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The Sweet Sound Of Success

By MARK HALPER | Sunday, Aug. 08, 2004

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It was a gloomy December morning in Helsinki in 1997 when 26-year-old Vesku Paananen woke up with a hangover after a night of Koskenkorva vodka and beer. Paananen, a chief technology officer with new-media company Yomi Group, was jolted out of bed by the annoying ring tone of his Nokia 6110 mobile phone. "I didn't want to hear '*de de de de deeee'* ever again," Paananen recalls. "I wanted to hear Van Halen's *Jump*, and I was willing to pay for it." The technology was there to program mobile phones to play pop tunes rather than electronic bleeps, so he tried to talk operators and handset makers into offering a selection of popular hits. But his pleas fell on deaf ears: "The biggest resistance was from the operators, who said, 'Ring tones, what's that?'"

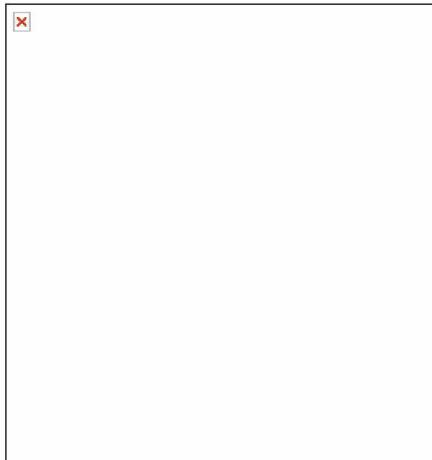
After almost a year of failed pitches, Paananen managed to convince Finnish operator Radiolinja that ring tones could help workers in open-plan offices distinguish their own incoming calls from those of others. So in the fall of 1998, Radiolinja launched the world's first commercially available ring-tone service, allowing users to download songs like *Smoke on the Water* and the Finnish national anthem.

An industry was born, and last year about 2.6 billion ring tones — those musical ditties that sound off when a mobile phone receives a call — were downloaded worldwide, one-third of them in Japan. Delivered by the Internet or text message, they account for 80-95% of a "phone personalization" market that was worth \$3.2 billion last year and will reach \$6.5 billion in 2008, according to London market-research firm Ovum. That makes ring tones a bigger business than CD singles, which last year racked up \$1.4 billion in sales. And the market is even bigger if "caller tones" — in which the caller, not the recipient, hears the tune — are included. Caller tones are already big in Korea, and Ovum predicts they'll be worth an additional \$2.8 billion globally in 2008.

With that kind of money in play and with new "real tones" that play actual (rather than synthesized) songs, a battle is brewing. Mobile operators and the small outfits that supply the synthesized songs — Finland's Jippii, Italy's Buongiorno Vitaminic, France's Musiwave and Germany's Jamba! — are clashing with the big record labels over whose slice of the ring-tone pie should be biggest.

But how did an unlikely innovation like ring tones get to be such a big business in the first place? It's definitely not about the music. Most ring tones are only about 20-30 seconds long, and until recently have had at best [an error occurred while processing this directive] an approximate relationship to the melodies on which they're based. But like the craze for plastic mobile-phone covers, ring tones are more about making a personal fashion statement. "You're not buying a ring tone to enjoy Christina Aguilera," says Ovum analyst Dario Betti. "You're buying it to tell everyone else who you are." And for that assertion of identity, high-use mobile-phone customers (read: teenagers) are willing to pay dearly. British consumers pay the most — between \$2.70 and \$6.40 for a ring tone, while it costs just \$1.45 to get the whole song online. Though charges elsewhere are less, replacement rates can range from once a year to several times a month, and some users change frequently "based on movements in the music Top 10," says Ovum's Betti.

The latest innovation is real tones — genuine song excerpts, not electronic cover versions. First introduced in Japan in 2002 and Europe last year, they are a fast-growing segment of the market. And that's where the record labels come in. Still hurting from a 7.6% drop in sales to \$32 billion in 2003, the labels have been left out of the ring-tone party because they don't own the synthesized tones; instead, composers and song publishers have been claiming up to 20% of royalties from suppliers who have been "composing" ring tones based on originals. But "real tones" come straight from the record companies, and they're demanding a big piece of the action: as much as 50% of sales. The



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SINGLE LIFE: In some markets, artists like Usher, left, sell more ring tones than singles

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disarray. Up until now, mobile operators like Vodafone and Orange have taken around 40% of the ring-tone fee; middlemen like Musiwave and Buongiorno, whose roles range from composing and aggregating songs to delivering them, around 40%; and music publishers — which are sometimes owned by labels and sometimes aren't — up to 20%, which they share with the actual songwriters. "The 40% that's getting squeezed are the guys in the middle," says Patrick Parodi, chairman of the London-based Mobile Entertainment Forum, an industry association whose members include companies from all sectors of the ring-tone business.

Not surprisingly, the middlemen firms don't want to give up their cut to the labels, and fear a fight over percentages could push up prices. Andrea Casalini, chief executive of Buongiorno, argues that record companies "should consider low double digits as reasonable. Ultimately, they'll realize that if they make rational judgements on pricing, the market will keep on growing. Otherwise, they'll limit the growth."

If middlemen like Buongiorno are looking for sympathy from mobile operators, they're unlikely to get it. Operators don't ultimately care much where the tones come from, and increasingly they are hooking up directly with the record labels on real tones. Industry sources say that operators, too, are unhappy with the share that labels are seeking, though Vodafone's head of music Edward Kershaw says, "I don't think [the record labels] are being unrealistic." Not to be forgotten are the music publishers and artists, who complain their rights are ignored. "For the most part, they are not getting paid," says David Simmons, chief executive of Songseekers International, a London company that represents EMI's publishing division in ring-tone matters. He says publishers last year collected just \$3.6 million in ring-tone-related fees in Britain, well below 10-20% of that country's estimated \$130 to \$165 million in overall sales. That's because many fly-by-night ring-tone suppliers are not paying. So national "copyright collecting societies" are stepping up their efforts to monitor ring-tone companies.

In response to the squeeze on their earnings, the middlemen are rushing to consolidate. Last month, Britain's iTouch bought Jippii for £12 million; in June, the Mountain View, California-based security company VeriSign Inc. bought Jamba! for \$273 million. If the merging middlemen can gain some market clout, they might be able to retain their early advantage. But if real-tone songs catch on, firms like Jippii and Jamba! could well find themselves out of business. Either way, ring-tone companies will have to change their tune fast. Otherwise, the industry that Paananen helped launch may be in for a hangover of its own.

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