



By John McGlasson - GJD Contributor

If you've seen the recent news on free internet radio service Pandora, you'll see exactly what I was talking about a few months ago when I wrote that I saw no future for ad-supported music that's free to the user. My case was more about my opinion that it's just tacky to attach your art to any product that'll put out the cash, but I've never believed that music sells products, unless they're music related, like guitarists buying a guitar or piece of gear because someone they admire uses the product as an endorsee, that's been proven to work. (Ask Ibanez!!!)

I've mentioned Pandora a lot in my articles because it's an interesting experiment, and because I love it! I listen to Pandora for hours and hours while working, and I do hope it survives. I also love it because it's free to me. Founded by musicians, these people have their hearts in the right place. If you're familiar with the Music Genome Project you'll know that there's a lot of integrity at Pandora. The fact is, Pandora has had huge growth, it's been a huge success in many ways, but they're now having to face the realities of the business world and the affects of government intervention.

Pandora's founder Tim Westergren is very publicly claiming that his company is on it's death bed and is "making the last stand for webcasting". I'd be shouting publicly too, knowing that royalty rates they pay now are about to more than double. So if Pandora's founder is being honest, it's over for Pandora when the rates go up by 2010.

There's a circle of events that have to take place for it to work: customer listens to music, views advertising on the side of the page, clicks through the ad, and buys the product. And while Pandora is adding new users at a huge rate each week, largely because of a new I-Phone app, and revenues top \$25 million, they claim that at the current .08c per play they pay now, over 70% of their revenue goes to royalties. 25% of their staff is made up of their ad sales team, and much of their staff listens to and classifies the music. Most businesses showing this kind of growth would just raise ad rates a bit to compensate and advertisers would comply, but there's another dynamic at work here; the advertisers can't possibly be seeing the results. Traffic and happy users don't mean revenue for advertisers, it's being proven by Pandora's business model.

It's safe to gather from Pandora's own numbers that if they're retaining 30% of revenues after paying out royalties, then it's because advertisers are paying 30% more than the current .08 per play Pandora pays out now. Apparently the click-through numbers the advertisers are seeing don't justify the 120% ad rate increase Pandora would have to inflict just to be even on royalties once they go up to .19 per play, forget the 30% they're able to retain now after royalties are paid out, that'd be gone. 150% ad-rate increase to survive? When they say they're losing money at the 30% margin they get now? Not likely.

One glaring discrepancy is that terrestrial radio (airwaves) pays no royalties. Zero. Never has. It was clear in the "old" music biz that radio airplay sold records, so labels and publishers didn't demand royalties from terrestrial radio stations. Terrestrial radio is and has always been ad-supported in the exact same model that Pandora's using now, so why the discrepancy between the medium of airwave and internet? And while there's a movement to change that, there's no date on the change the way there's a date on the doubling of internet radio royalty rates, which is just a typical example of government hypocrisy. Radio giants like Clear Channel have always had very powerful lobbies, and you're seeing the results of it now. The fact is, before the internet, radio airplay resulted in sales for the labels and the advertisers, it worked for decades, because the labels sold albums, the advertisers sold products, and radio stations paid no royalties.

Bottom line; if the advertisers aren't seeing the results they need to see for the dollars they're putting out to advertise on Pandora, it's over for Pandora. The crumbling affect will match that of retail music giant Tower's bankruptcy, in that when the biggest falls, there's little question the rest will fall as well. Unfortunately perception is reality in the advertising world, and when it looks like ad-supported has failed, they'll all pull out. And if labels were seeing greater music sales as a result of ad-supported, free-to-the-user radio, they'd be letting Pandora and others use their goods freely, but they're not seeing increased revenues, the situation is quite the opposite. Pandora has taken the place of the music purchase for the consumer. If Pandora profits from the music they play, they'll be the only one doing so. From this standpoint, labels and publishers are perfectly entitled to demand reasonable royalties from anyone using their music to sell products and profit.

Maybe there's a way to do ad-supported music tastefully and profitably, but until Pandora can find a way to pay .19 per play and charge advertisers a per-play rate above that to profit, and do it without losing what people like me love about Pandora, then this experiment has failed. Until the public is ready to pay for higher-quality music than they can get for free, then free will be what we're competing with. Thanks for reading!