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78 Million People Can't Be Wrong: Why Consumers Are Still Buying CDs

Prepared for NARM Town Hall

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Music Acquisition Themes 2010

- Buyers continue to explore newer, alternate means of acquiring music
  - Acquisition through paid, unpaid & sharing methods, off nearly 20%
  - Downward pace being accelerated by decline in unpaid modalities
  - Most severe physical downturn among 26-50 year olds, who were the most dedicated CD buyers in the marketplace.
  - Apathy with content and releases acute among 36+. Digital modes and free still most prevalent among younger music consumers
  - Dissatisfaction with retail accelerating decline among core customers
- The CD is still the dominant mode of music purchasing
  - 80% of music consumers are buying CDs
  - Strong format for discovery of new artists
  - The consumer spend on CDs has stayed level for the past couple of years on an individual basis. The challenge is getting more of them back into the stores/sites as incidence has decreased

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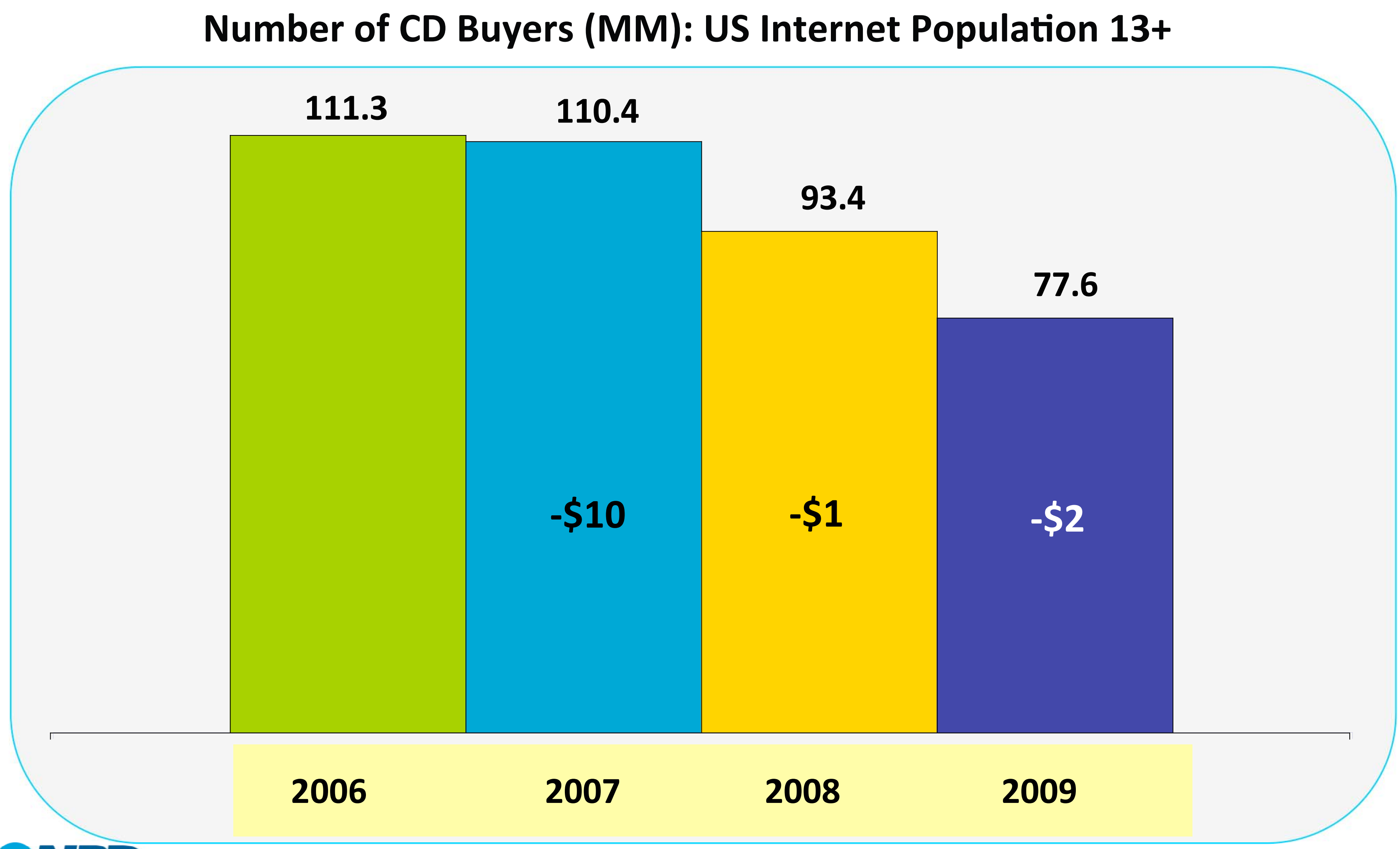
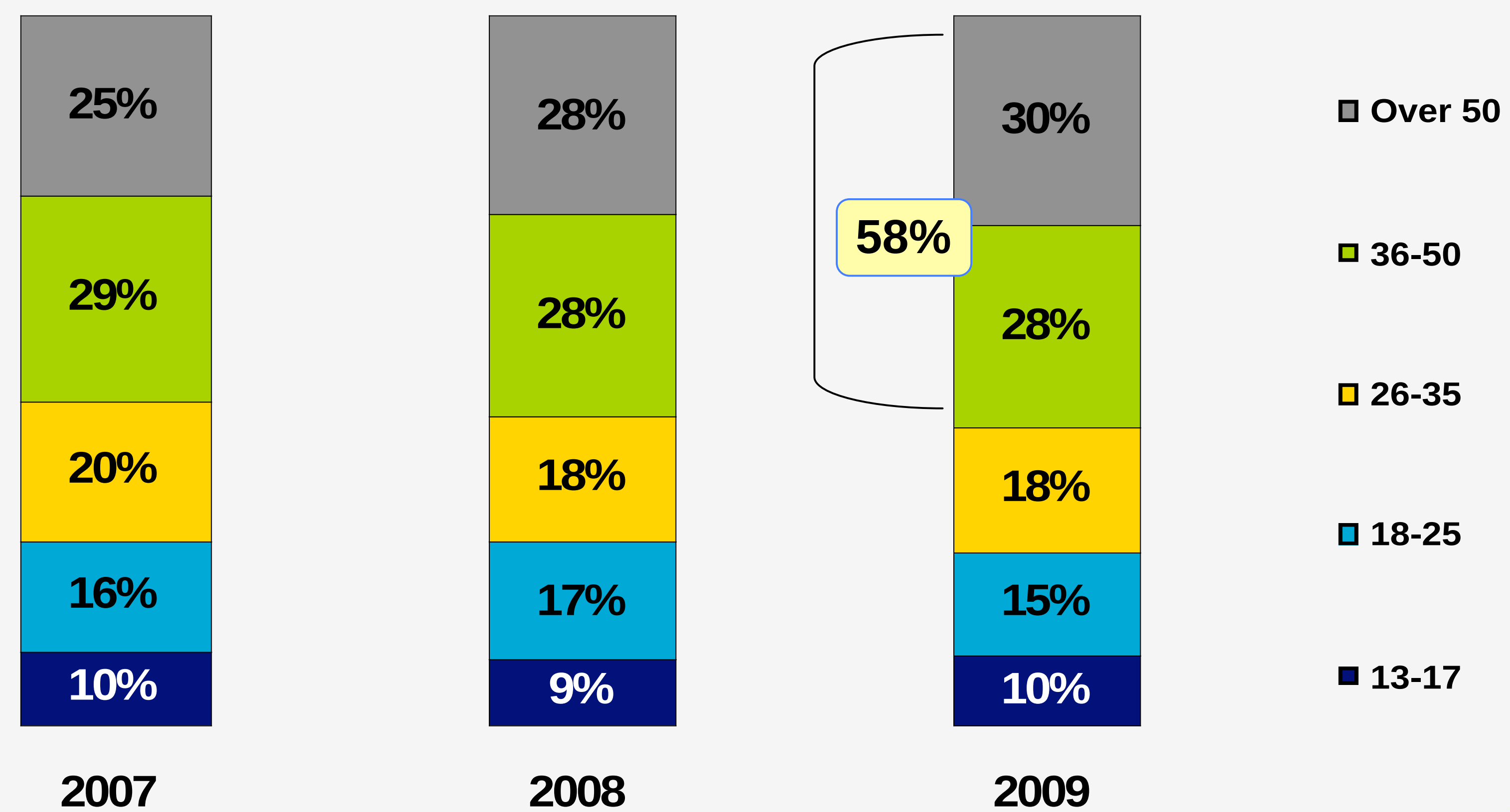
Source: NPD Digital Music Study December 2009 (US Internet Pop. Age 13+), NPD MusicWatch, March 2010

CD buyers are falling out of the market, but they outnumber digital buyers 2/1 and those that remain have kept their spending level consistent over the past couple of years



Source: NPD Digital Music Study December 2006, 2007, 2008, 2009 (US Internet Pop. Age 13+)

The CD buyer has aged over the past 3 years. Consumers 36+ account for nearly 60% of all CD units purchased in 2009.



Other demos remain steady: roughly 50/50 male/female split, 70% White/Caucasian, 18% African-American, 15% Hispanic, geographic distribution

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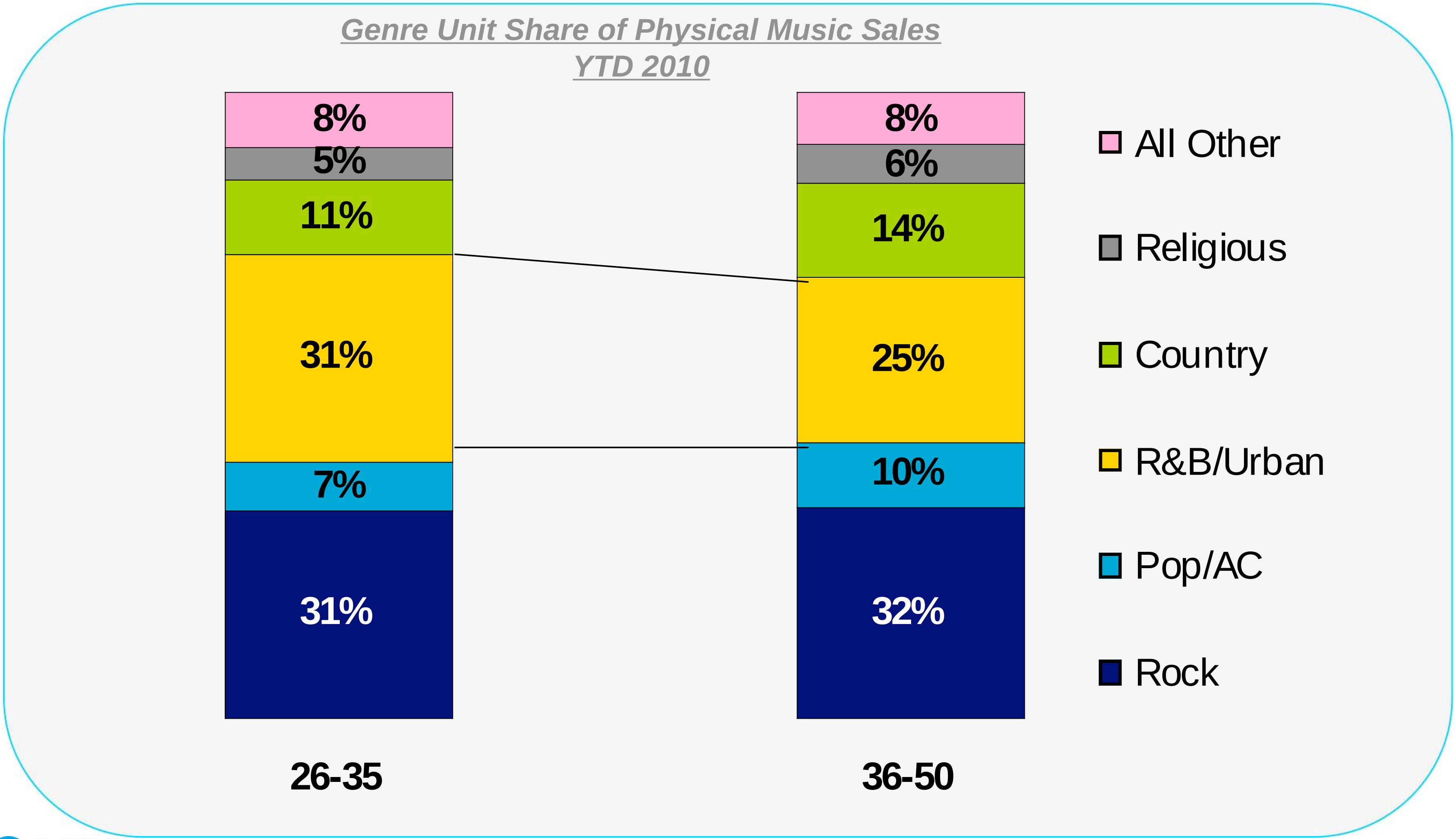
Source: NPD MusicWatch, March 2010

Genre profile shifts with age– R&B/Urban drops off dramatically, while Pop & Country become a bigger part of the mix



Source: NPD MusicWatch, March 2010

So consumers are buying, but when they do they're buying less… When they buy, why?

- **Three-quarters** of CD buyers cite some type of artist affinity as a reason for their purchase
- Motivations around hearing a specific song remain strong
- If the consumer likes what they hear, they're still willing to buy
- When CD buyers are in stores: "On sale" motivates roughly 1-in-5 purchases of a CD, browsing & impulse are near the same level.
- But, more than half of CD buyers state that they bought because the "price was right" highlighting a need for the industry to deliver a strong message around the value of a CD (portability, connection to music, listenability)
- **$635m** was spent on CDs by consumers who were motivated to buy while browsing the music section in 2009, making sections more "browsable" can deliver more revenue to the industry
- Spending shift away from going to the movies and buying DVDs. CDs & music seen as a good value proposition for the entertainment dollar
- But, bonus content, instore displays & circulars, content in ads aren't motivating those already buying CDs more than they were a couple of years ago.

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Source: NPD MusicWatch, March 2010, NPD Entertainment Trends In America, April 2010

The brick & mortar CD buyer is a slightly different animal than the online physical one

- The in-store CD buying consumer is far more likely to be a fan of the artist they're purchasing
- Ability to pre-order, online listening, reviews/articles are all more likely to motivate the purchase of a CD through online sources than instore.
- Online purchasing gets less impulse purchasing, but more motivations from recommendation engines, and on-site advertising.
- Online CD buyer is typically older & more likely to be male. AmazonMP3 has also begun to convert some of them to a digital consumer.
- Online CD buying trends away from Rock/Urban/Country and more towards "other"– Classical, Soundtracks, Electronic etc.
- People buy online because of the entire experience. Online retailers' CD buyers are the most satisfied customers of any music retailer

Source: NPD MusicWatch, March 2010

It's a challenge, but physical still provides value to the consumer and to retail

- **Sales decline is primarily a result of reduced CD shopping incidence**
  - Motivating incremental sales from those still engaged with the CD is important
  - Finding artists that connect with the 36+ age groups
  - Need to reverse the course of disinterest in the release schedule
- **CD buyers still see the format as good value for the money they spend**
  - Finding the right value proposition for the "on the fence" consumer can bring added revenue, without relying on everything being "on sale" all the time
  - Gift buying is important, reminding customers to treat CDs like a gift can also drive sales
- **Consumers will go to retail for artists they like or feel a connection to**
  - Online CD purchasing more about immediacy, convenience and selection
  - Digital strategies can drive physical sales, but also foster a connection to retailer & artist that brings revenue from merchandise and other areas
- **The CD-only buyer is a shrinking part of the revenue pie- nearly half of music buyers buy both CDs & downloads.**
  - Dual buyers spend more on average annually on CDs than CD-only buyers.
  - Aging trend in download purchasing opens opportunity to entice both modes of purchase, and the 36+ consumer isn't as married to the leading digital music retailer as younger demos.

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Source: NPD Digital Music Study December 2009, NPD MusicWatch March 2010, NPD Entertainment Trends In America, April 2010

Paid digital the exception…it's dramatic incidence cuts that drove declines in acquisition

	% Change Volume	% Change People	% Change Eq. Vol. Per Acquirer
CD	**-19%**	**-17%**	**-2%**
Paid DDL	**12%**	**-4%**	**16%**
P2P	**-25%**	**-22%**	**-3%**
Borrow/Burn	**-20%**	**-11%**	**-9%**
Borrow/Rip	**-34%**	**-18%**	**-16%**

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Source: NPD Digital Music Study December 2008, 2009 (US Internet Pop. Age 13+)

2009 appears to be the year 36-50 year olds began abandoning the CD in exchange for all digital. Dual buyers

Buyer Composition Demo Profile

(among the US Internet Population age 13+)

	2008	2009	2008	2009	2008	2009
	CD Only Buyers		**Digital Only Buyers**		**Dual Buyers**	
Age						
13-17	8%	6%	17%	12%	10%	11%
18-25	13%	13%	22%	17%	20%	23%
26-35	16%	15%	27%	36%	27%	26%
36-50	35%	33%	22%	31%	34%	30%
51 or Over	28%	33%	12%	4%	11%	11%
Gender						
Male	45%	44%	55%	46%	50%	54%
Female	55%	56%	45%	54%	50%	46%

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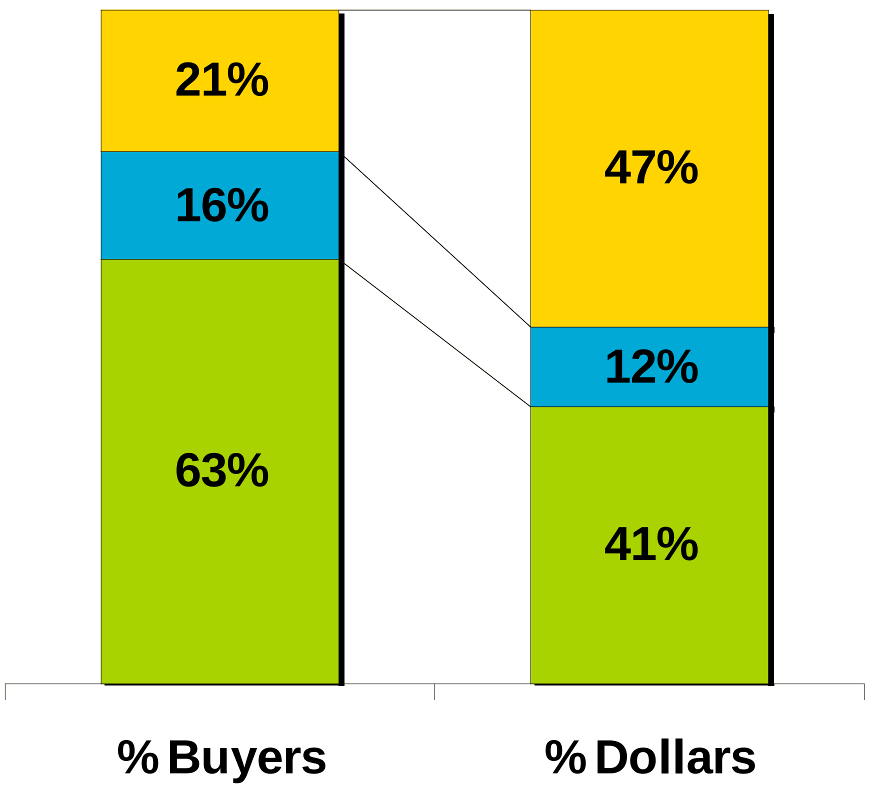
Source: NPD Digital Music Study December 2008, 2009 (US Internet Pop. Age 13+)

Even with a small shift away from dual format purchasing, the dual buyer segment still represents nearly half of music spent

Buyer Composition (Past 12 Months)

(among the US internet population age 13+)



	Spend Per Buyer	
Dual CD/Paid Download	$126	CD:$59 Paid DL:$59 Subscription:$9
Paid Download Only	$42	CD:$0 Paid DL:$38 Subscription:$4
CD Only	$37	CD:$35 Paid DL:$0 Subscription:$2

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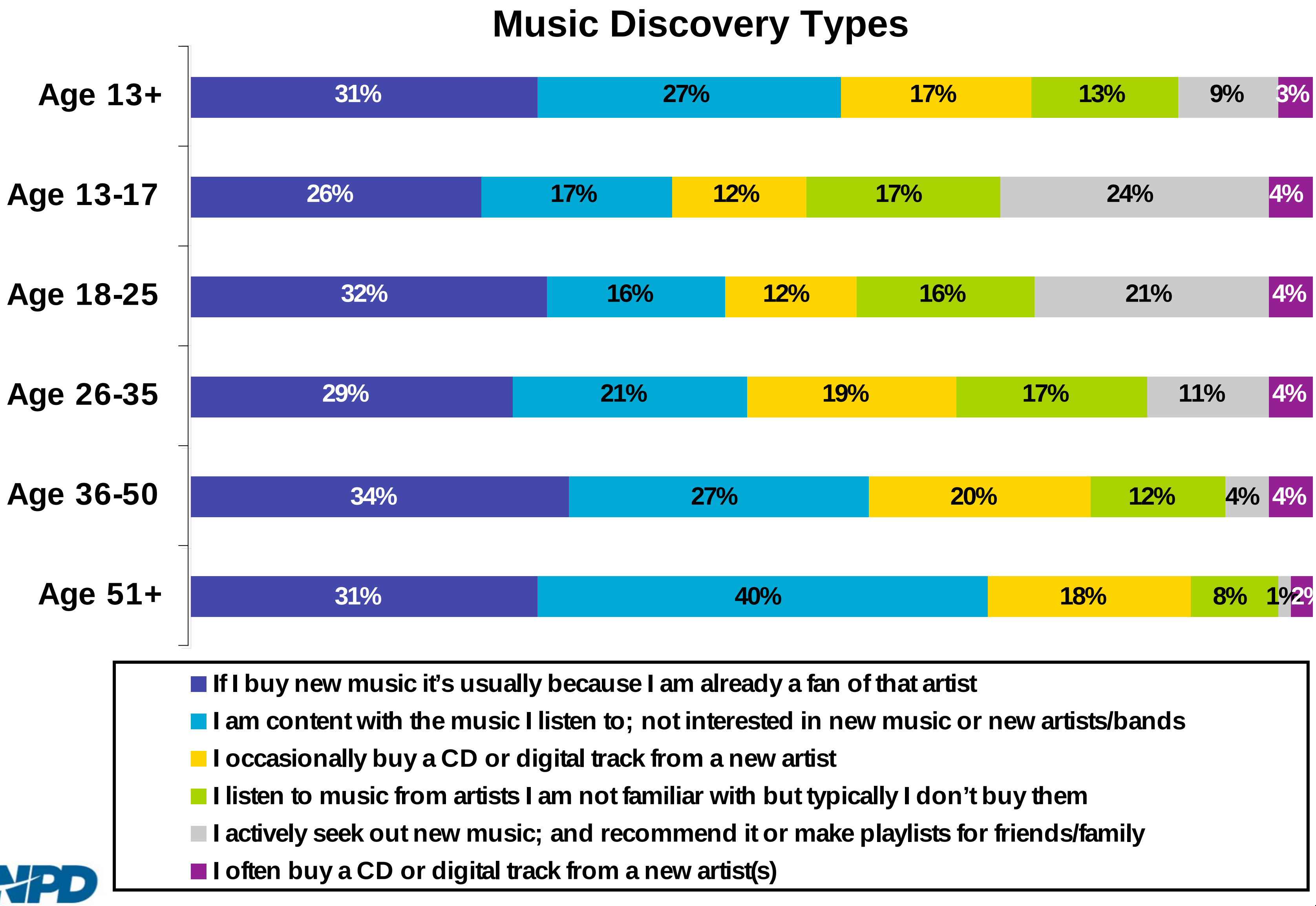
Source: NPD Digital Music Study December 2009 (US Internet Pop. Age 13+)

Listening Habits – Initial Stats

- CD Only Buyers
  - Significantly more likely to listen via
    - CD in car or home → Spend ~4 hours per week
    - Satellite Radio → Spend ~1.5 hours per week
- Digital Only Buyers
  - Twice as likely to be listening to music via
    - Portable digital music player → Spend ~6 hours per week
    - Digital music files on computer → Spend ~4 hours per week
- Dual Buyers
  - Twice as likely to be listening to music via
    - Portable digital music player → Spend ~8 hours per week
    - Digital music files on computer → Spend ~5 hours per week
    - Mobile Phone → Spend ~1 hours per week

At least half of consumers 35 and younger are experimenting with new music



Teens seem to be the most aware, and discontent, with prices. As noted earlier access models are having an impact on paid digital

Reasons for Purchasing Less Digital Downloads in P12M

(among US Internet Pop 13+)

Teens – nearly 2x more likely:

Songs I wanted were often priced too high (46%)
Spend more time listening online (39%)
Can listen for free so many other places there was less need to pay (32%)
Spent more on other entertainment and/or technology related expenses (30%)
Downloaded from free file-sharing service instead (20%)
Files took up too much space on computer (14%)
Paid for a digital music subscription service instead (9%)
Downloaded/streamed music from a community/social networking site more (8%)
Less comfortable buying digital formats (8%)

Young Adults (18-25) – nearly 2x more likely:

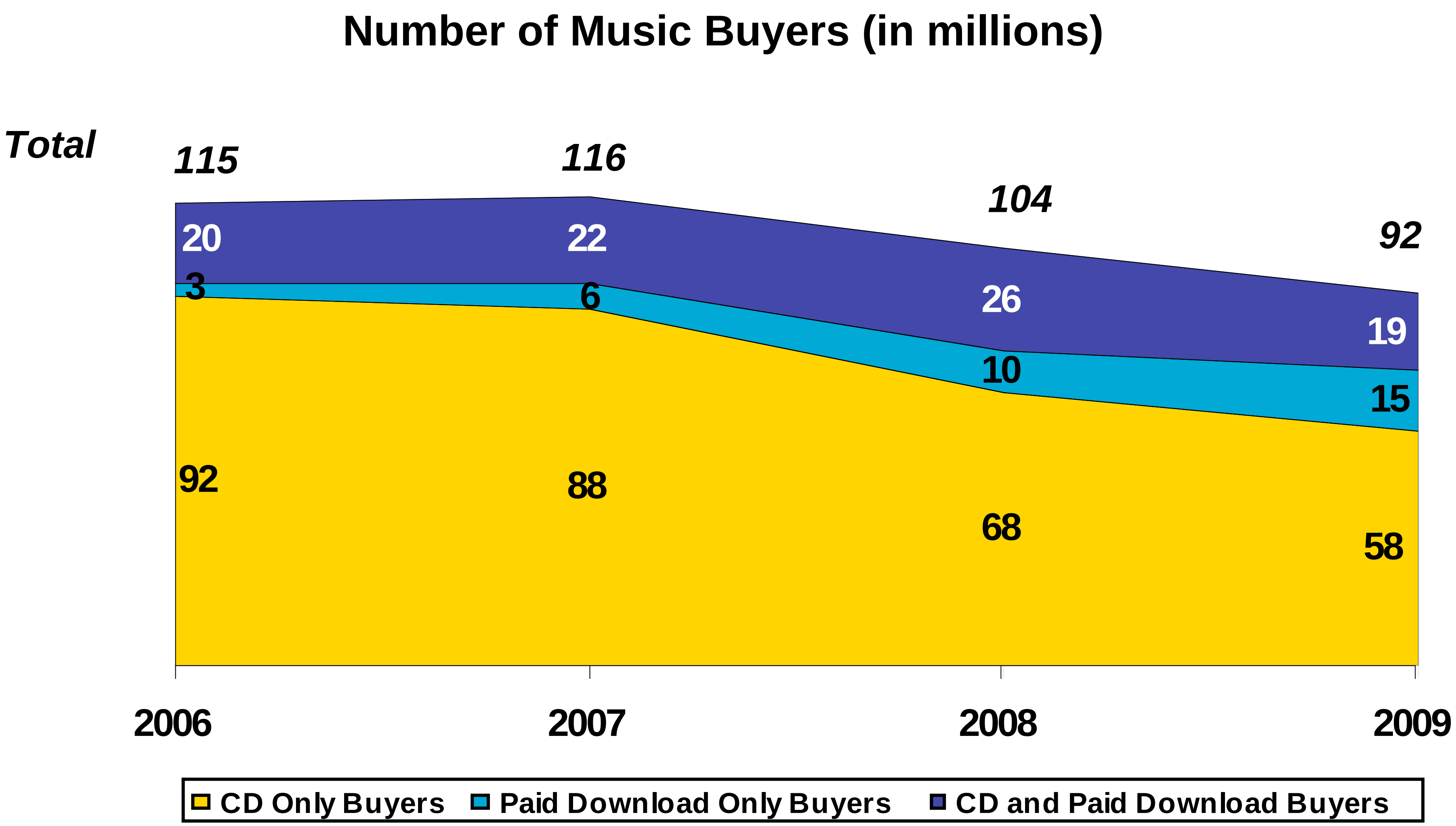
Borrowed CDs to rip or burn instead (43%)
Can listen for free so many other places there was less need to pay (39%)
Don't spend as much time listening to digital music as I used to (28%)
Borrowed friends/family members hard-drive and copied music to my hard drive (26%)
Downloaded from free file-sharing service instead (26%)
Downloaded/streamed music from a community/social networking site more (11%)
Less comfortable buying digital formats (7%)

Source: NPD Digital Music Study December 2009 (US Internet Pop. Age 13+)

Listening Habits – Initial Stats

- Teens and Young Adults (13-25):
  - Twice as likely to be listening to music via
    - Free On-Demand → Spend ~2 hours per week
    - Mobile Phone → Spend ~1 hour per week
  - Significantly more likely to listen via
    - Portable Digital Music Player → Spend ~5 hours per week
    - Digital files on computer → Spend ~3.5 hours per week
    - Free internet radio → Spend ~2 hours per week
- Adults 26-35
  - Significantly more likely to be listening to music via
    - Free internet radio → Spend ~2 hours per week
    - Mobile Phone → Spend ~1 hour per week

Since 2006 the industry has lost roughly 23 million music buyers



Source: NPD Digital Music Study December 2006, 2007, 2008, 2009 (US Internet Pop. Age 13+)

The challenge is lost buyers rather than erosion in spend; still a large and loyal following

Among Those that Purchased a CD in P12M						
	Age 13+	13-17	18-25	26-35	36-50	51+
% Change YOY	-5%	-9%	-15%	-2%	+4%	-8%
'09 CD Spend	$ 41	$ 32	$ 41	$ 42	$ 48	$ 34
'08 CD Spend	$ 43	$ 35	$ 48	$ 43	$ 46	$ 37

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