

The Economist: Finland/World telecoms: Qualms with music

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Cross-subsidised subscriptions offer a promising new model—if the sums add up.

IT IS a gift that keeps on giving—for a year, at least. Starting in Britain this month, buyers of some handsets made by Nokia will be able to download as much digital music as they like. The handsets, starting with a model costing £130 (\$230), are bundled with a year's free online-music subscription, called "**Comes With Music**" (CWM), launched on October 2nd. You can download music, and listen to it, on both the handset and your PC. Once the subscription expires at the end of the year, you can still listen to the tracks.

Nokia's new handsets are sure to appear under many Christmas trees this year. The offer of unlimited downloads will appeal to teenagers; and parents will not have to worry about their children getting caught downloading music illegally, or spending a fortune at online music-stores. But CWM and similar subscription services are also being touted as a potentially life-saving gift to the ailing music industry. That is because they cleverly reconcile the demands of teenagers, who think music should be free, with those of record companies, which want to make money.

The world's biggest handset-maker has pulled this off by acting as a go-between: it licenses music from the four major labels and some independent record firms at a discount, tags some of the cost onto the device's purchasing price and absorbs the rest itself. Such a deal is made possible by a convergence of interests. Sales of digital music are growing, but not fast enough to offset falling sales of CDs, partly because of internet piracy (see chart). Record companies are realising that their efforts to get young music fans to pay up are not working. Many are unwilling, or unable, to pay for downloads, and legal action results in bad publicity. So something new is needed. Nokia, for its part, wants to move beyond hardware, and considers music a way to kick-start Ovi, its new initiative to offer a range of mobile-internet services.

Both camps also have a common interest in reining in Apple, the computer-maker that dominates digital music with its iTunes download service and iPod music-players. At the moment, record labels have to accept Apple's terms. A strong rival service

from Nokia could strengthen their negotiating hand. As for Nokia, it hopes to catch up with iTunes and defend its core market against Apple's iPhone handset.

CWM is the most prominent example of a wider trend. Other companies have also started to combine their offerings with similar "all you can eat" music subscriptions. TDC, a Danish telecoms operator, has bundled such a service with its broadband connections. Orange, a European mobile operator, has launched Musique Max, which combines unlimited music downloads with a mobile-broadband service for €12 (\$17) a month. And Sony Ericsson, another handset-maker, is planning to launch an unlimited music service called "PlayNow plus", which will be offered to consumers via mobile operators.

Will this new model work? For the record labels CWM is likely to be a good deal. If they receive, as some analysts have estimated, a total of €4 (\$5.60) per handset per month (about half the cost of all-you-can-eat subscription services on the internet) and Nokia sells 5m CWM handsets, the additional income would add up to €240m (\$338m)—equivalent to more than 1% of global recorded-music sales in 2007 and 12% of the digital business. The potential market is far bigger: last year Nokia sold 146m phones that can play music.

But Paul Jackson of Forrester, a market-research firm, worries that Nokia will end up overpaying. The firm has not released details of its agreement with the record companies, but it is said that they will receive a fixed fee per handset, have been guaranteed a large number of handset sales, and will receive additional fees once a subscriber exceeds a certain number of downloads. So the promise of "unlimited" music is actually subject to a "fair use" limit, beyond which access will be cut off.

The economics of CWM will become clearer when Nokia reveals what exactly will happen after the 12 months of free downloads are over. The company hopes that most owners will simply buy a new CWM handset, says Elizabeth Schimel, the head of Nokia's music business, since teenagers like to be seen with the latest model. (CWM could thus encourage people to upgrade their handsets more often than they otherwise would have.) But customers will also be offered the chance to switch to Ovi's paid-for music service.

The cost of that service will indicate the extent to which Nokia is underwriting the free CWM service. The level of subsidy will also determine how long CWM will remain in its current form. At the moment, Nokia's priority is to get Ovi off the

ground. But over time, the firm's willingness to absorb some of the cost of a music subscription may well diminish, says Mark Mulligan of Jupiter, another market-research firm. Either the labels will have to make do with less, or other firms, such as the mobile operators, will have to pitch in. Consumers are unlikely to contribute much, simply because they will refuse to: take-up of subscription-based music services has been disappointing so far.

Even if the sums do add up, the new model may face other problems. To start with, the services will be available in only a few countries and will not compete directly: CWM in Britain (and, perhaps, India soon), Musique Max in France and PlayNow plus in Sweden. But as these services spread and start to compete, consumers may object to the fact that they are not compatible with each other. Next, record labels may have second thoughts about appearing to allow other firms to give away their wares—even if they are, in fact, paid for behind the scenes. Subsidised subscriptions will only strengthen the widely held belief that music should be free. "They are another step in the commoditisation of music," says David MacQueen of Strategy Analytics, a consultancy.

That said, unlimited music services could help to reduce piracy, by making it unnecessary. With services such as CWM, "the person with a hard-drive with 60,000 stolen files is all of a sudden deeply uncool, as other people have access to everything," says Rob Wells, a senior executive at Universal, the world's biggest record company and the label that is most keen on CWM. But they could also undermine people's willingness to pay for CDs and music downloads from iTunes and other online stores, as avid consumers of music switch to unlimited, free services instead.

"CWM is almost too good for its own good," says Jupiter's Mr Mulligan. The impact of such services is uncertain; there are many details still to be worked out; and even then they will not solve all of the industry's problems. But they are potentially a big step forward.