

IFPI Music
Piracy Report 2000

june 2000



representing the
recording industry
worldwide



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Introduction

Music piracy is proliferating, driven by increased traffic in mass-produced audio CDs, an alarming surge in illegal sales of CD-Recordable discs and an exponential spread of pirate music files on the internet. Underpinning these trends has been a huge increase in global optical disc manufacturing capacity, far outpacing the growth of legitimate demand. There is also increasing evidence of the link between CD piracy and organised crime.

Against this background, IFPI's recently-created global anti-piracy structure has made substantial headway in 1999 and 2000. Several modern plants, operating covertly, were put out of action in Latin America, Europe and South East Asia in 1999. There have also been a number of ground-breaking cases of litigation against pirate operators, both physical and online.

There have been some encouraging steps to fight piracy by a number of governments, with notable initiatives in Hong Kong, Bulgaria, parts of Latin America and by the European Parliament in Brussels. In most high-piracy territories, however, the response by government and enforcement agencies falls far short of what is required to tackle the problem.

The spread of piracy, both of CDs and on the internet, is the greatest threat to the legitimate music industry. The future of a dynamic creative sector, of artists' livelihoods and of hundreds of thousands of jobs are all at stake. The need for governments worldwide to provide strong laws, effective enforcement and adequate deterrent penalties against piracy has never been greater.

Summary

The global pirate music market is estimated to have totalled 1.9 billion units in 1999, with an increase in CD piracy partly offsetting a worldwide decline in sales of illegal music cassettes, which fell to 1.4 billion units. Total sales of pirate music CDs topped 500 million units for the first time, with pressed pirate CDs (as opposed to CD-Rs) rising to an estimated 450 million units, from 400 in 1998.

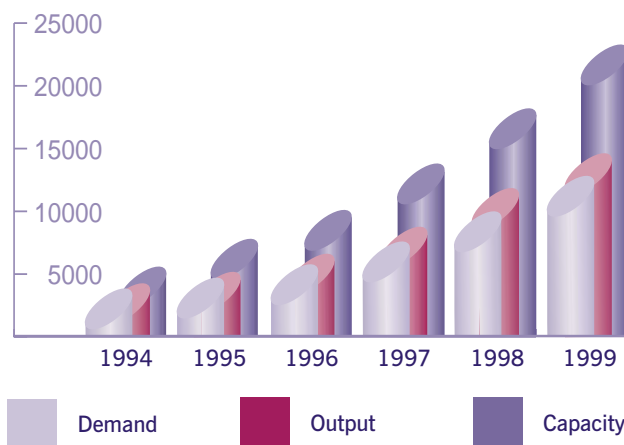
Pirate CD-Recordable discs are making a significant impact. IFPI's first estimate is that pirate music CD-R sales amounted to at least 60 million units in 1999. Further research showed seizures worldwide of more than 1 million CD-R discs annually. This is unquestionably the tip of the iceberg. Total CD-R sales in all formats worldwide (audio and non-audio) more than doubled in 1999 to 1.5 billion units.

The total value of the pirate music market in 1999, including sales of audio CDs, cassettes and CD-Rs, is estimated at \$4.1 billion – less than the estimated value in 1998, reflecting falling prices of illegal recordings and the decline in pirate sales of cassettes, particularly in Latin America, South East Asia and eastern Europe, where poor economic conditions prevailed.

Underlying these trends was another year of dramatic growth in global optical disc manufacturing capacity. World capacity of all disc formats (including audio, CD-ROMs, CD-Rs and Video-CDs), rose 28% to 23 billion units in 1999. Over the past five years manufacturing capacity has increased by 340%. The number of known CD plants increased by 75 during the year, to 660.

Optical Disc Manufacturing (all formats)

million units



Region by region, South East Asia remains a huge source of pirate CD production despite a fall in pirate sales in Hong Kong. In Europe, Ukraine poses the greatest threat to legitimate markets, although illegal manufacturing by disc plants in western Europe is also a substantial problem. Brazil and Paraguay stand out as the markets most under attack by CD and cassette pirates in Latin America.

The following table lists those countries where known overcapacity is thought to be driving very high levels of pirate production:

Current Estimated Pressing Capacity

| Country | Current estimated capacity – all formats (million units) | Total legitimate demand for all discs 1999 (million units) |
|----------------|--|--|
| Taiwan | 3,900 | 190 |
| Hong Kong | 2,800 | 140 |
| China | 680 | 620 |
| Singapore | 490 | 50 |
| Macau | 340 | negligible |
| Malaysia | 280 | 50 |
| Czech Republic | 90 | 25 |
| Russia | 90 | 30 |
| Israel* | 90 | 9 |
| Ukraine | 70 | 5 |

*Not including Palestine Authority

Paraguay – there are believed to be underground CD plants, but no known legitimate ones

Internet piracy spread dramatically during the year, through file-sharing services and on websites, but it is impossible to quantify the extent of the problem accurately. An estimate by Forrester Research puts the number of illegal downloads of music files at more than 1 billion in 1999. IFPI estimates that several million music files are available on the internet through file-sharing services such as Napster alone.

CD Piracy and Organised Crime

Evidence of the link between music piracy and organised crime became apparent in the late 1990s as the CD format offered crime syndicates a simple, cheap and highly lucrative entry into a mass-scale illegal trade. In 1999 and early 2000 a number of cases were uncovered showing the convergence between CD piracy and other forms of serious and organised crime.

They include the arrests by London police of members of a Russian crime ring charged with being involved in large-scale credit card fraud as well as in the traffic of pirate CDs; arrests by anti-mafia police in Italy and reports from the General Attorney of Naples that 100 Camorra gangs are involved in piracy as well as in drugs, firearms and extortion; and the crackdown by Dutch police against a US\$50 million CD pirate ring in raids which seized firearms and large amounts of cash.

Other seizures in the year showed the growing scale, sophistication and audacity of the international pirate traders – exemplified by the seizure in Frankfurt in January of half a million CDs manufactured in Ukraine and bound for Uruguay. The flood of international pirate traffic from South East Asia into Latin America, which began in 1998, continued in 1999. A new phenomenon of wholly “underground” pirate CD plants also emerged for the first time in 1999 (see next page). Illicit plants have been uncovered in Latin America, Asia and Europe. The trend reflects a move by the largely South East Asian-based pirate syndicates into local manufacturing in Latin America, complementing the existing direct exports.

The music industry responds: enforcement and litigation

In 1998 IFPI established a new enforcement structure to match the global proliferation of CD piracy with a commensurate global response. That structure is now operating through a network of regional offices throughout the world. It takes a “zero tolerance” approach to piracy, an approach that has reaped results.

In November 1999 IFPI's Main Board granted new resources to the enforcement structure, which will double the team's headcount to around 50 in the year ahead. The expansion reflects the rapid growth of IFPI's investigative and litigation activity. There are presently more than 100 cases involving cross-border pirate traffic under investigation, and more than 20 cases of litigation in progress. IFPI's anti-piracy resources now include a training section to work with enforcement authorities worldwide, a central forensic facility and state-of-the-art intelligence processes.

There were significant anti-piracy successes in 1999. Total seizures of optical discs were roughly on a par with 1998 at 60 million. Some 15 million illegal CDs were seized in Latin America, largely sourced from South East Asia, taking the total to 34 million CDs seized in that region over the past two years.

Even more significant in 1999 were the actions against entire underground CD plants in Holland, Philippines and Paraguay. Most spectacular were raids in Paraguay which uncovered two plants with an annual production capacity of some 50 million CDs. Syndicates based in Hong Kong were behind these illegal businesses.

Enforcement successes have set in motion a series of litigation cases by IFPI, its national groups and its US affiliate, the RIAA. These have a major deterrent effect on future would-be infringers. In November RIAA won record damages of US\$13.7 million against Global Arts Productions and Danny Jordan who had engaged in back catalogue piracy internationally; IFPI reached a US\$1 million settlement – the largest in Europe – with a mastering plant in Switzerland over unauthorised mastering of IFPI members' sound recordings for Bulgarian and Ukrainian clients during 1997 and 1998.

Another litigation case, involving Golden Science, taken jointly with the Motion Picture Association (MPA), exemplifies the increasing cooperation between IFPI and other optical disc based industries. This civil litigation followed the largest ever seizure of optical discs in 1998, a massive 22 million units in a case involving charges of corruption on the part of a senior customs official.

Government anti-piracy strategies: some highlights in 1999/2000

- Controlling optical disc manufacturing is a key part of governments' fight against piracy. There have been encouraging steps on this front. CD plant regulations have been introduced in Hong Kong and Bulgaria, and they are in preparation in Malaysia, India, Thailand and Macau.
- Hong Kong adopted legislation recognising copyright piracy as a serious and organised crime. This gives stronger powers to enforcement officers and the courts. A newly-formed Special Enforcement Team has focused on raids against pirate outlets in shopping centres and street-level stores. Meanwhile, Hong Kong Customs now has a substantially enlarged IPR enforcement team, with over 300 officers that are actively taking action against pirates.
- Poland belatedly adopted a new anti-piracy law which should help lower one of the highest piracy rates in eastern Europe; Italy, with the highest piracy rate in western Europe after Greece, failed to deliver on years of promises to enact a new anti-piracy law.
- The European Parliament adopted a report on the EC Green Paper on Piracy and Counterfeiting in the Single Market calling for increased co-operation between rights owners and authorities in dealing with cross-border piracy in the EU and eastern Europe, higher deterrent penalties and controls to prevent the manufacture of pirate CDs.
- Ukraine failed, in 1999 and to date, to tackle its mounting pirate manufacturing levels and needs both legislation and effective enforcement. Ukraine is one of a number of territories coming under strong pressure from the US government through the “Special 301” provisions of its trade legislation.
- Israel, also under scrutiny by the US government, has seen an alarming increase in piracy reflecting a breakdown in the enforcement process.
- There was no sign of improvement in China for the whole of 1999. Piracy remained high and the figure released by the government suggested that the piracy rate was running as high as 90%. There were large-scale imports of pirated products from surrounding areas and the number of production lines has also increased. However, the government will be obliged to take more determined enforcement actions against pirates after the official WTO accession of China.
- Mexico enacted a new anti-piracy law in May 1999, allowing for better enforcement. This has helped reduce piracy in the country.

Internet Piracy

Internet piracy spread rapidly in 1999 and early 2000, but it is too early to quantify the economic impact on the music market. Online piracy poses exactly the same threat as its physical equivalent to the creativity of artists and the investment of record producers. Potentially its impact is far greater than physical piracy. Internet piracy hampers the industry's efforts to give consumers the benefits of a legitimate online music market. Record companies are making steady progress towards legitimate online business models, via a string of internet corporate investments and joint ventures, and through the technological forum of the Secure Digital Music Initiative (SDMI) and DVD-Audio.

IFPI's response to internet piracy is a combination of education of consumers and service providers and, where necessary, strategic litigation to remove infringing sites. A newly-formed dedicated internet piracy unit is developing a fully automated search and identification service, jointly with the Motion Picture Association (MPA).

Legislation also plays a vital role in the fight against internet piracy. In the USA the Digital Millennium Copyright Act (DMCA) was adopted at the end of 1998. In Europe, the Copyright Directive was first proposed in 1997 to allow rights owners adequate rights and technical controls to protect their works. These legislative measures are the implementation vehicle for the WIPO Treaties, concluded in December 1996. They provide the legal foundation for the development of a legitimate online music industry internationally, and need to be ratified in 30 territories worldwide in order to come into force. By early 2000, approximately 15 countries in Latin America, Asia, central and eastern Europe, and the US had already ratified the treaties.

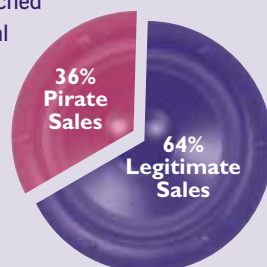
On the litigation front, the RIAA in the United States has spearheaded the industry's response against infringers such as MyMP3.com and Napster which have tried to build large-scale businesses based on breaching copyright. These actions have attracted strong support from artists. Internationally, IFPI and its national groups have taken action to close down thousands of pirate sites. A global internet piracy campaign launched in October 1999 drew support from hundreds of artists worldwide. There have also been successful legal actions against internet service providers (ISPs) and content providers, notably:

- Belgium: a court decision against an ISP and against a website operator who offered on his site links to 25,000 illegally posted sound recordings
- France: Criminal litigation against two individuals who operated illegal link sites. This litigation ended with damages of US\$15,000 and suspended prison sentences
- China: a settlement between several major record companies and the leading TV portal operator MyWeb which had provided links to infringing MP3 files. IFPI filed a lawsuit against MyWeb in December 1999

Governments in the fight against piracy

Music piracy erodes culture, destabilises legitimate economic activity and nurtures serious crime. It also robs governments of hundreds of millions of dollars in unpaid tax revenues and lost investment. Governments have a key role to play in supporting the efforts of the music sector and other copyright industries in the fight against piracy. Legislation and enforcement strategies in many territories are woefully mismatched to the scale of today's international piracy business.

One in three recordings worldwide is pirate



The recording industry's two key priorities are:

- Adequate legislation: IFPI's anti-piracy efforts have shown that in many jurisdictions intellectual property protection is inadequate. New legislation is also needed to give governments tighter controls over the operations of CD plants.
- Effective enforcement: in many territories, enforcement agencies are inadequately resourced and ineffectively managed to tackle piracy. In particular they are unequal to the global spread of today's pirate networks. In many cases, fighting piracy is given a very low priority and penalties handed out by courts are often derisory.

High domestic piracy rates

IFPI's anti-piracy activities focus both on countries that are heavy producers of pirate CDs, and on territories where the levels of domestic piracy are excessively high. The following table provides information on the current priorities for IFPI in terms of domestic piracy:

Current IFPI priorities in terms of domestic piracy levels in 1999

| Country | Piracy (US\$m) | Piracy Level (Units) |
|-----------|----------------|----------------------|
| China | 620 | 90% |
| Russia | 200 | 75% |
| Brazil | 180 | 50% |
| Italy | 115 | 25% |
| Mexico | 75 | 40% |
| Taiwan | 70 | 25% |
| Poland | 55 | 50% |
| Israel | 45 | 60% |
| Greece | 45 | 45% |
| Hong Kong | 25 | 50% |

Regional View

North America

The level of piracy over all in the region remains low, which is to a large extent due to an aggressive litigation strategy against pirate producers. In the US, the RIAA reported an increase in CD-R seizures. Internet piracy has become a priority issue with lawsuits filed against MP3.com and Napster.

Europe

Domestic piracy rates are considerably higher in eastern than in western Europe, with the notable exception of Italy and Greece. Finland has been increasingly affected by pirate product entering from Estonia, with piracy rising to over 10% of the market. CD-R piracy is a growing problem. In eastern Europe, piracy levels remain stubbornly high in Russia, Ukraine, CIS, the Baltic States, Bulgaria, Romania and Poland, restricting development of those developing markets.

Asia

Asia remains one of the high-piracy regions in the world both in terms of domestic piracy levels and production of pirate material. China saw almost 100% growth in the pirate market with a proliferation of different disc formats. There has been an improvement in Hong Kong (piracy down from 70% to 50% in 1999) due to new laws and strong government action against pirate retail outlets. Other countries such as India, Pakistan and Malaysia also show very high piracy levels.

Latin America

CD piracy is estimated at about 30% throughout the region. Cassette piracy has virtually destroyed the cassette markets of countries such as Brazil. In 1999 the piracy rate in Brazil grew from 45% to 50% as a result of a deteriorating economy and inadequate enforcement measures by the government. The value of pirate sales was down due to lower pirate prices. Mexico saw a slight improvement to 40% due to a new law and more effective enforcement action coupled with economic recovery. CD-R piracy is increasingly affecting Latin America, particularly Argentina, Colombia, Mexico and Peru.

One of the biggest concerns for the recording industry remains Paraguay, used widely as a transshipment point by Asian organised crime groups for distribution throughout Latin America.

Middle East

Israel's piracy sales value increased sharply in 1999 due to inadequate enforcement. The deteriorating situation also affects the territories of the Palestine Authority. The average level of piracy across the Middle East region was over 30%, running at a much higher rate in Egypt, Israel, Kuwait and Lebanon. Piracy levels fell in Bahrain and Oman and remain low in the UAE. Outside Israel, cassette sales continued to account for the bulk of pirate unit sales.

Africa

Piracy in South Africa and Zimbabwe is around 15%. Elsewhere in Africa, however, the figure is thought to be above 50%. CD-R piracy is a growing problem.

Australasia

Piracy in Australia and New Zealand has increased since the lifting of parallel imports restrictions, but remains at comparatively low levels.

Note

The value of pirate sales is calculated at local pirate prices, which fell in many of the high piracy regions – particularly Asia, Latin America and eastern Europe. If legitimate prices were applied, the value would be much higher.

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Communications and the Market
Research Departments
IFPI Secretariat
54 Regent Street
London W1R 5PJ
Tel: +44 (0)20 7878 7900
Fax: +44 (0)20 7878 7950
Email: info@ifpi.org
Web: www.ifpi.org

Level of domestic piracy 1999 (units)

| | Over 50% | 25-50% | 10-25% | Less than 10% |
|--------------------|---|---|--|---|
| North America | | | | Canada USA |
| Europe | Bulgaria CIS (other) Estonia Latvia Lithuania Romania Russia Ukraine | Cyprus Greece Poland Slovenia | Finland Hungary Italy | Austria Belgium Czech Republic Denmark France Germany Iceland Ireland Netherlands Norway Portugal Slovakia Spain Sweden Switzerland UK |
| Asia | China Pakistan | Hong Kong India Malaysia Thailand | Indonesia Philippines Singapore South Korea Taiwan | Japan |
| Latin America | Bolivia Central America Ecuador Paraguay Peru | Brazil Colombia Mexico Uruguay Venezuela | Argentina Chile | |
| Australasia | | | | Australia New Zealand |
| Middle East/Turkey | Israel Palestine Authority | Egypt Kuwait Lebanon Qatar Saudi Arabia Turkey | Bahrain Oman | UAE |
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IFPI Secretariat
54 Regent Street
London, W1R 5PJ
Tel: +44 (0)20 7878 7900
Fax: +44 (0)20 7878 7950
www.ifpi.org