consumers would pay for music.' 'Radiohead simply conducted an experiment but consumers are now used to paying with a range of retail pricing so there isn't that need anymore.'

Excluded record labels are responding to this threat to their income stream in a variety of ways. Take, for example, the Kaiser Chiefs, the British indie rock stalwarts, who in the summer of 2011 invited fans to create a bespoke version of their new album - choosing tracklisting and cover design. The band, which has enjoyed success with songs such as 'I Predict a Riot' and the chart-topping album *Yours Truly, Angry Mob*, released its new album *The Future is Medieval* not via iTunes but through their own website. The launch is a collaboration between Universal Music and the advertising agency Wieden + Kennedy, which has managed the development of the website and the viral launch, keeping much of the music industry in the dark.

On the website, kaiserchiefs.com, fans are able to select 10 tracks from 20 new songs and create their own version of the album by choosing the playlist and designing the cover. They can download the album for around €8.62. However, the band has also given fans the opportunity to post their versions of the album on Facebook and Twitter - and make money in the process. For every copy of their own version of the album fans sell, they receive €1.15. All sales take place via the band's website using the online payment system PayPal. Only eight sales are required for a fan to start making a profit. Ricky Wilson, the band's lead singer who came up with the idea, says: 'I'd been looking at how people buy music and I thought "Well if that's what you want, we'll give it to you". If people want to buy tracks, let them buy tracks. If people don't want to buy the album you've put together but just buy the tracks they like, all right.' 'You've got to embrace being digital, but the only problem with being digital is that it's not very tactile, there's no ownership over it,' says Wilson. 'It's not just that you get your own artwork and your own tracklisting, it's the experience. The experience of making the album does make the untangible tangible.'

'I think it's really important that we as record labels help bring the value back to music,' says Jim Chancellor, head of Fiction Records, a subsidiary of Universal Music Group, who has been working on the Kaiser Chiefs launch. 'It's becoming harder and harder. It's not just the general perception, its retailers trying to push prices down.'