2 | The Digital Revolution: Trends in Media and Entertainment

It may be a cliché, but it must be stated: the Internet has changed our lives, especially in the world of media and entertainment. In this chapter, I discuss how this and other related social and technological trends have shaped the new media and entertainment industries.

Production and distribution costs

Paul McCartney's first solo album, the 1970 *McCartney*, was primarily recorded at the artist's home. Except for some backing vocals by Linda McCartney, Paul performed the entire album — instruments and voice — on a Studer four-track tape recorder. In those days, home recording required a lot of space, a lot of training, and a lot of money — dozens of thousands of dollars. An established and wealthy musician like McCartney could easily afford it, but not many others.

Nowadays, studio-quality recording can be attained for a fraction of that cost. A standard personal computer, inexpensive (or free) software, a microphone — that's all that's required for getting started. In November 2010, Austrian band XBloome released *X Marks The Spot*, possibly the first ever commercial album produced exclusively using free software (open source) and without a professional studio or graphic designer.

Cheap as music recording may have gotten, the most important trend is probably in distribution rather than in production. Nowadays, a new artist or band can completely forego a record label, instead marketing and distributing their music directly on the Internet. Digital marketing sites such as iTunes offer music and video hosting for relatively low cost. Writes musician Rob Pearce:

> I'm no rock star, but I did a couple "niche" songs and put them up for sale just for fun to see what would happen. They earned about $150 in one year, which

Forthcoming in *The Economics of Entertainment and Sports: Concepts and Cases*. This draft: April 2010.

From XBloome's *X Marks The Spot* website: "As maybe the first album ever, 'X marks the spot' was produced exclusively using Free Software (Open Source) and without a professional studio or graphic designers. With this 'proof of concept' album, XBloome have debunked several prejudices about feasability [sic], professionality and quality of free and self-made productions."

> more than payed for the cost of putting them up. It's fun to know that money is trickling in while you do nothing, and neat to know that people in foreign countries enjoy your song enough to put up their hard-earned cash.[1]

Similarly to music, the movie and television industries have also been impacted by a sharp decline in production costs. Nowadays, cinematographers can shoot professional-quality motion pictures for a fraction of the cost of a decade ago or so. Post production software is also more accessible and easier to use. The rise in independent production, which I will document in greater detail in Chapter **??**, is closely related to this cost trend.

Any field of media and entertainment that is in some way related to technology has been impacted by the digital and Internet revolutions, resulting in easier content creation and distribution. This evolution has changed the nature of the game in important ways. Take for example book publishing: it used to be that the challenge was to get published; nowadays, the challenge is to get read. In some of the sections below, and in some of the chapters that follow, I will examine some of the implications of these changes.

Social networking

In some cases, consumers are interested in goods whose characteristics match the consumer's preferences or interests. In other instances, however, the consumer is primarily interested in interacting with others. For example, if a reader looks for the book *Crafting the Culture and History of French Chocolate* (written by Susan Terrio), it's likely that he or she has a strong interest in either history or France or at least chocolate. However, when I read Rowling's *Harry Potter* books I am equally interested in the book per se as I am in discussing it with others, and more generally being part of the cultural phenomenon that the books represent.

Social networking, in particular online social networks, greatly enhances social consumption goods. With online social networks such as Twitter, Facebook, MySpace, etc., the "snowball" effects that create buzz for a book, a movie or a song may reach magnitudes that were unheard of in the pre-Internet era. Anita Renfroe, for example, went from local standup comedian to regular commentator on *Good Morning America* in a matter of few a months thanks to a viral YouTube video.

An additional feature of social networking is the phenomenon of "crowdsourcing," a term coined by *Wired* magazine's Jeff Howe. The idea is to use social networks — and more generally the Internet — as a means to outsource tasks required in media content

creation. The Oxford English Dictionary provides one of the earliest examples of crowd-sourcing (though not a web-based one). An open call for volunteer contributions — indexing all English words and finding example quotations — resulted in over six million submissions over a 70 year period.[2]

A more recent example started on June 18, 2009, when the United Kingdom's House of Commons released thousands of Parliament Minister receipts, a total of 700,000 individual documents (four years worth of expenses and every claim).[3] Such an enormous amount of information could not possibly be analyzed by one single individual or institution in a reasonable period of time. To address the issue, British newspaper *The Guardian* created an online application that allowed volunteer readers to help analyze the data and look for interesting stories buried in possibly a few of the thousands of receipts. Some time after the online application was set up, the web site notice read:

> We have 458,832 pages of documents. 28,333 of you have reviewed 223,797 of them. Only 235,035 to go...[4]

The campaign was highly successful: it allowed *The Guardian* to come up with a good number of interesting stories without spending almost any of its staff research time.

Search technology and the long tail

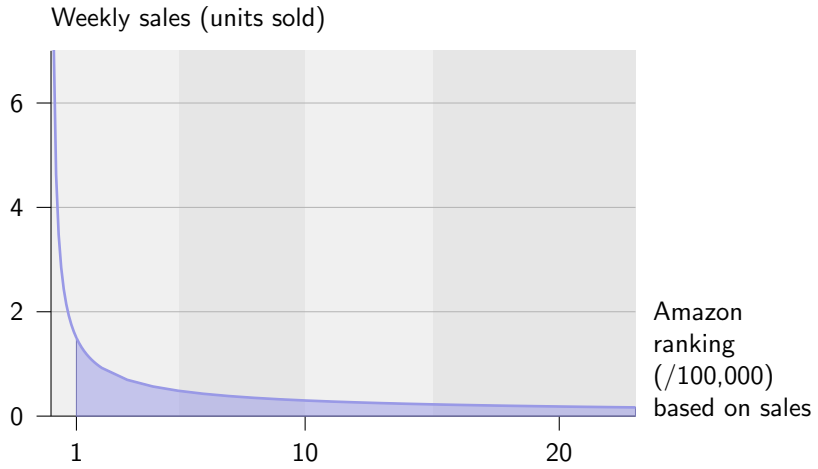
In a recent, influential article (and then book), *Wired* magazine editor Christopher Anderson put forward the thesis that the Internet is changing business models dramatically. As a general point this is not particularly innovative; but Anderson's theory about the impact of the Internet is rather specific:

> For too long we've been suffering the tyranny of lowest-common-denominator fare, subjected to brain-dead summer blockbusters and manufactured pop. Why? Economics. Many of our assumptions about popular taste are actually artifacts of poor supply-and-demand matching — a market response to inefficient distribution.

To put it differently: in traditional markets, it is difficult and costly to offer a good match between customer needs and product offerings. This leads to the the "tyranny of the lowest-common-denominator fare," in Anderson's words: relatively little variety at the store and offerings that basically cater to the median taste. One of the beauties of the Internet is that, together with powerful search engines, it allows for a much better match between customer preferences and product offerings. And this in turn allows for the survival of low-output products that otherwise would not be able to cover their fixed entry costs.

Consider for example the sale of Lebanese folk music CDs. At any particular location throughout the world the demand for a particular Lebanese folk musician is unlikely to be very high. However, given the size of the Lebanese diaspora, the total world market is quite significant, in particular sufficient to justify the recording and distribution of a CD by the particular artist in question. In a traditional market, based on brick-and-mortar distribution, it would difficult to make the match between seller and buyers. By contrast, with the Internet and online search it is much easier to "find" your demand and process the sale. Distance still matters a bit, but much less than in a traditional market. Ultimately, if

Figure 2.1
Amazon's long tail.[5] The shaded area corresponds to about 40% of the total area below the sales curve.



what you are purchasing is a series of mp3 files, then distance matters very little: a seller's market is the world.

The emergence of the Internet and search technology has led to the emergence of a multitude of small suppliers like the hypothetical Lebanese folk musician. Anderson refers to this phenomenon as the *long-tail:* a large fraction of sales in a variety of industries correspond to low-sale products. Consider for example Exhibit 2.1, which depicts book sales at Amazon.com by sales rank, beginning on the left with #1, the top seller. The first thing to notice is that Amazon.com sells an enormous number of different titles: more than 22 million. A large brick-and-mortar store, by contrast, would carry about 100,000 different titles (which corresponds to the number 1 on the horizontal axis of Exhibit 2.1). Second, the average weekly sales of titles ranked below 100,000 is rather low: about 1 copy per week or less. Third, the percentage of total sales accounted by titles ranked below 100,000 is rather large: somewhere from 30 to 40% depending on the estimates.

Erik Brynjolfsson, Yu Jeffrey Hu and Michael Smith, there scholars who have studied the long-tail phenomenon, present an interesting anecdote:

> Eric Clemons, a professor at the Wharton School, is an aficionado of Dogfish Head World Wide Imperial Stout beer at $160 per case. How did Dogfish Head find a customer like him? They didn't. He found them. Clemons was not always a connoisseur of rare beers, but after trying Victory Hop Devil beer, the top-ranked India pale ale at the time, he learned of Dogfish Head, as well as Victorys Storm King Imperial Stout and other niche beers, through the Internet. Clemons notes that he "would never have bought the Dogfish Head without the reviews on ratebeer.com and without the chain of experiences with ever-more interesting beers along the way."[6]

As the anecdote suggests, the phenomenon is not exclusive to books; it is also found in music (e.g., Rapsody.com) movie rentals (e.g., Netflix.com) and other industries. For example, Rapsody's inventory includes more than 700,000 tracks, and most of these sell at

least a copy a month. Even if it's only one copy a month, it's one copy multiplied by a large number of tracks.

In sum, together with the declining trend in media production costs, the Internet has empowered small content creators, who can now reach their audience much more easily. Concurrently, this evolution has also created a significant new revenue streams to large content intermediaries such as Amazon or iTunes.

Supermegablockbusters

"The winner takes it all / The loser standing small." So sang Swedish group ABBA in their eponymous 1980 hit. Fifteen years later, two books took up a similar theme — not in the context of romantic relationships, but in the world of professional salaries. In *The Cost of Talent*, Derek Bok documented the dramatic increase in corporate executive compensation (as well as in other professions).[7] Two years later, Philip Cook and Robert Frank's *The Winner-Take-All Society* presented a conceptual framework to understand the rapid increase in earnings concentration at the top.[8]

Were Cook and Frank to revisit their analysis fifteen years later, they would find ample reasons to reaffirm their point, especially as it applies to media and entertainment. Earnings are very concentrated at the top, that is, a few artists earn a substantial fraction of total revenues. Moreover, the degree of concentration has increased considerably in recent years. In what follows, I document these trends and suggest a few reasons for why they have taken place.

■ **Earnings concentration in media and entertainment.** The concentration of earnings among a few players has always taken place in the world of media and entertainment. However, the evidence suggests that such concentration has increased considerably in recent decades. Let us look at the numbers from two industries: music and books.

□ **Music.** According to economists Connolly and Krueger, in 1982 26% of all concert revenues in the U.S. was accounted for by the top 1% artists, whereas the top 5% accounted for 62%. These numbers reveal a very skewed distribution — more skewed than, say, the distribution of tax revenues in the U.S. By 2003, the distribution was even more skewed: the top 1% artists then accounted for 56%, whereas the top 5% corresponded to 84%.[9]

Additional evidence is provided by Exhibit 2.2, which lists the top 20 money earners in 2008. To put things into perspective, in 2008 the average Fortune 500 CEO received about $13 in total compensation (salary & bonus, stock gains and other compensation).

□ **Television.** In the past decades, television has become considerably fragmented; it has also seen the emergence of many competing entertainment options. However, popular shows remain remarkably popular, especially in comparison with second-tier shows. One illustrative measure of the skew in television audiences is the ration in audience with respect to the top show. This is shown in Exhibit 2.3, which compares the top shows in 1998 and 2008. As the first row of numbers shows, the top show in 2008 (*American Idol*, 22.5 million) attracted a smaller audience than the top show in 1998 (*Who Wants to Be a Millionaire*, 28.5 million). However, this drop in audience was not nearly as big as that of lower ranked shows. By 2008, the 100th show only attracted an audience five times smaller than the top,

Figure 2.2
Top 2008 moneymarkers in music. Source: Billboard.

1	Madonna	242,176,466	11	The Eagles	61,132,213
2	Bon Jovi	157,177,766	12	Lil Wayne	57,441,334
3	Bruce Springsteen	156,327,964	13	AC/DC	56,505,296
4	The Police	109,976,894	14	Michael Buble	50,257,364
5	Celine Dion	99,171,237	15	Miley Cyrus	48,920,806
6	Kenny Chesney	90,823,990	16	Taylor Swift	45,588,730
7	Neil Diamond	82,174,000	17	Journey	44,787,328
8	Rascall Flatts	63,522,160	18	Billy Joel	44,581,010
9	Jonas Brothers	62,638,814	19	Mary J Blige	43,472,850
10	Coldplay	62,175,555	20	Kanye West	42,552,402

Figure 2.3
U.S. Television audiences. Source: *The Economist*, May 1st, 2010.

Year	1998	2008
Top show	*Who Wants to Be a Millionaire*	*American Idol*
Top show audience (million)	28.5	22.5
10th show (as % of top)	63%	55%
100th show (as % of top)	30%	20%

whereas in 1998 that number was a little less than one third. In other words, whereas there was a drop of 21% in the top show's audience, for the 100th show the drop was considerably greater: 47% (a value obtained as follows: $20\% \times 22.5/(30\% \times 28.5) - 1$).

□ **Books.** In book publishing, the trend toward concentration is even more striking than in music and television. Exhibit 2.4 summarizes data for the best-selling books and best-selling authors in the past two decades. In the 1990s, the top-selling books shipped around 10 million copies per title. By contrast, in the 2000s that number was closer to 100 million. The best selling author in the 1990s, John Grisham, sold more than 60 million books. J. K. Rowling, the leader of the pack in the 2000s, registered close to 500 million. In other words, the numbers in the 1990s are staggering; but the numbers in the 2000s are approximately *ten times higher* than the numbers in the 1990s.

■ **Why does the winner take all?** In their above mentioned 1995 book, Cook and Frank introduce the idea of a *winner-take-all market*: a market in which "a handful of top performers walk away with the lion's share of total rewards." What makes some markets have the form of "winner takes all," or at least "winner takes most"? Why would media and

Figure 2.4
Best selling books and authors. Sources: cnn.com, danbrown.com, forbes.com, publishersweekly.com, wikipedia.org, answers.yahoo.com; and author's estimates.

Best selling books (million copies worldwide)			
1990s		2000s	
The Pelikan Brief	11	Harry Potter and the Philosopher's Stone	110
The Client	8	The DaVinci Code	80
Men Are From Mars, Women Are From Venus	7	Harry Potter and the Chamber of Secrets	77
Best selling authors (million copies worldwide)			
1990s		2000s	
John Grisham	61	J.K. Rowling	478
Stephen King	38	Dan Brown	100+
Danielle Steel	38	Stephenie Meyer	100+

entertainment industries be particularly prone to such phenomenon? And what explains the recent change in concentration?

One first important factor is globalization. With the the expansion of television, the Internet, and other means of communication most people have easy access to content created around the globe, including music and books. Suppose the world were initially made up of two countries with a population of 100 million each. If the top star gets 50% of his or her country's audience, then we have two stars with 50 million fans each. Now suppose that improvements in communications lead to a single world market with a 200 million population. Again, the top star attracts 50% of the market audience, which now corresponds to 100 million fans.

A second important factor is branding. Years ago, Nobel laureate Herbert Simon wisely observed that "a wealth of information creates a poverty of attention."[10] Cheaper production technologies have led to a plethora of content supply in various media industries, including music and books. Faced with such a wealth of options to choose from, consumers crave for signals to help them navigate the vast information seas. This in turn creates a demand for brands, which in music and books correspond primarily to performers and authors. For example, readers looking for legal drama will buy a Grisham book even if they have not read any review of the particular title they buy: the Grisham brand is guarantee enough of quality, whereas a different author, promising as he or she may be, is a riskier proposition.

Finally, a third factor that pushes in the winner-takes-all direction is social networking and viral marketing. When Susan Boyle first appeared on *Britain's Got Talent*, her rendition of "I Dreamed a Dream" was watched by a few million viewers. Within days, videos of Boyle's performances were watched by over 100 million.[11] Within months, that number had increased to more than 300 million.[12] This kind of snowball effects would be impossible in the pre-Internet era, both in terms of timing and in terms of extension. Networking

Susan Boyle's first album, *I Dreamed a Dream*, released in November 2009, was the fastest selling UK debut album of all time.

sites such as Facebook, YouTube, MySpace, etc., allow for news regarding talent to spread rapidly, thus creating self-reinforcing dynamics that make the famous even more famous. Technical note **??** deals with the mathematics of these snowball, or viral, phenomena.

What is the source of these magnifying effects? First, many consumers interpret the popularity of a singer or an author as a signal that the product must be good ("if everyone is reading this, it can't be that bad"). Second, independently of quality, many people follow the crowd simply because they do not want to be left out. Personally, I read the first Harry Potter book mostly because not doing so would leave me out of many conversations. I suspect many teenagers listen to the Jonas Brothers for similar reasons.

All of the above effects contribute to the "winner-takes-all" (or "winner-takes-most") nature of media and entertainment. However, if I had to choose one factor I would go for social networking. The idea is that media and entertainment is a consumption good with a strong social element: people demand media and entertainment not just for its immediate and direct enjoyment (as in eating an apple) but also for the value it creates in social relations.

One of the hallmarks of the Internet-age society is the extent and the impact of social networking, especially online social networking. Every industry that produces goods with a social consumption element is affected by the growth in social networking. This has implications at various levels. In particular, it leads to a greater concentration of earnings among the top players. From a strategy point of view, this means that, more than ever, it is crucial to be in the right place at the right time.

Globalization

In a much discussed New York Times' 2005 bestseller, Thomas Friedman declared that "The World is Flat." But is it? In recent years, authors such as IESE's Pankaj Ghemawat have convincingly argued that rumors of a global world have been greatly exaggerated, frequently degenerating in what he refers to as "globaloney." Specifically, writes Ghemawat,"despite talk of a new, wired world where information, ideas, money, and people can move around the planet faster than ever before, just a fraction of what we consider globalization actually exists."

What about the world of media? To the extent that media products are largely intangible — especially in the digital era — one would have thought of media as a prime candidate

for globalization. However, as I will show next, this is one of many media-related myths regarding recent economic and social trends. Specifically, I will argue that the idea of global music and movie industries is not as simple as one might have thought at first.

■ **Music.** In a 2010 study of the music and movie industries, Fernando Ferreira and Joel Waldfogel examine international demand patterns in CD sales.[13] In one of their most revealing exhibits, they plot what one might call a "chart divergence index." The index is the ratio of the number of distinct artists appearing on world charts in a given year over the number of chart entries in all of the countries in the same year. For example, if the top artists were all different from country to country, then the index would be equal to 100%. This is maximum divergence: there are as many artists as there are artist slots. At the opposite extreme, if the same 50 artists covered the top 50 positions in all of the countries (say, ten countries), then the index would be equal to $50/500 = 10\%$, the lowest possible value, corresponding to maximum overlap, that is, maximum globalization.

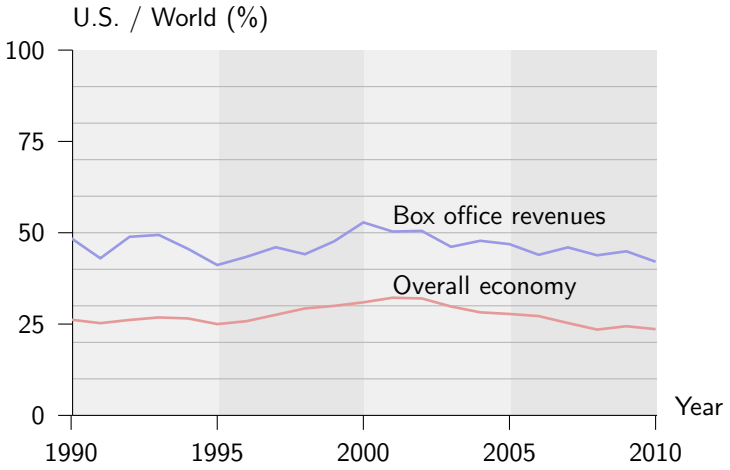
Plotting the values of this index from 1960 to 2007, one notices a considerable drop from a high of 70% in 1963 to a low of 36% in 1983, reflecting a sharp increase in "globalization" over a period of 20 years. However, since 1983 the index has rebounded to about 55% in 2007, recovering about one half of the drop from 1963 to 1983. In other words, since the mid 1980s we have observed a decrease, not an increase, in the globalization of music, as reflected in music charts.

What explains the de-globalization trend in music sales? Ironically, one possible factor is the global expansion of MTV. Some authors claim that the early expansion of MTV contributed to a form of "global imperialism." For example, Jack Banks claims that "MTV's networks lavishly play and promote US and UK artists, giving scant attention to local musicians in the countries where MTV is offered." However, according to Ferreira and Waldfogel, beginning in 1987 the MTV formed regional channels which gradually carried more and more local artists.

A second important factor is the Internet. It's cliché to say that the Internet has changed our lives in every dimension, and music is no exception. In the present context, an important question is whether the Internet is a vehicle for bringing foreign content into a given country or rather gives local artists in a small country a better chance (when without the Internet they would more easily lose out to imported music from larger music-exporting countries). For example, most likely Canada's Justin Bieber would not have had the same chances if the Internet did not exist (in particular, if YouTube did not exist). In this sense, the Internet helped develop a domestic talent in a country that might otherwise succumb to imports from its larger neighbor. But YouTube is also responsible for Bieber's increased popularity in many other small countries, possibly to the detriment of local talent in those countries. It's hard to say which of these effects dominates, but the numbers seem consistent with the hypothesis that the Internet has actually helped home-grown talent in small countries (musically small or population small).

Finally, a third factor in the direction of decreased globalization is given by regulatory policy. For example, in the mid-1990s France introduced a 40% minimum quota of French music radio play. In this regard, it should be noted that, at France's insistence, audiovisual goods were granted a "cultural exception" under the Uruguay Round of the General Agreement on Trade and Services. This allows countries such as France, Canada, Australia or New Zeland to impose import or radio play quotas without violating trade agreements.

Figure 2.5
U.S. and the world: relative weight of box-office revenues (blue line) and the overall economy (red line). Source: imdb.com, IMF, and author's calculations.



French President Franois Miterrand once warned his countrymen "Let us be on guard. If the spirit of Europe is no longer menaced by the great totalitarian machines that we have known how to resist, it may be more insidiously threatened by new masters."[14] Along these lines, one frequently hears the assertion that the United States is "neo-colonizing" the world through the export of movies and popular music. Is globalization a one-way street? Does the data reflect the U.S. preponderance hypothesis? It's true that U.S. music represents a big chunk of world music trade, but one would expect a large country to have large music exports anyway. The interesting question is: does the U.S. export music more than proportionally to its size?

To address this question, Ferreira and Waldfogel plot each country's share of world music trade against that country's share of world GDP (a measure of country size). It turns out that the U.S. falls approximately on the equal proportion line: its share of world GDP is approximately equal to its share of world music trade. In this sense, the truly upper outlying countries — the countries that are "punching above their weight" - are Canada, the UK, Sweden, Finland and New Zeland. (In this sense, two developed countries that are "punching well below their weight" are Japan and Portugal.)

It is noteworthy that, of the above set of outliers, three are English speaking (Canada, UK, New Zeland) and two include artists who sing in English (Sweden, Finland). An alternative story might then be that the English language is the true "emperor" or "colonizer" in the new "global music world," not any country in particular. Moreover, when reading the numbers for local talent creation one must evaluate how truly local this talent is. In other words, one story supporting the "neo-colonization" hypothesis is that, through MTV, the Internet and so forth, U.S. music is influencing local artists around the globe, so that "local talent" really becomes a proxy for American culture. Whatever the case is, the numbers suggest that reality is not as linear as one might have thought at first.

■ **Movies.** How global is Hollywood? Clearly, on the supply side, the answer is, very little. In fact, the mere fact we still refer to the movie industry as "Hollywood" says it all.

While India and Nigeria have emerged as important challengers to Southern California's hegemony, the industry is still very concentrated geographically.

What about the demand for movie entertainment? While there are reasons for geographical concentration of production, globalization would seem to imply a trend toward greater uniformity in consumption patterns, especially when transportation costs are very small, as is the case with digital media.

In Exhibit 2.5, I plot two time series that address the above question. The blue line shows the fraction of world-wide box-office revenues that is accounted by the U.S.[15] As can be seen, this is relatively stable between 40 and 50%. There is a slight downward movement, but a rather small one. Compare this to the red line, which plots the fraction of the world's GDP accounted for by the U.S. Again, we see a slight downward movement, but basically values between 20 and 30%.

In a truly global, flat world, the consumption of each good should be evenly spread across the various countries. In this context, we should expect the fraction of movie consumption in the U.S. to be equal to the fraction of GDP creation in the U.S. In fact, we observe that Americans buy movie tickets at a much higher rate than the rest of the world (approximately twice as much). Moreover, the gap between the blue and the red lines seems relatively constant in the past three decades, suggesting that globalization trends have not had much impact in the movie industry.

In conclusion, despite the common stereotype that everything in the world has become "global," recent trends in trade patterns suggest that reality is rather more complicated and nuanced. In the case of music, notwithstanding the emergence of "global stars" one also observes an increased weight of local talent in each country's charts. In the case of movies, we still observe a strong domestic consumption component. The entertainment world may have become somewhat flatter, but it is still far from flat.

Endnotes

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14. Quoted in Darrin McMahon, "Echoes of a Recent Past: Contemporary French Anti-Americanism in Historical and Cultural Perspective," International Security Studies at Yale University, January 1995.
15. Actually, this is just an estimate of the fraction of U.S. revenues over worldwide revenues. Due to data availability issues, I only consider box-office hits. Intuitively, one would expect hits to have a wider appeal, that is, to be well received both in the U.S. and abroad. In this sense, my measure of globalization may overstate the extent to which Hollywood movies make it abroad.