Labels eye variable pricing for digital sales

By Antony Bruno
Fri Jun 6, 7:45 PM ET

DENVER (Billboard) - Arguably the No. 1 item on record labels' to-do list for the year is, "Establish variable pricing for digital downloads."

As luck would have it, the No. 1 item on the to-do list of digital music services not named iTunes is converting their library to digital rights management-free sales. So it comes as no surprise that the labels have made an openness to variable pricing a prerequisite of any DRM-free licensing negotiations.

That digital music sales are not yet compensating for falling CD revenue is no secret. Whether experimenting with the price of digital music will make any difference remains to be seen.

According to a recent survey by analysts at IDC, music is not exactly a high priority for U.S. households. A full 25% of respondents say they spend nothing on average each month on music in any format. Another 23% report spending less than $10 per month on average, while 27% say they spend between $10 and $25 per month. Far fewer households spend more than that.

CDs remain the most popular source of music, at 32%, followed by FM radio (31%) and dropping sharply to paid online music services (8%). Peer-to-peer services follow closely behind at 5%. For those who did pay for music, 33% downloaded between 10 and 50 songs in the six months preceding the survey, while 26% downloaded less than 10.

"Digital music services in aggregate . . . have yet to fully live up to their potential in becoming the next medium of choice for music purchases," IDC analyst Susan Kevorkian says. "(Variable pricing) is one way to make that happen."

The idea behind variable pricing is to make more money from those 33% who downloaded up to 50 songs in six months by slightly raising the price on certain tracks,
while at the same time convincing those who only downloaded 10 or fewer to buy more by slightly lowering the price of others.

How that's done is where the real science kicks in, which is why even those labels pushing for variable pricing most aggressively are still only in the test phase. The latest is Warner Music Group (WMG), which last month began a trial of a dynamic pricing system from Digonex.

The company's system recommends raising or lowering the price of a track and/or album based on a variety of factors. In some cases, new releases selling very well may get priced higher, but so might catalog items appealing only to the die-hard fan willing to pay more. In other cases, the system recommends lowering the price of even new releases to spur more sales.

Digital service PassAlong, which operates its own branded digital music store as well as providing the back-end technology to several others, two months ago completed a test of the Digonex variable pricing system conducted with Canadian label Nettwerk.

Once per week for 16 weeks, the service altered the price on around 2,000 tracks participating in the trial based on the suggestions from Digonex. Singles were priced at 99 cents, 66 cents and 33 cents, with albums priced more granularly.

According to PassAlong CEO David Jaworski, the system on average priced full albums $1.18 less than what other services were selling them for -- between $4 and $6. Singles pricing also fell on average. However, revenue from the tracks included in the program increased an average of 122%, with some individual singles' sales spiking up to 500%.

"We had albums that weren't selling at all before the pilot that started generating revenue every week," he says.

What's more, as the price of a hot single rose, the price of the album dropped, which encouraged more album sales.

"There'd be a point where people who would only buy two or three tracks bought the entire album," Jaworski says. "They really came shopping for those two or three tracks."

However, the test did not include single sales for more than 99 cents, so the jury is still out on whether variable pricing or "elasticity" can support more expensive singles. Jaworski says PassAlong will conduct another test soon that includes more pricing tiers, as well as more music from major labels, but is not commenting on whether PassAlong is part of the WMG trial.

While other digital music services either have variable pricing in place today -- such as Amazonmp3 -- or plan to begin testing it in the near future as part of new DRM-free deals -- such as Napster -- the real impact of the strategy won't be felt until the market-leading iTunes comes onboard or its rivals step out of its shadows in a meaningful way.

Aside from a brief flirtation with a $1.29 price point when EMI Group launched DRM-free downloads on iTunes, Apple CEO Steve Jobs to date has resisted straying from the 99-cents-per-song strategy for fear of confusing customers. Although the company has already started pricing TV shows from HBO at different levels, it is unlikely that development represents a shift in its music strategy.

In the meantime, the music industry hopes the one-two punch of DRM-free music and
flexible pricing will help empower its competitors.

"In conjunction with DRM-free downloads, it gets to be a very compelling value proposition," Kevorkian says. "Transitioning to a variable pricing doesn't need to be static. There's lots of room for experimentation. There's still plenty of room for change."

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