Online music: The price remains the same
Recent rumblings show the war between the technology and music industries is heating up.
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By Eric Hellweg, CNN/Money contributing columnist

BOSTON (CNN/Money) - The news hit me like a John Bonham bass-drum kick to the gut: Record labels want to raise the wholesale prices of songs on downloading sites like iTunes, Napster, and Yahoo! MusicMatch, according to a report in Monday's Financial Times.

I just couldn't believe the industry would move to hike prices so quickly in a nascent market that, for all its ballyhooed success, still accounts for only a low-single-digit percentage of overall music sales.

I set out to find more information, but none of the major labels and none of the aforementioned music sites would comment for the record about the report. While I can't vouch for the story's veracity, however, it's not surprising to hear that the labels might want a price increase. "They're definitely interested in raising prices," one source who requested anonymity told me.

Labels making noise?

The news comes at a time when Apple is likely renegotiating its annual contracts with some of its content partners. Last April, on the one-year anniversary of the company's introduction of its groundbreaking iTunes online music store, we saw the results of the first round of renegotiating: Apple was able to increase the number of computers a purchased song could play on from three to five, but the labels brought down the number of times a playlist could be burned from 10 to seven.

"The labels want to feel like they have some power and influence," says Phil Leigh, an analyst with Inside Digital Media. "They're losing the control they once had."

It's possible that music labels have decided to focus on controlling pricing in this early round of renegotiations. It's unlikely, however, that they will get what they want -- at least for now.

"We view price increases as inevitable," says Gene
Munster, an analyst who covers Napster and Real for Piper Jaffray. "But we believe it's premature at this point." (Piper Jaffray has provided Napster with investment banking services within the past six months.)

**Price hikes could dampen sales**

Munster and others say a price increase at this stage of the digital music market evolution would have a deleterious effect on download sales -- and on the earnings of online music sellers. A hike would likely tamp consumer interest in purchasing tracks, and if the sellers ate the wholesale increase and kept the retail price the same, already paper-thin margins would all but disappear.

A price increase would have a dramatic impact," Munster says.

One thing is clear: With the proven success of paid online distribution, the power struggle between the music industry and technology companies is reaching a new level.

The labels tried for years to figure out a successful online strategy on their own, through legal tactics, political efforts, and failed early versions of Web retail shops such as PressPlay and MusicNet. It was only after technology companies -- most notably Apple -- took charge that legitimate online music took off.

But one thing hasn't changed. The labels need the technology companies' distribution, and the technology companies need the labels' content.

Right now the technology companies are in a better position, thanks entirely to their cracking the code of legitimate online music sales. It's hardly a coincidence that the major labels finally saw their fortunes reverse in 2004, posting their first sales increases after five years of decline just as online music was taking off.

As such, investors needn't panic about this most recent report. The wholesale pricing and rights issues will remain a rub for these two industries in the foreseeable future, but for now the technology camp has the upper hand.

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