

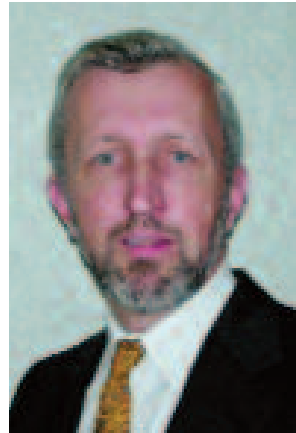
The Music Industry's “X” Factor

From a distance of 30 feet, a fine Stradivarius and a cheap Chinese violin are visually indistinguishable to all but the most sharp-eyed experts. And despite all of today's digital audio wizardry, there is also no way to accurately differentiate the two instruments through sonic analysis. But put the violins in the hands of a player of even modest abilities, and they can, within a few notes, readily understand why one is worth \$3.0 million and the other a mere \$59. This curious situation defines the entire music products industry. The products that we sell are differentiated by qualities that are impossible to measure precisely, and equally difficult to explain. However, for the end-user these intangibles are very real and are what drive purchasing decisions. For lack of a better word, we'll call these intangibles the “x” factor.

These hard-to-pin-down qualities of “tone” and “feel” and “presence” call to mind Louis Armstrong's famous summation of jazz: “If I have to explain it to you, you wouldn't understand anyway.” Despite the seeming impossibilities of reducing this “x” factor down to a neat equation, that doesn't stop some people from trying. Amazon.com lists over a dozen books purporting to explain the secret of the Stradivarius violin. (Not surprisingly, there is little agreement on exactly what the “secret” is.) We've seen similar scientific studies attempting to pinpoint the essence of great tube distortion, superior piano tone, or a magically warm vocal mic. These efforts are not without value, but ultimately they never fully explain the elusive “x” factor. If they did, the product development craft would have been completely formulized by now, and everything on the market would be flawless.

The importance of these intangibles transcends product design and development and permeates every facet of our industry. Which explains, to a large degree, why this business is different from most others. Like the guy measuring harmonics in an effort to recreate the magic of a Strad, a hot-shot MBA trying to make sense of a successful music enterprise relying on only an Excel spreadsheet is never going to fully understand what it's all about.

We're all for using quantitative tools for analyzing a business. In fact, understanding the turn rate and margin



performance of every SKU in a store is vital in today's increasingly competitive market. However, a grasp of the numbers alone isn't enough. Rembrandt had a thorough grasp of the mathematical rules of perspective, but the genius of his art was in the subtle ways he occasionally bent, or even ignored the rules. On a somewhat more mundane level, the art of a successful music business also relies on knowing when to stick to the numbers and when to ignore them. When is it worth setting aside cost considerations to help a band director, an anxious parent, or a local performer in a bind? What slow-turning products are worth keeping in stock because they create a “halo” effect? These are just a few basic questions that can't be answered through a numeric analysis alone.

Over the past few years, outside investors have poured considerable amounts of capital into our industry. If the past is any guide, we suspect that most of them will exit disappointed and a good deal poorer for their efforts. One reason is that music industry growth has never been terribly predictable or persistent. Equally important is the fact that some, but certainly not all, of the outsiders have a tendency to dismiss the importance of the “x” factor in their scramble to reduce the business to a straightforward formula. Just because you can't measure it doesn't mean it isn't real.

With the opening of the NAMM show and the beginning of the new year, it's worth stopping a moment to think about the undefinable “x” factor that characterizes our industry. It can be vexing, but at the end of the day it's what makes our work more satisfying than selling toothpaste or heating oil.

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