



The Canadian Music Industry

2004 Economic Profile



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About the 2004 Economic Profile

This document is the first annual economic profile on the Canadian sound recording industry produced by the Department of Canadian Heritage. It provides information on the Canadian and International sound recording markets and music copyright royalties in Canada.

The Department of Canadian Heritage would like to thank Paul Spendlove for writing this profile.

Special mention is also extended to:

- Mary Ann Fulop (Financial Controller, Society of Composers, Authors and Music Publishers of Canada)
- Vanessa Thomas (General Manager, Nielsen Music, Nielsen Home Entertainment)
- Al Mair (President, MHL Communications)
- Jennifer Hardy (Manager of Administration, Canadian Recording Industry Association)

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Minister of Canadian Heritage and
Minister responsible for Status of Women



Ministre du Patrimoine canadien et
ministre responsable de la Condition féminine

Ottawa, Canada K1A 0M5



In recent years, Canadian artists have achieved considerable success both nationally and internationally. The work of those who showcase their talent has greatly contributed to the growth of our sound recording industry.

Today, the industry of which we are so proud, faces major challenges, particularly with respect to copyright. The economic profile of the Sound Recording Industry provides an opportunity for us to share ideas. It will help us discuss what we can do, within the industry, so that our artists and key players in the music world can contribute to our cultural vitality.

As Minister of Canadian Heritage, I would like to thank all the people who have devoted their lives to music, as well as all those who give the artists the tools they need to succeed. Thanks to your commitment, the influence of our culture is felt far beyond our borders.

A handwritten signature in cursive script that reads "Liza Frulla".

Liza Frulla

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OVERVIEW

Overview

The music industry is constantly evolving. Styles of popular music, change at a dizzying rate, requiring artist & repertoire (A&R) departments at record labels to stay on their toes. More notably, the latest shift in music format and consumer behaviour—to the online realm—has the global music industry playing catch-up. The result: five years of declining music sales.

Between 1999 and 2003, the value of music sold dropped 28%, from \$1.3 billion to \$946.4 million.

This downturn is as true in Canada, the world's sixth largest music market, as elsewhere. Between 1999 and 2003, the value of music sold dropped 28%, from \$1.3 billion to \$946.4 million.¹ Last year, the decline in value was 2.9%, and some predict the slump to continue for at least another year.

Ironically, the last few years have been a period of incredible success for Canadian artists, both at home and abroad. On the strength of releases from the likes of Céline Dion, Shania Twain, Avril Lavigne and Nickelback, Canadian artists' share of the top 200 best selling albums in Canada has increased from 15.1% in 2001 to

27.2% in 2003.² During the same period, while sales of albums by foreign artists in the top 200 continued to decline, albums by Canadian artists—led by Shania Twain, Avril Lavigne, Sarah McLachlan and Diana Krall—actually grew 36.8%.³ It's little wonder that in a recent survey conducted by Millward Brown, more than 90% of Canadians said they consider the quality of music produced by Canadian artists to be equal to or better than that of foreign artists.⁴

Canadian artists' share of the top 200 best selling albums in Canada has increased from 15.1% in 2001 to 27.2% in 2003.

Canadians also shone on the international stage, based on foreign album sales as well as performing rights royalties collected by the Society of Composers, Authors and Music Publishers of Canada (SOCAN). Between 1999 and 2003, Canadian artists garnered 144 album certifications from their three largest foreign markets alone—the United States, the UK and France. Performing rights royalties from international sources have flowed to SOCAN songwriters, composers and publishers in higher numbers, reaching \$47.3 million

in 2003, 68.3% higher than 1999 levels, according to SOCAN.⁵ In fact, 2002 and 2003 are the first years in SOCAN's history that royalties revenues from international sources have exceeded royalties paid out to foreign songwriters, composers and publishers. In 2003 more of SOCAN's distributions of domestic collections went to its own members than to non-SOCAN members in addition to virtually all of the incoming international revenue.

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As for the Canadian retail market, there are signs the worst may be over. The retail value of music may have declined 2.9% in 2003, but this was the lowest drop in five years, and less than half the fall in value of global music sales. And by September 2004 there were signs of a possible recovery, as unit sales in the first nine months of the year grew 5.0% over the same period last year.⁶ Similar growth has been noted in the US and UK, pointing to a possible larger global recovery. But that recovery may take time: at least one forecaster does not expect Canada's sales to return to growth until 2006.⁷

The Impact of the Sales Slump

A turnaround may come too late for some in the industry. Staff layoffs are reported to have occurred over the past year, particularly as a result of restructuring at the larger labels. Although detailed statistics on industry employment are unavailable, the Canadian Recording Industry Association (CRIA) estimates that 20% of industry jobs have been cut in the past year. Some also fear that the 2004 merger between the Sony Music Group and BMG could lead to further job losses.

Falling music sales have also led to some turmoil at the retail level. Following consumer trends, retailers have devoted more shelf space to DVD movies and computer games while reducing their music inventory, leading to tension between retailers and distributors. The most notable fallout came in early 2004, when EMI decided to withdraw its volume discounts from retail leader HMV, claiming sales of its product at HMV had dropped 25% in 2003. HMV responded by raising the price of EMI distributed albums, including those of many Canadian independent labels, and relegating them to the back of the store.⁸

Some observers believe the compact disc, the dominant sound carrier format since the late 1980s, is simply past its prime, following a wave of strong sales in the 1990s as consumers replaced their older formats in their music collections. In Canada, CD unit sales have fallen steadily in the past five years, from 71.9 million in 1999 to 53.1 million in 2003. Other formats have not fared much better; except for a brief jump largely due to the Canadian Idol and *Star Académie* franchises, singles sales are still marginal, while the cassette format could soon disappear entirely at its current rate of decline. The only format to show signs of growth is the music video DVD, which saw sales grow 150% from 2002 to 2003, the highest increase among the top ten music markets in the world.⁹ However, with total unit sales of four million in Canada, the music DVD's impact remains limited.

Besides the decline of the CD and competition for retail shelf space from other sources of entertainment, other potential factors in the fall of music sales range from the cost of music to a sense of diminishing star-power in the charts. For example, the top ten albums in 1999 totalled 5.9 million units, compared with 3.4 million units in 2003.¹⁰ For many in the industry, however, the biggest challenge is the Internet.

The Downloading Phenomenon

While certainly not the only factor in the drop in music sales, widespread downloading of free digital files, MP3s in particular, has received the most attention. Though file sharing on peer-to-peer (P2P) networks such as Kazaa and Grokster is considered to have peaked in 2003, the International Federation of the Phonographic Industry (IFPI) estimated the number of copyrighted music files on P2P networks worldwide in early 2004 at 800 million, with another 100 million on Web and FTP (file transfer protocol) sites.¹¹

Canada, with one of the highest rates of Internet penetration in the world, has experienced its fair share of downloading. Recent studies suggest that 32% of adult Internet users in Canada have downloaded a music file at least once,¹² with rates of downloading in Canada estimated to be as high as 180 million tracks per month.¹³

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In the United States, the Recording Industry Association of America's response to the downloading phenomenon has been to sue individual computer users offering large

numbers of copyrighted music files on P2P networks. In Canada, however, the recording industry's efforts to do the same have so far been impeded by a couple of widely publicized court cases.

On March 31, 2004, Federal Court Justice Konrad von Finckenstein ruled against the Canadian Recording Industry Association's (CRIA) attempt to require five Canadian Internet service providers (ISPs) to reveal the names of individuals whom CRIA believes illegally made available thousands of songs on file sharing networks. In his decision, the judge asserted that placing a music file in a computer directory that others might share did not constitute copyright infringement under Canadian law, comparing it to a library placing a photocopier near its books. "In either case the preconditions to copying and infringement are set up but the element of authorization is missing," he wrote. Justice von Finckenstein also cited the *Copyright Act*, which preserves the private copying rights of individuals while compensating the recording industry by way of a levy on recording media.

In June, the Supreme Court of Canada ruled unanimously against a Society of Composers, Authors and Music Publishers of Canada (SOCAN) request for a tariff setting up a royalty structure for ISPs,

stating that ISPs were not responsible for copyright infringement when they communicate copyright works to the public if they only provide the means necessary for others (websites) to communicate.

Reactions to the court cases have varied. Consumer and privacy advocates have claimed that Justice von Finckenstein's decision was a victory for users' rights that amounted to the legalization of file sharing on P2P networks. CRIA and other Internet experts argued it represented a basic misunderstanding of how such networks operate. CRIA has appealed the federal court decision.

Meanwhile, industry players hope new pay-per-download services can harness the popularity of the digital music format and translate it into sales. The first Canadian-based pay-per-download site, Moontaxi Media's Puretracks.com, was launched in late 2003, followed this year by *Groupe Archambault's* Archambaultzik.ca, the American-based Napster 2.0, and Bell's Sympatico Music Store. By February 2004, Puretracks had proclaimed its launch a success, announcing it had sold one million downloads. The company has also expanded its service in Canada, powering the music store Web sites for Bell Sympatico and electronics retailer Future Shop. Yet compared with the

United States—where Apple’s iTunes sold its 100 millionth download in July—Canada clearly has a ways to go; one 2004 survey found that only 15% of Canadian downloaders had ever purchased a music file.¹⁴ Signs of rapidly increasing download sales in the United States in 2004, however, suggest that the market has strong potential for growth.

There has been speculation that radio is the next traditional music medium to be adversely affected from the digital revolution. This is not immediately apparent from listenership numbers, as the average number of hours per week Canadians listen to the radio only dropped one hour, to 19.5 hours per week, between 1999 and 2003. But for the next generation of listeners, the drop was more substantial: Canadian teens aged 12 to 17 listened to the radio an average 8.5 hours a week in 2003, down from 11.3 in 1999.¹⁵ The fact that teens’ TV watching has shown a similar drop, while time spent online has grown, supports the hypothesis that the next generation will turn more to the Internet for its entertainment than to traditional sources.

Canadian teens aged 12 to 17 listened to the radio an average 8.5 hours a week in 2003, down from 11.3 in 1999.

Innovation in the Music Industry

As in the past, the Canadian music industry will continue to adapt strategically to economic and technological changes, through creativity and innovation. A recent demonstration of the industry’s ingenuity is the development of the online pay-per-download model.

Some independent music labels, taking advantage of their size and relative flexibility, have responded to the sluggish recording market by shifting their business strategy. Vancouver-based Nettwerk, for one, has expanded its lucrative artist management division, with the result that album sales now make up just 20% of the company’s revenues.¹⁶

At the retail level, prices for CDs have been coming down. This year, Universal brought its “JumpStart” price reduction program to Canada, reducing the wholesale price of CDs by up to 32%. The plan, launched last year in the United States, began a general trend of price reduction that is said to have contributed to a recovery in the American market ahead of many forecasts.¹⁷

In addition, it’s probably just a matter of time before Canadians tap into the market for the latest and most improbable music format, the cellular phone ringtone. Surveys show 18% of Canadian mobile phone owners have downloaded ringtones to their mobile; among respondents, 5% said they would definitely buy “master recording” ringtones should they become available, while 25% would probably buy them.¹⁸

That a market still exists for music in Canada, and for Canadian artists, is without question. The challenge for the industry, it seems, is how best to deliver music to a new generation of consumer who would rather point and click their way to listening satisfaction.



I—CANADIAN MARKET



I—Canadian Market

Sound Recordings in Canada— Retail Sales and Market Trends

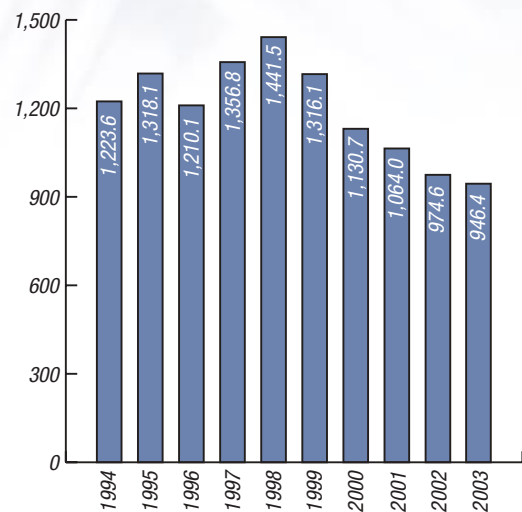
Retail sales for sound recordings in Canada declined 2.9% from 2002 to 2003, continuing the downward trend that began after its peak in 1998. Total retail value of the Canadian sound recording market in 2003 was \$946.4 million, down from \$974.8 million the year before. Since 1999, the market's retail value has dropped 28.1%.¹⁹

Unit sales of albums in the top 200 by Canadian artists grew 36.8% between 2001 and 2003, while foreign artists have shown a steady decline, falling 34.8% in the same period.

Compact disc sales declined 7%, from 57 million units to 53.1 million in 2003. Cassette tapes continued their slide, with 64% fewer units sold. Sale of singles jumped 50%, due largely to Canadian

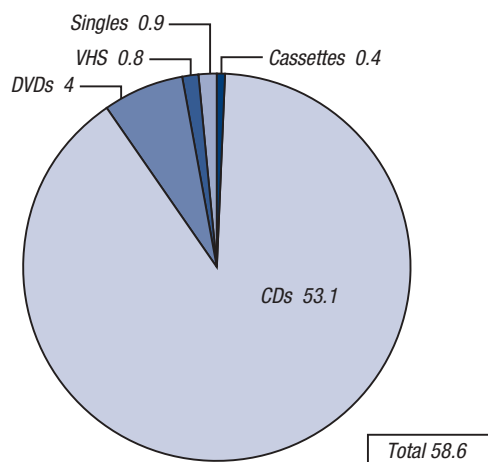
Idol and *Star Académie* output. The most growth by format was posted by DVD music videos, a trend seen in most major world markets, though the quantities for this relatively new format are still marginal. Sales of music DVDs in Canada grew 150%, to four million units sold, from 1.6 million the year before.²⁰

Retail Sales of Recordings
in Canada (\$000,000 CAD)



Source: Music & Copyright, July 7, 2004.

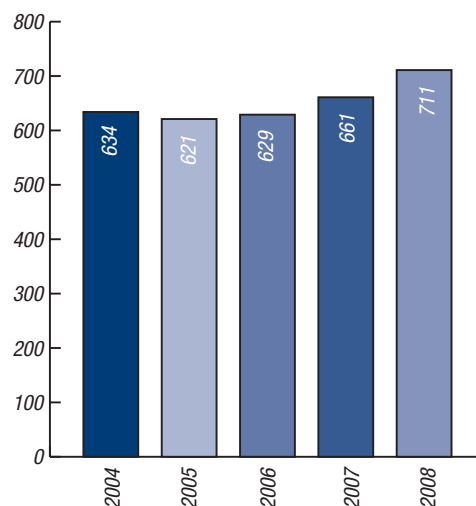
2003 Retail Sales of Recordings in Canada—by Format—Units (000,000)



Source: Music & Copyright, July 7, 2004.

By September 2004, the market was showing signs of growth, with unit sales in the first nine months rising 5.0% over the same period the year before, according to Nielsen SoundScan. This growth was led by the mass merchant sector, with unit sales 8.9% higher than the same previous year period, compared with 3.6% unit sales growth at traditional retail outlets.²¹ Despite this positive news, some analysts do not expect sales to recover this year. Pricewaterhouse Coopers, for one, forecasts Canadian music sales to fall 3.4% in 2004 and a further 2.1% in 2005 before rebounding 1.3% the following year.²²

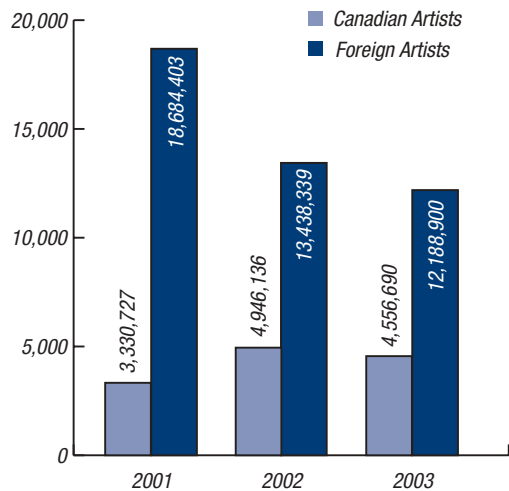
Forecast—Recorded Music Sales in Canada (\$000,000 US)



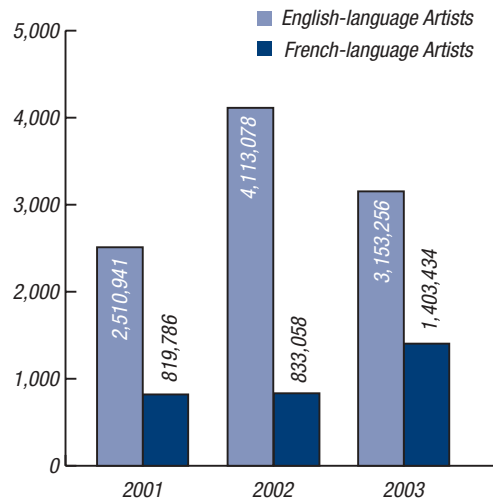
Source: Pricewaterhouse Coopers, Wilkofsky Gruen Associates from Music & Copyright, July 21, 2004.

Canadian recording artists have fared better than their foreign counterparts in the national market, according to Nielsen SoundScan. Of the top 200 albums in Canada, accounting for around 25% of total annual album sales, Canadian artists' share of units sold has been on the rise since 1998, reaching 27.2% in 2003 with sales of 4.6 million units.²³ Unit sales of albums in the top 200 by Canadian artists grew 36.8% between 2001 and 2003, while foreign artists have shown a steady decline, falling 34.8% in the same period. The proportion of albums by Canadian artists on Nielsen SoundScan's top 200 list has also increased, rising from 18% in 2001 to 26% in 2003.²⁴

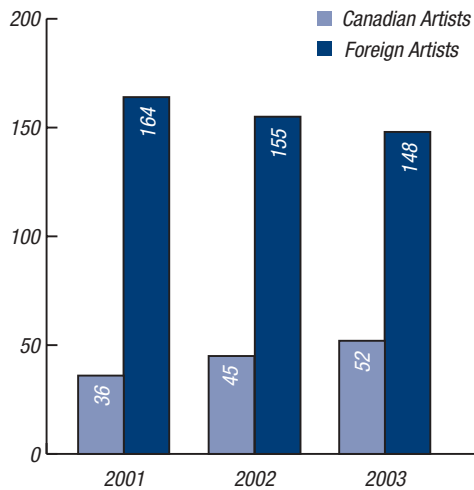
Nielsen SoundScan Top 200—Album Sales in Canada by Artist Nationality—No. of Units



Nielsen SoundScan Top 200—Sales of Canadian Albums in Canada by Language—No. of Units

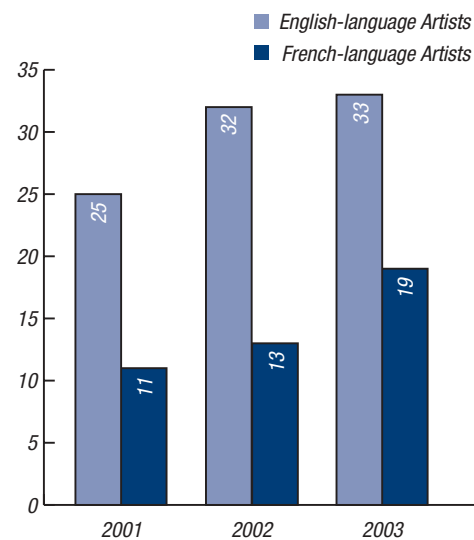


Nielsen SoundScan Top 200—Album Sales in Canada by Artist Nationality—No. of Titles



Source: Nielsen SoundScan

Nielsen SoundScan Top 200—Sales of Canadian Albums in Canada by Language—No. of Titles



Source: Nielsen SoundScan

New Recordings Released by Canadian Artists

Since 1999, the number of annual new recordings by Canadian artists has increased 63.3%, from 1,261 in 1999 to 2,059 in 2003. English-Canadian releases, however, accounted for the full amount of that growth, jumping from 1,043 in 1999 to 1,859 last year, while hitting a high of 1,911 in 2002, according to the Canadian Music Industry Database (CMID).

New Albums Released by Canadian Artists—by Language

	1999	2000	2001	2002	2003
French-language	218	205	236	223	200
English-language	1,043	1,310	1,505	1,911	1,859
Total	1,261	1,515	1,741	2,134	2,059

Source: CMID & Société de gestion collective des droits des producteurs de phonogrammes et de vidéogrammes du Québec (SOPROQ)

The number of French-language releases in the last five years has stayed comparatively constant, ranging from a low of 200 in 2003 to a five-year high of 236 in 2001, according to the Société de gestion collective des droits des producteurs de phonogrammes et de vidéogrammes du Québec (SOPROQ).

Breakdown by Genre

Of the 2,059 new Canadian productions released in 2003, by far the largest share, 54.9%, were rock/pop recordings, followed by country and folk (16.4%), urban and dance (9.8%), jazz and blues (7%), world music (3.6%) and classical (3.1%). Other genres totalled 5.2% of releases.

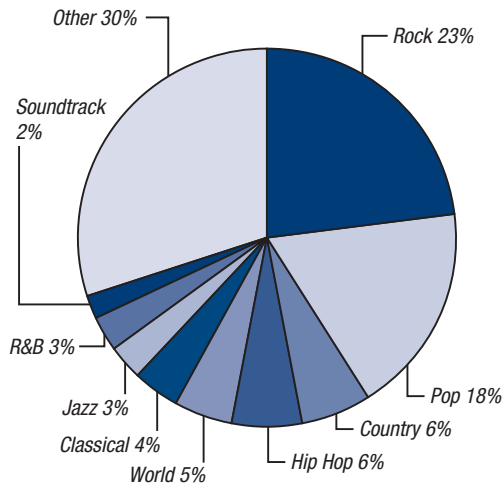
New Albums Released by Canadian Artists (2003)

Genre	No. of Recordings	% of Total
Classical	63	3.1%
Country and Folk	338	16.4%
Jazz and Blues	144	7.0%
Other	108	5.2%
Pop/Rock	1,130	54.9%
Urban and Dance	202	9.8%
World Music	74	3.6%
Total	2,059	100.0%

Source: CMID & Société de gestion collective des droits des producteurs de phonogrammes et de vidéogrammes du Québec (SOPROQ)

The proportion of releases by genre is also reflected in sales. According to the International Federation of the Phonographic Industry and the Canadian Recording Industry Association (CRIA), rock and pop recordings accounted for 51% of total sales, followed by country (6%), Hip Hop (6%), world music (5%), classical (4%), jazz (3%), R&B (3%), and soundtrack (2%). Other genres combined for a 30% share.

Album Sales by Genre in Canada (2002)



Source: IFPI Recording Industry in Numbers, 2003.

Gold and Platinum Records and Other CRIA Certifications Statistics

Canadian artists were awarded a total of 42 album certifications in 2003 by CRIA, down significantly from 71 such awards in 2002. The 2003 awards included 27 gold, 6 platinum, 8 multi-platinum and one diamond album. This last award went to Avril Lavigne for *Let Go*, which has sold more than a million copies.

Canadian Artists Canadian Album Certification Awards (CRIA)

	Gold	Platinum	Diamond	Total	Artists
1999	28	41	3	72	60
2000	29	30	2	61	52
2001	24	24	1	49	40
2002	35	35	1	71	58
2003	27	14	1	42	40

Source: PCH compilation of CRIA data.

Note: Only the highest certification given to an album in a given year is included.

Platinum and multi-platinum albums, for sales of more than 100,000 units, went to such artists as Diana Krall (*Live in Paris*), Michael Bublé (*Michael Bublé*), Bruno Pelletier (*Concert de Noël*) and Sam Roberts (*We Were Born in a Flame*), as well as to such compilations as *Star Académie* and *Oh Canada—A Canadian Celebration*.

Gold albums, awarded for sales of 50,000 units, went to La Chicane (*Ent'Nous Autres*), Chantal Kreviazuk (*What If It All Means Something*), Billy Talent (*Billy Talent*) and Nicola Ciccone (*J't'aime tout court*), among others.

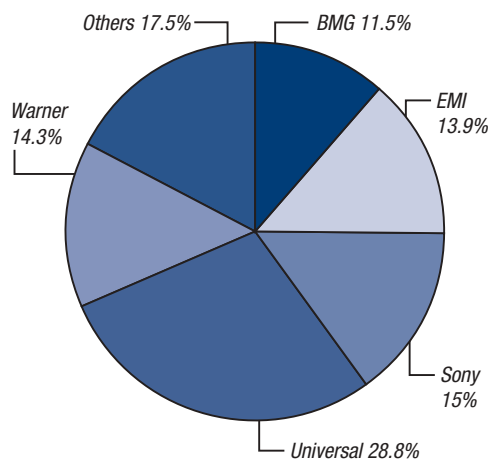
Canadian Companies

The four major labels and approximately 300 independents in Canada share a music market that, these days, is worth around \$950 million in annual revenues. (By comparison, the Canadian book publishing industry brings in about \$2.4 billion in revenues annually.)²⁵

Warner, EMI, Universal and the newly-minted Sony BMG account for more than 80% of sales in Canada, with the largest share of the market going to Universal (30%) followed by Sony and BMG's combined 27%. Although the majors get most of their earnings from foreign releases, they are also home to some of the most commercially successful Canadian artists, including those with a significant international profile. In 2000, foreign-owned firms—including the five majors and 11 foreign "indies"—released 16% of the product of Canadian artists, yet captured 54% of sales of Canadian artists.

The approximately 300 Canadian independents, for their part, play a significant role in developing Canadian talent, accounting for more than 80% of all Canadian

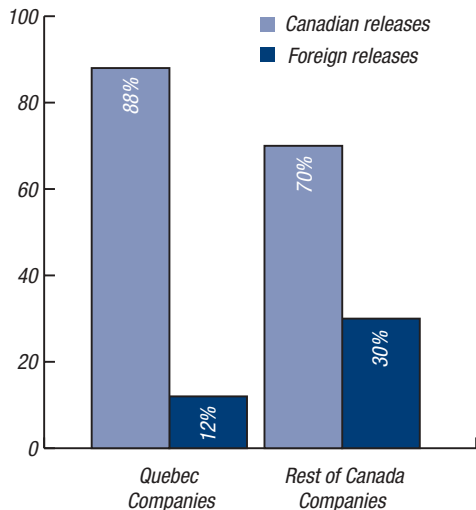
Album Sales Market Shares
in Canada (2003)



Source: Nielsen SoundScan—Music & Copyright, July 7, 2004.

releases each year, with an estimated total market share of 15%.²⁶ Releases by Canadian artists account for approximately 90% of revenue for smaller labels (firms earning less than \$1 million in a year) and 77% for firms earning more than \$1 million annually. About a dozen labels are responsible for 80% of the roughly \$200 million earned by independents (about 12% of total sales).²⁷ The reality of day-to-day business for the hundreds of Canadian "micro" labels is intense dedication by a small part-time staff working on a shoestring budget.

Sound Recording Revenues by Origin of Releases



Source: Profile of the Sound Recording Industry in Canada, Nordicity Group Ltd.

In the province of Quebec, independents have long dominated a small but self-sufficient French-language music market. Around 100 Quebec independent labels produce approximately 200 albums per year, accounting for around 90% of French-language releases and between 25% and 30% of annual sound recording sales in the province, according to the *Association québécoise de l'industrie du disque, du spectacle et de la vidéo* (ADISQ).²⁸

Foreign-owned and Canadian labels are not, however, isolated from each other, and many share business arrangements and resources. In many cases, independent

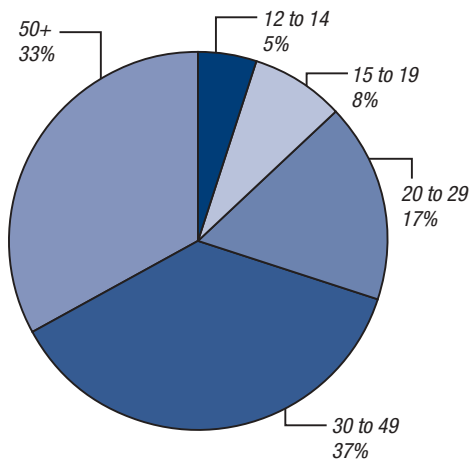
labels are distributed through the major foreign-owned labels, while some have marketing arrangements with the majors, as well.

65% of Canadians say they regularly or occasionally buy recorded music.

The Canadian Music Consumer

Demographics and public opinion research combine to paint a picture of a typical Canadian music consumer who is a long way from their teen years. We are a nation of keen music enthusiasts that are strongly supportive of Canadian artists, with 54% of Canadians saying they listen to recorded music (cassettes or compact discs) at least several times a week, while 19% listen to music once a day or more. As well, a 2003 survey by Millward Brown reports that 65% of Canadians say they regularly or occasionally buy recorded music.²⁹ More than two-thirds of music consumers are over 30 according to 2002 data from International Federation of the Phonographic Industry (IFPI).³⁰ This comes as no surprise to industry players, basking in the success of jazz-influenced adult contemporary artists like Diana Krall and Michael Bublé, not to mention the phenomenal success of American artist Norah Jones.

Sales by Age in Canada (2002)



Source: IFPI—Recording Industry in Numbers, 2003.

Surveys also show Canadians have a high regard for music by Canadian artists. A 2003 survey by Millward Brown, reports a large percentage, 92%, believes that the quality of music produced by Canadian artists is equal to or better than that of foreign artists. And when asked whether Canadian musicians are important in supporting Canadians' sense of cultural identity, 86% of respondents agree (39% agree strongly, 47% agree somewhat),³¹ while 77% of Canadians believe that it is important to buy or listen to music that is made in Canada (29% very important, 48% moderately important).³²

A 2003 survey by Millward Brown, reports a large percentage, 92%, believes that the quality of music produced by Canadian artists is equal to or better than that of foreign artists.

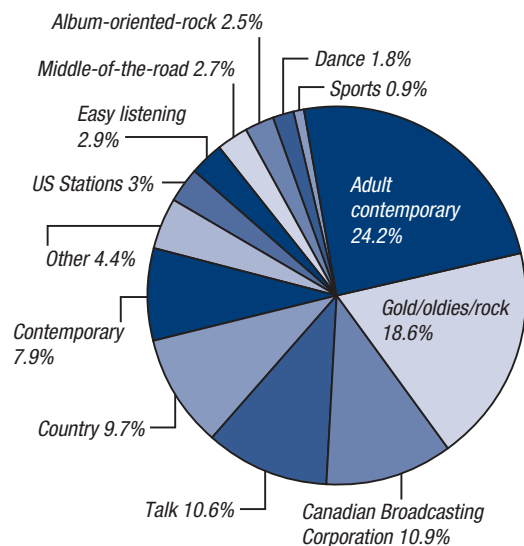
Radio Audiences

In 2003, Canadians spent on average 19.5 hours per week listening to the radio, one hour less than in 1999, according to the latest survey data from Statistics Canada. However, the amount of time spent by teenagers aged 12 to 17 listening to the radio has fallen steadily for a number of years, from 11.3 hours per week in 1999 to 8.5 hours per week in 2003. The most avid radio listening demographic in Canada is women over 65, at 23.5 hours per week, followed by men aged 35 to 49 at 22.3 hours per week.³³

The three most popular radio formats in Canada, unchanged from 2002 to 2003, are adult contemporary (with a 24.2% share of the audience), golden oldies and rock (18.6%) and the Canadian Broadcasting Corporation (10.9%), followed by talk radio (10.6%), country (9.7%) and contemporary music (7.9%). Among teens, the

top formats are adult contemporary music (22.2%), gold/oldies/rock (21.5%) and contemporary music (20%). In 1999, teens strongly preferred contemporary music (42%), but this format has been in decline in recent years, with several stations making the switch to adult contemporary and golden oldies formats.

Percentage Share of Radio Listening by Format in Canada—Fall 2003



Source: Statistics Canada: Radio Listening Data Bank, Fall 2003; Radio Listening data tables, July 2004, catalogue no. 87F0007XIE.

Downloading and New Technologies

There has been an ongoing debate on the impact of file sharing over P2P networks. Many in the sound recording industry would say that it hurts music sales, and most recent surveys seem to support this view. A survey by Pollara sponsored by the Canadian Recording Industry Association (CRIA) found that only 35% of Canadian music consumers who download music files are likely to have purchased music in the previous month, compared with 52% of music consumers who do not download.³⁴ And among music consumers who said they had spent less on music in the past year, 28% said downloading and CD burning were the main reasons that their purchases had declined.³⁵

However, one recent study by two American researchers found that file sharing had no effect on CD sales. Using data from file sharing servers in the second half of 2002, the researchers, from the Harvard Business School and the University of North Carolina, found no significant correlation between file sharing habits and the large drop in US CD sales between 2000 and 2002. They also found that for the most popular 25% of albums, downloading had a positive effect on sales.³⁶

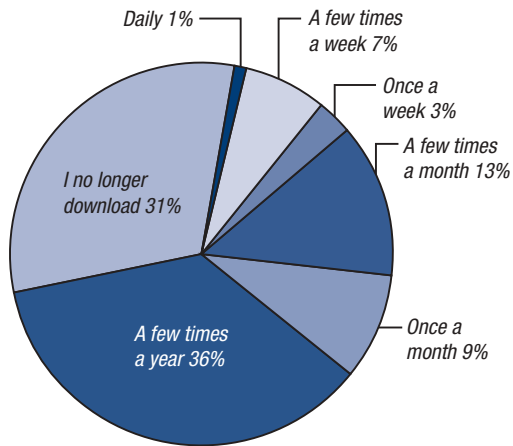
The International Federation of the Phonographic Industry, though clearly opposed to P2P file sharing, has acknowledged that total music consumption, including music sales and downloading, grew 30% between 1997 and 2002 in five major world markets, including Canada. Though many in the industry hope this will translate into demand for commercial downloading services, so far this has primarily been led by the United States. Between late 2002 and 2003, the percentage of U.S. downloaders 12 and up who paid to download tracks almost tripled, from 8% to 22%, while in Canada, only 15% of downloaders had purchased a music file by early 2004.

Canada's pay-per-download industry, for that matter, is still in its infancy. By mid-2004, three players had established themselves in the Canadian market—Puretracks.com, Archambaultzik.com, and American-owned Napster. Each service provides approximately 300,000 songs to consumers, compared with iTunes' more than 700,000 tracks in the United States. Major and independent music labels, however, continue to sign with these services at a rapid rate as industry resistance to the

digital file format diminishes. Meanwhile, public opinion research shows a market for such services exists in Canada, with 56% of downloaders saying they would prefer to download music from a legitimate online music downloading service than purchase a CD from a record store.³⁷

Some believe, however, that pay-per-download services will remain marginal until the rate of free file sharing declines. Though file sharing from sites like Kazaa seems to be no longer at its peak—particularly in the United States where casual downloaders have retreated from the threat of lawsuits by the Recording Industry Association of America—the latest figures show file sharing to be on the rise in Canada. One survey in spring 2004 found that half of Canadians age 12 to 19 said they downloaded a music file in the past month—lower than the peak of 60% in spring 2003, but higher than the 40% who shared files at least once a month near the end of 2003.³⁸

Frequency of Downloading of MP3 Files from Internet by Canadians



Note: universe—422 respondents who have downloaded an MP3 file.

Source: The Canadian inter@ctive Reid Report—
Music Downloading in Canada: Past, Present and Future,
A Special Feature / Spring 2004.

31% of Canadians who admit to have downloaded music files at some point also say they no longer do so.

Still, another recent study found that 31% of Canadians who admit to have downloaded music files at some point also say they no longer do so. Many seem to take legality into account: according to the study, Canadians who have stopped downloading say concerns about the legal aspects were the main factor.³⁹ What effect the March 2004 federal court decision will have on the frequency of file sharing is not yet known.



II—INTERNATIONAL MARKET



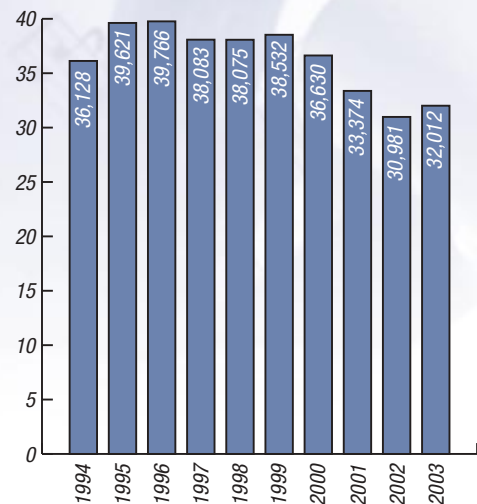
II—International Market

World Sales and Market Trends

In July 2004, American and European antitrust regulators approved the merger of the Sony Music Group and BMG, clearing the way for the 50/50 joint venture. The regulators said there was insufficient evidence that the merger, which reduces the number of major music labels from five to four, would negatively affect consumers.

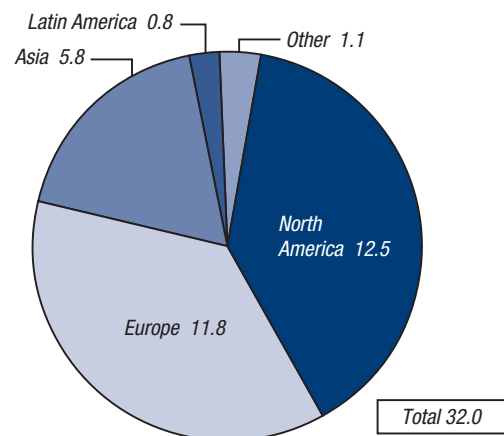
The creation of Sony BMG comes in the wake of the fourth straight year of a global decline in sound recording sales. According to the International Federation of the Phonographic Industry (IFPI), worldwide sales in 2003 fell 7.6% in constant US dollars.⁴⁰ Among major markets, the largest declines were seen in Europe. Germany and France saw sales plummet 19% and 14.4%, respectively, while Spain's sales fell 9.4%. As a region, Europe, which accounts for 37% of the world market, saw sales decline 8.7%, compared with a 5.9% drop in North America. Japan, with a 15.5% share of the global market, saw sales fall 9.2%.

World Retail Value—Recorded Music Sales—Market Value (\$000,000 US)



Source: IFPI—Music & Copyright, April 28, 2004.

Retail Value by Region—
(\$000,000,000 US Variable) (2003)



Source: IFPI—Music & Copyright, April 28, 2004.

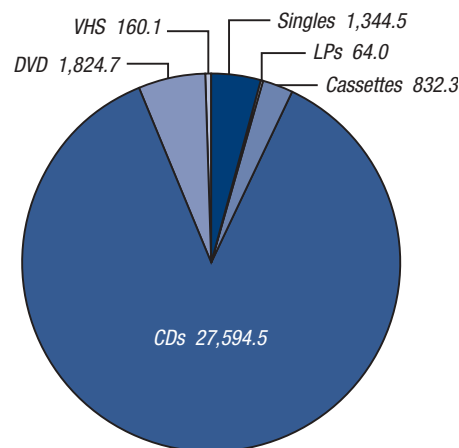
Retail Recorded Music Sales Ranking by Value (2003)

2003 Rank	Country	Value— (\$000,000 US)	% of World
1	USA	11,848	37
2	Japan	4,910	15
3	UK	3,216	10
4	France	2,115	7
5	Germany	2,022	6
6	Canada	676	2
7	Australia	674	2
8	Italy	645	2
9	Spain	596	2
10	Netherlands	499	2

Source: IFPI—Music & Copyright, April 28, 2004.

The global retail value of CDs, which account for 86.2% of the value of music sold, fell by 9.1%. The only retail format to show growth is the music video DVD, representing 5.7% of market value. Spurred by widespread adoption of DVD player technology, the format's global retail value climbed 67%. Among the top 10 music DVD markets, which collectively accounted for 90% of global music DVD sales, Canada posted the highest level of growth in 2003, at 150%.

The World Retail Value of Recorded Music Sales—by Format (\$000,000 US) (2003)



Source: IFPI—Music & Copyright, April 28, 2004.

There are signs of recovery in some markets. The UK, representing 10% of world sales, and Australia, representing 2%, both saw growth in 2003, by 0.1% and 5.9%, respectively. The United States, with a 37% share of the world market, saw its sales decline slow in the second half of 2003. According to Nielsen SoundScan, unit sales in the United States in the last three months of 2003 were 10.5% higher than in the same quarter in 2002, while album sales were up 5.6%. That trend has continued into 2004; for the first five months of the year, album sales in the United States were up 7% over sales for the same period in 2003, and sales of downloads were also higher.⁴¹

As in Canada and the United States, the global music industry considers music file swapping and CD burning to be the major cause of falling sales. According to IFPI, global unit sales of counterfeit CDs grew 4% in 2003 to 1.1 billion units, more than one-third of all CDs sold worldwide.⁴²

However, technology has also given rise to a new commercial format, the mobile phone ringtone. The phenomenon, in which users can purchase basic versions of popular tunes from commercial Web sites and download them to their handset, is so far only established in Europe and Asia, where mobile phone penetration is much higher than in North America. But it has already shown promise: in the UK in 2003, ringtones of recordings sold as singles often outsold the actual singles.⁴³ A recent survey shows a potential market for ringtones in Canada; though master recording ringtones were not available in 2003, 30% of survey respondents said they would consider buying them, when available.⁴⁴

The Canadian Music Industry on the International Scene

Canada has established a solid reputation for producing music artists with worldwide commercial appeal. Over the past decade, Canada's top ten recent international success stories together have sold 359.5 million units around the world, grossing around \$5.4 billion (US), based on average retail price of \$15 (US) per album. Leading the way is Céline Dion, with sales of 150 million units since 1995, followed by Shania Twain (70 million), Alanis Morissette (45 million), and Avril Lavigne (20 million).⁴⁵

Sales of Canada's Top 10 Selling Artists Around the World Since January 1995

	Artist	Approximate worldwide sales (units 000,000)
1	Céline Dion	150
2	Shania Twain	70
3	Alanis Morissette	45
4	Avril Lavigne	20
5	Sarah McLachlan	19
6	Nickelback	17
7	Diana Krall	11.5
8	Barenaked Ladies	11
9	Nelly Furtado	6
10	Sum 41 (tied)	5
10	Our Lady Peace (tied)	5

Source: Applaud!—Vol. 2, No.11—July/August 2004.

The Canadian track record has also improved over the years, judging from the annual list of Canadians with gold and platinum certifications in international markets. Over the last five years, the number of certifications for Canadian artists in our three biggest foreign markets—the United States, France and the United Kingdom—has risen nearly 70%, from 23 in 1999 to 39 in 2003, for a five-year total of 144 certifications.

Canadian Artists US Album Certification Awards (RIAA)

	Gold	Platinum	Total	Artists
1999	3	9	12	6
2000	6	5	11	9
2001	7	8	15	12
2002	4	9	13	11
2003	7	11	18	13

Source: PCH compilation of RIAA data.
Note: Only the highest certification given to an album in a given year is included.

Canadian Artists France Album Certification Awards (SNEP)

	Gold	Platinum	Total	Artists
1999	1	5	6	3
2000	3	4	7	6
2001	2	9	11	7
2002	5	7	12	8
2003	3	11	14	7

Source: PCH compilation of SNEP Data.
Note: Only the highest certification given to an album in a given year is included.

Canadian Artists UK Album Certification Awards (BPI)

	Gold	Platinum	Total	Artists
1999	2	3	5	5
2000	0	2	2	2
2001	0	1	1	1
2002	1	9	10	8
2003	2	5	7	6

Source: PCH compilation of BPI Data.
Note: Only the highest certification given to an album in a given year is included.

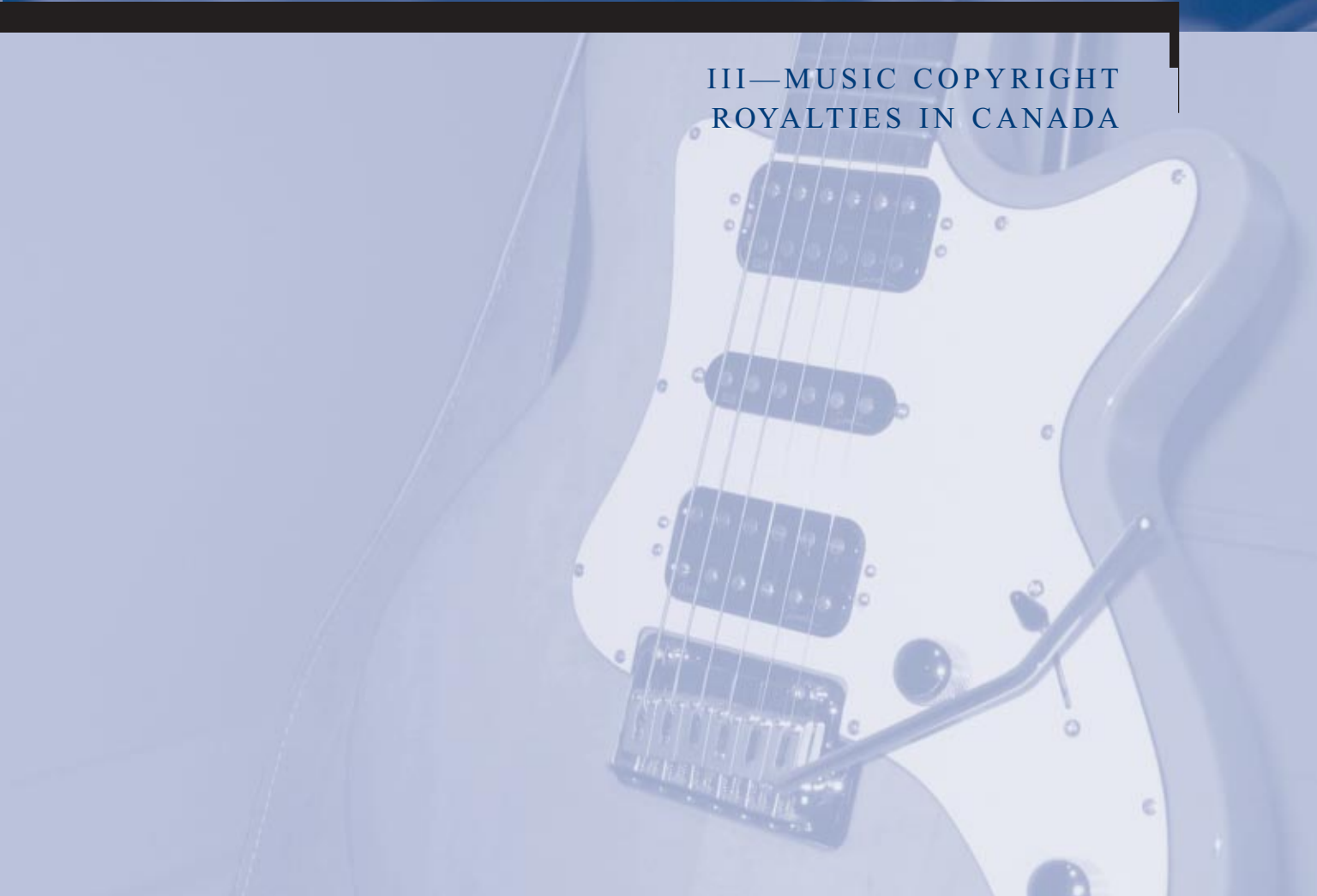
The United States, Canada's largest foreign market, has awarded Canadians 69 certifications since 1999. In this period, 2003 saw the most certifications, with 18 gold and platinum albums awarded to 13 unique artists, led by Shania Twain with *Up* (10 times platinum, or 10 million albums sold), Avril Lavigne with *Let Go* (six times platinum), and Nickelback's *Silver Side Up* (five times platinum). Shania Twain set the five-year record for Canadian artists in the United States with 19 times platinum certification for *Come On Over*. France awarded Canadians 50 certifications over the last five years, with five artists—Isabelle Boulay, Céline Dion, Lara Fabian, Garou and Neil Young (for a reissue of *Harvest*)—achieving Diamond status (1 million albums sold). Top-ranking

Canadians in the United Kingdom for the same time period included Alanis Morissette, Shania Twain and Céline Dion—who, unsurprisingly, has the most certifications in all three markets over five years, at 21.⁴⁶

Canadians' success is not limited to these markets, of course. For example, Nelly Furtado's latest album, *Folklore*, has hit platinum in Germany and gold in five countries, including India and the Netherlands, while Alanis Morissette's *So-Called Chaos* has reached gold status in seven countries, including Norway and Taiwan. Avril Lavigne's *Under My Skin*, meanwhile, has topped the album charts in Greece and Spain.



III—MUSIC COPYRIGHT
ROYALTIES IN CANADA



III—Music Copyright Royalties in Canada

Music Writing and Publishing in Canada

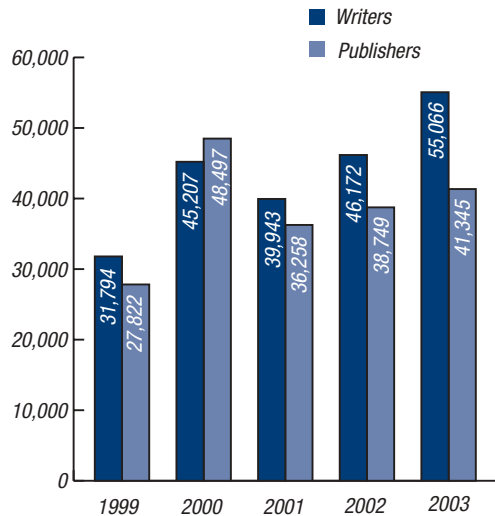
Music publishers work closely with writers and composers to promote their songs. In a typical publishing agreement, the songwriter or composer assigns ownership and control of a copyright protected musical work to the publisher, who in turn earns a percentage of the income derived from the work's commercial use. The Society of Composers, Authors and Music Publishers of Canada (SOCAN) administers the performing rights on behalf of these songwriters, composers and their publishers and collects license fees from users of copyright-protected music in Canada (for the public performance of the works) and distributes these fees to its members in the form of royalties. SOCAN is the only copyright collective for the public performance of musical works in Canada. Virtually all Canadian songwriters, composers and publishers are SOCAN members, therefore the data provided by SOCAN will assist to explain the success of Canadian songwriters, composers and their publishers. SOCAN also works with international affiliated performing rights organizations to distribute royalties to

foreign songwriters, composers and publishers, and collect international royalties for distribution to Canadian songwriters, composers and publishers.

In 2003, SOCAN's total funds available for distribution to its members rose 10.3% from the year before, to \$152.1 million. Total revenue, including Private Copy royalties of \$3.8 million, for SOCAN in 2003 was \$180.7-million, an 8.9% rise from the previous year. Net administrative costs in the same period rose slightly by 1.9% to \$28.7 million.

Over the last five years, SOCAN has seen an increase in both the numbers of its members as well as the royalties it collects and distributes. The number of songwriter and composer members who received royalties jumped from just over 16,000 in 1999 to over 19,500 in 2003, while royalties for writers and composers grew 73.2% in the same time period. The number of publishers, meanwhile, grew from 4,218 to 4,771, while publishers' domestic royalties rose 48.6% to \$41.3 million. (Note: These results exclude any special cable arrears, pay audio arrears, cable overhead rebates and private copy royalties.)

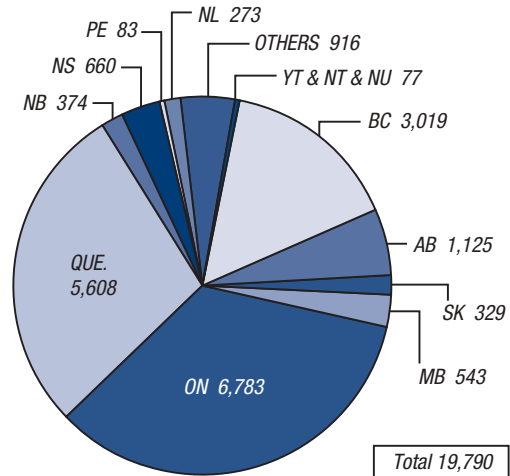
SOCAN Royalties (\$000)



Source: SOCAN

Note: Excludes any special cable arrears, pay audio arrears, cable overhead rates and private copy distributions.

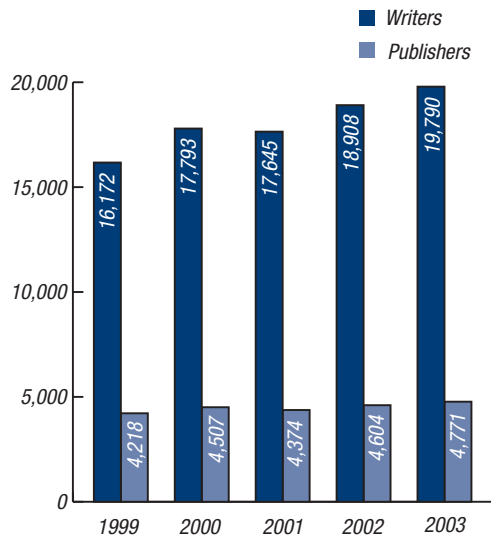
No. of Writers which Received Royalties from SOCAN, 2003



Source: SOCAN

Note: Excludes any special cable arrears, pay audio arrears, cable overhead rates and private copy distributions.

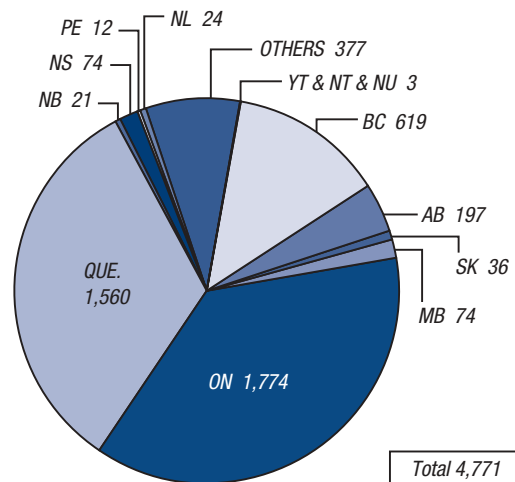
No. of Writers and Publishers Receiving Royalties from SOCAN



Source: SOCAN

Note: Excludes any special cable arrears, pay audio arrears, cable overhead rates and private copy distributions.

No. of Publishers which Received Royalties from SOCAN, 2003



Source: SOCAN

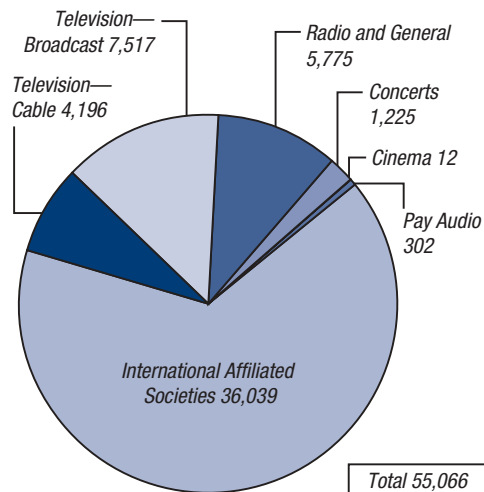
Note: Excludes any special cable arrears, pay audio arrears, cable overhead rates and private copy distributions.

The number of songwriter and composer members who received royalties jumped from just over 16,000 in 1999 to over 19,500 in 2003.

Distributions of Performing Rights Royalties to SOCAN Members

International royalties was the largest single source for SOCAN songwriters and composers in 2003, accounting for 65.4% of the total distributions to them, or \$36.0 million, compared with \$28.4 million the year before. Among domestic sources, broadcast television provided the largest share of royalties to writers and composers (\$7.5 million) up 3.7% from 2002, followed by radio (\$5.8 million) and cable television (\$4.2 million). Pay audio services provided royalties for the first time in 2003, amounting to \$302,000. Disbursements from concerts rose 16.1% to \$1.2 million in 2003, while cinema royalties stayed flat at \$12,000.

SOCAN Writers' Royalties by Distribution Pool, 2003 (\$000)

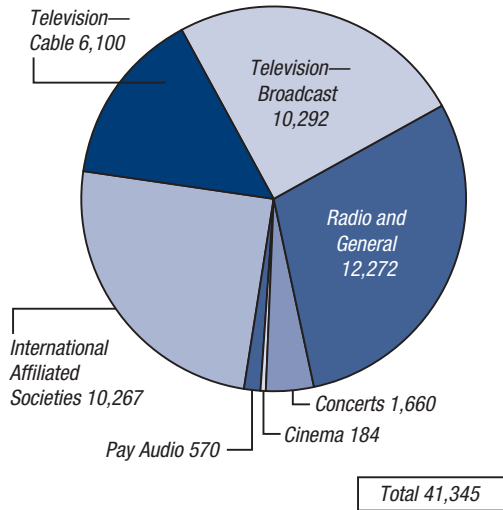


Source: SOCAN

Note: Excludes any special cable arrears, pay audio arrears, cable overhead rates and private copy distributions.

For publishers, radio was the biggest source of royalties, with \$12.3 million in distributions, followed by broadcast television (\$10.3 million) and royalties from international affiliated organizations (\$10.3 million).

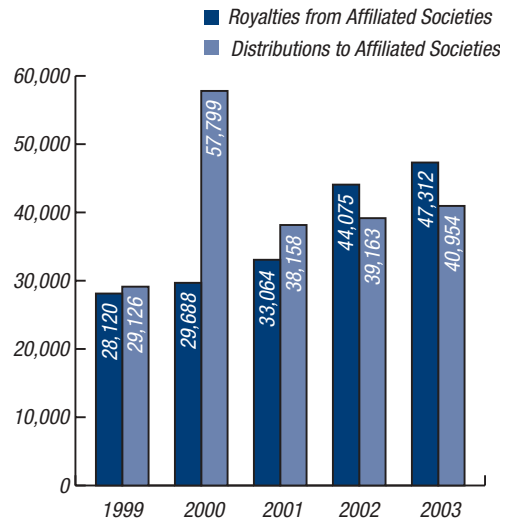
SOCAN Publishers' Royalties by Distribution Pool, 2003 (\$000)



Source: SOCAN

Note: Excludes any special cable arrears, pay audio arrears, cable overhead rates and private copy distributions.

SOCAN Distributions to and Royalties from Affiliated Societies (\$000)



Source: SOCAN

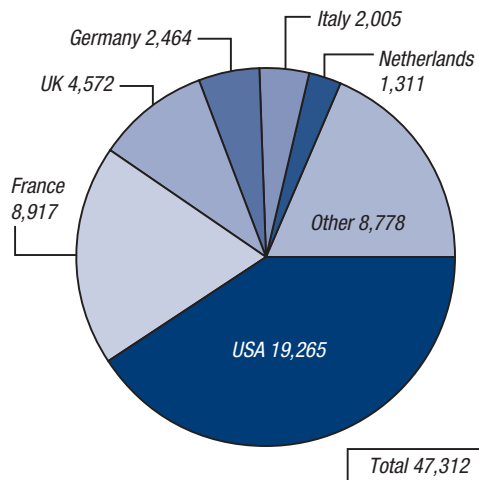
Note: Excludes any special cable arrears, pay audio arrears, cable overhead rates and private copy distributions.

International Performing Rights Royalties to SOCAN

Foreign royalties for SOCAN members grew 7.3% in 2003 to \$47.3 million, according to SOCAN, which collects these royalties from foreign performing rights organizations and distributes them to its members. SOCAN's foreign royalties in 2003 exceeded foreign distributions, which climbed 4.6% to \$41.0 million from 2002.

The United States is the largest single source of international performing rights royalties, accounting for 40.7% of all foreign royalties, followed by France (18.8%) and the United Kingdom (9.7%). Royalties from France and the UK both increased in 2003, by 39.9% and 27.2%, respectively. The United States contributed \$19.3 million to SOCAN songwriters, composers and publishers in 2003—down 12.4% from the previous year but representing a 60.4% increase over five years.

International Revenue from Affiliated Societies—2003 (\$000)



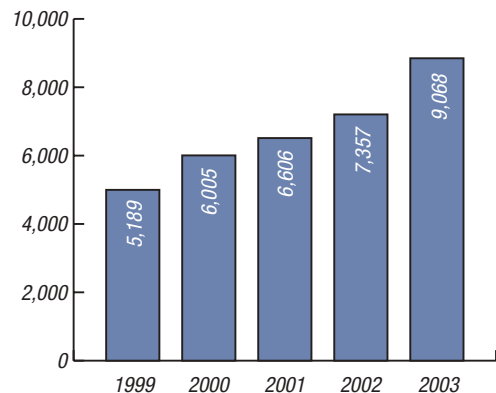
Source: SOCAN

According to research group MHL Communications, however, the SOCAN figures only show part of the story. While SOCAN collects international performing rights royalties for its members, many Canadian music publishers collect their share of royalties from their representatives (agents, affiliated publishers, etc.) in foreign territories. On this basis, MHL calculates total international royalties to be as high as \$72.0 million, 57.0% higher than in 2001 and much higher than domestic royalties.

SOCAN Live Music Royalties

Although Canada has no central data source for live music attendance, a consistent rise in royalties from live concert venues since 1999 gives a sense of the vitality of the live music scene in Canada. SOCAN levies a 3% tariff on popular music concerts, and year-on-year growth of these license fees has been in the double digits. The largest increase occurred in 2003, as fees paid by concert halls, bars and other live music establishments grew more than 23.3%, from \$7.4 million in 2002 to almost \$9.1 million last year.

SOCAN License Fees Paid by Concert Pool (\$000)



Source: SOCAN

SOCAN's distributions from the concert pool to its members and foreign performing rights organizations have been more modest, and in fact declined 3.6% from 2002 to 2003. Over the last five years, concert pool disbursements grew 18.0%, from \$4.6 million in 1999 to \$5.4 million in 2003.

Concert Pool Distributions to SOCAN Writers, Publishers and Affiliated Societies (\$000)

	SOCAN Writers	SOCAN Publishers	International Affiliated Societies
1999	987	1,432	2,178
2000	1,082	1,634	2,475
2001	1,035	1,616	2,561
2002	1,055	1,817	2,758
2003	1,225	1,660	2,541

Source: SOCAN

Other Sources of Copyright Royalties

Mechanical rights compensate composers, authors, songwriters and publishers when their songs are recorded, legally downloaded, or used in film, television programs or commercials. The two main but not exclusive collectives operating in Canada are the Canadian Mechanical Reproduction Rights Agency Ltd. (CMRRA)

and the Société du droit de reproduction des auteurs, compositeurs et éditeurs du Canada (SODRAC). Based on a 2001 study undertaken by Paul Audley and Associates and Michel Houle, it is estimated that mechanical rights represent annual revenues of \$100 million, which are distributed to both Canadian as well as non-Canadian creators and publishers.

The **private copying** levy compensates composers, songwriters, music publishers, recording artists, and record companies for copies made of their recordings onto blank recordable media. In 2003, the Canadian Private Copying Collective (CPCC) collected \$28 million, unchanged from 2002, to be distributed to both Canadians and non-Canadians.

Neighbouring rights compensate the performers and makers in the creation of a sound recording for the public performance of their works.⁴⁷ In Canada, neighbouring rights are currently paid by radio and pay audio services. Based on information from the Neighbouring Rights Collective of Canada (NRCC), it is estimated that neighbouring rights represented \$12 million in revenues in 2003.

Notes

- 1 Music & Copyright, July 7, 2004. Informa Media Group.
- 2 Nielsen SoundScan—Top 200 lists.
- 3 Nielsen SoundScan—Top 200 lists.
- 4 Millward Brown Goldfarb, Consumer Trendz, 2003.
- 5 SOCAN results, although other estimates put foreign royalties for Canadians at \$72 million (see sect. III).
- 6 Nielsen SoundScan MarketWatch, September 19, 2004.
- 7 Pricewaterhouse Coopers, in Music & Copyright, July 21, 2004. Informa Media Group.
- 8 “Canadian Indie Labels Caught in Dispute Between HMV and EMI,” May 22, 2004, www.cirpa.ca.
- 9 Music & Copyright, April 28, 2004. Informa Media Group.
- 10 IFPI—The Recording Industry in Numbers, 2004.
- 11 IFPI online music report 2004.
- 12 Canadian Inter@ctive Reid Report—Music Downloading in Canada: Past, Present and Future—A Special Feature, Spring 2004.
- 13 CRIA-Pollara.
- 14 Canadian Inter@ctive Reid Report—Music Downloading in Canada: Past, Present and Future—A Special Feature, Spring 2004.
- 15 Statistics Canada, Radio Listening data tables, July 2004.
- 16 Music & Copyright, July 7, 2004. Informa Media Group.
- 17 Music & Copyright, July 21, 2004. Informa Media Group.
- 18 CRIA data sheet, July 2004.
- 19 Music & Copyright, July 7, 2004. Informa Media Group.
- 20 Music & Copyright, July 7, 2004. Informa Media Group.
- 21 Nielsen SoundScan MarketWatch, September 19, 2004.
- 22 Music & Copyright, July 21, 2004. Informa Media Group.
- 23 Nielsen SoundScan.
- 24 Nielsen SoundScan.
- 25 Statistics Canada, Book Publishers and Exclusive Agents, 2000-2001. Catalogue No. 87F0004XDB.
- 26 Based on Statistics Canada data from 2000. More recent statistics on market share that give independents closer to 20% typically include the 11 foreign-owned independents operating in Canada.
- 27 Profile of the Sound Recording Industry in Canada, Nordicity Group, 2004.
- 28 Montreal Gazette, “At the digital crossroads: Quebec’s music industry has a good chance of weathering the storm battering the biz. Among its advantages: an independent, partnership model and a strong yet intimate star system”, D1, March 27, 2004.
- 29 Millward Brown Goldfarb, Consumer Trendz, 2003.
- 30 IFPI—The Recording Industry in Numbers, 2003.
- 31 Millward Brown Goldfarb, Consumer Trendz, 2003.
- 32 Ekos, Rethinking North American Integration, 2002.
- 33 Statistics Canada, Radio Listening data tables, July 2004.
- 34 CRIA-Pollara, July 6, 2004.
- 35 CRIA-Pollara, July 6, 2004.
- 36 Olberholzer and Strumpf, The Effect of File Sharing on Record Sales: An Empirical Analysis, March 2004.
- 37 Canadian Inter@ctive Reid Report—Music Downloading in Canada: Past, Present and Future—A Special Feature, Spring 2004.
- 38 Solutions Research Group, June 24, 2004.
- 39 Canadian Inter@ctive Reid Report—Music Downloading in Canada: Past, Present and Future—A Special Feature, Spring 2004.
- 40 “This decrease contrasts with the fact that the value of global recorded music sales grew in current dollar terms by almost \$3B to just over \$32B. However, this was due entirely to the weakness of the US dollar against the other major currencies.” Music & Copyright, April 28, 2004. Informa Media Group.
- 41 Music & Copyright, July 21, 2004. Informa Media Group.
- 42 “Study: Global CD Piracy Trade Tops \$4.5 billion,” by Bernhard Warner, Reuters, July 22, 2004.
- 43 Music & Copyright, April 28, 2004. Informa Media Group.
- 44 CRIA, July 2004.
- 45 Applaud! Magazine, July/August 2004.
- 46 In the US, 500,000 units sold earns a gold record, while one million units sold earns platinum. UK certifications include silver (60,000), gold (100,000) and platinum (300,000). French certifications are the same but include diamond (one million).
- 47 http://www.actra.ca/actra/control/nr_fa