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CONTRIBUTION OF CULTURAL ECONOMICS TO THE ANALYSIS OF THE CREATIVE INDUSTRIES

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Notes for a talk to WIPO International Conference on IP and the Creative Industries
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Introduction: Why measure the creative industries?

Cultural economics is a branch of economics and so shares its theories, its methodology and its concern with empirical testing; it applies these concepts to the cultural sector of the economy, partly in the same way as economics is applied to any other sector (health, education, electricity …) and partly by differentiating those features of the cultural economy that differ from other sectors. What is different about the creative industries is 1) that they produce goods and services with culturally significant content and 2) the primary creators – artists (using that term in a loose sense) – appear to be untypical as workers. Cultural economics therefore has specialised in understanding (or trying to understand) the interaction between economics, culture and creativity. It is therefore well set up to consider the role of copyright in the creative industries.

Nevertheless, cultural economists do not go in for special pleading and the case for state intervention, as in any area of the economy, has to be made within the framework of accepted economic doctrine. Where the market would fail, the state may encourage the reallocation of resources by various financial means (often subsidies) and by regulation. Thus, establishing property rights and transferring funds from taxpayers to organisations they choose to support is part of the economist's mission to improve the workings of the market. This is not supporting 'lame ducks': market failure is the inherent failure of the market economy to work properly under certain circumstances.

In general, the aim of an economy is taken to be the enhancement of welfare and that is achieved, among other ways, by real growth. Therefore, knowing which industries and sectors of the economy contribute most to economic growth is important for governments with that aim. However, growth at all costs is not an economic goal and the cohesion of a society through education, science and culture are also vital.

Economists see the economy as being inherently flexible and responsive to supply and demand: when goods are in demand they will be produced and marketed to consumers who pay for them. When those goods are no longer in demand, producers must adjust by producing other goods or going out of business. This is the law of the market for any goods but, as mentioned above, some may be subsidised even if they do not succeed on the market for reasons of social choice. However, when firms go out of business, the resources they use are channelled by the market into other uses or industries: the goods may no longer be produced but others are and so the process of economic growth goes on. Moreover, all this plays out in an international environment of trade in which producers in some countries simply have better techniques and resources for producing some goods than others do elsewhere and so trade is beneficial as it allows the best use of global resources and contributes to increased growth worldwide.

All this is to say that, while it is important for governments to study the sources of wealth and growth in their economies, there is no particular reason to favour one industry over another. Of course, producers and industry bodies will lobby governments for any benefits they can profitably obtain and in that pursuit they have the incentive to produce figures showing how significant their enterprises are in the economy. They may even do this with as much accuracy as is possible but there is strong incentive to over-exaggerate their view of the underlying causal factors and this is certainly what we have observed in the arena of copyright and the creative industries. Showing that the arts or the cultural industries account for *x* percent of national income does not imply that withdrawing subsidy or protection by copyright law would reduce income by *x* percent, though that is commonly said by industry advocates, and what 'strength' of copyright is needed cannot be inferred just from such data.

Besides their interest long term economic growth, economists are also concerned with the efficient use of resources in the short run and that leads to the study of industrial organization and the degree of competition in markets because that is part of the welfare equation: competition drives down prices and that means consumers can buy more for their money. Copyright and other IP are a matter of concern to economists because of the monopoly power copyright can convey.

Moreover, while governments are concerned with the efficient allocation of resources, policies are more often motivated by concerns with equity and the distribution of economic welfare within the country or region and this is also a concern for international policy-makers. Growth is very often uneven and though it may benefit some sections of the population, others are left behind. The division of incomes between workers and employers (industries) has long been a concern of democratic governments and workers' bargaining power is supported by various means. However, as we see in the cultural sector, creators by and large are not in a strong bargaining position and it has been one of the contributions of cultural economics to study artists' labour markets. This is the basis for my contribution to this conference on IP and the creative industries.

Special features of the creative industries

The creative industries are a mixed bunch: there are the 'traditional' creative and performing arts (visual arts, literature, music, dance, opera, drama) and the cultural industries (film, radio, television, sound recording, multi-media). Other industries that utilise the ideas and skills of artists and other content creators and the media as well, such as fashion, advertising and computer software, are also included in the list. In most countries the 'high' arts are supported by some form of government intervention, whether state provision, government subsidy or indirect support via tax breaks and the like, in accordance with cultural policy. The creative industries may be publicly or privately owned, subsidised, assisted through the tax system and, in the case of broadcasting, regulated. At their core is the increasing significance in post-industrial economies of intangible production relying upon copyright law to establish property rights, protect revenues and thereby provide incentives to creativity. And with the advent of the Internet, the focus is on the creation of information and its delivery. As with all technological revolutions, these changes have altered the pattern of demand for workers, reducing the employment in the cultural sector of some types of artists and increasing it for others; they also have been the cause of the superstar phenomenon in the cultural sector.

However, as Caves (2000) observed in his book, *Creative Industries: Contracts between Art and Commerce*, there is a tension between the artists and what he called the 'humdrum' side of business and by and large, except in the case of the few superstars, the business side has the upper hand for both 'good' and 'bad' economic reasons: the good reasons are that the industry side puts up a lot of finance and has to protect its interests; the bad side is that with numerous artists available, the individual artist has little power to insist on a good deal. One of the questions that has been asked in cultural economics is the extent to which copyright law protects each party in the contracts between art and commerce: mostly, the creator has to transfer her economic rights and thereby loses control of her ability to earn from her work.

Economic role of copyright

Copyright law is a clever system for financing the creation of works of art, literature, music etc: by granting statutory property rights to creators, it makes it possible for them to charge for the use of their work. That control enables them, at least in principle, to charge a royalty for its use (the economic right) and to protect the type of use made of those works - the so-called moral rights. In the inimitable words of the English lawyer and politician Macaulay in 1841: 'Copyright is tax on readers for the purpose of providing a bounty for writers'. This is the basic economic principle of copyright law: it provides an incentive to creativity through the higher price that the grant of copyright protection makes possible. The monopoly revenues of the sales of works of art are the reward for creating them. In other words, copyright is a trade-off between the incentive to supply creative works and the disincentive to buy them at a higher than competitive price.

Copyright finances the creation of works of art by charging users for the use they make of those works: the more popular the work, the greater the income it generates for the author and publisher. The higher the price that users can be made to pay, the greater the royalty the copyright holder. Though this and other aspects of the monopoly power of copyright holders are often deplored, that is precisely how the system is supposed to work, as Macaulay very well understood! And although in the cultural sector we are much more familiar with the use of subsidy by taxpayers to finance artistic production, it may well be said that copyright is a preferable method of finance to that by taxpayers – taxpayers have no choice how much is spent on the arts except through the ballot box, whereas these schemes allow users to finance their chosen cultural products.

Cultural economics has contributed to the discussion about alternatives to copyright law as a stimulus to creating works of art. One central theme of cultural economics has been the study of artists' labour markets. Research on artists' earnings has shown that the rewards to artistic creativity are generally relatively low apart from the huge earnings of the few superstars. A feature common to all the creative industries, subsidised or commercial, is that they seek out outstandingly talented 'personalities', the high income superstars. Very talented and creative artists are, by definition and in contrast to the majority of artists trying to make a career, rare and in short supply. Consequently, great rewards fall to the chosen few. These disparities make the distribution of artists' earnings very uneven.

This research, however, is almost exclusively concentrated on earnings from fees, wages and sales of works of art and there is actually very little empirical evidence on artists' earnings from copyright; the little evidence there is, though, confirms what everyone knows anyway – that the superstars have high royalty earnings and the rest typically earn very little. In fact, the whole debate about the importance of copyright has always been conducted in an information vacuum as far as artists' rewards from it are concerned. Aggregate data on the contribution of the creative industries to the whole economy – the only empirical evidence that is bandied about – tells us nothing about the distribution of royalties and payments to artists.

Artists' incentive to creativity

Whatever the full picture, how relevant anyway are artists' earnings to the encouragement of creativity? Does creativity – whatever that means– respond to the stimulus of copyright-induced earnings? The copyright incentive is as likely to come from the recognition of the status of the artist and their moral rights as it is from the economic returns. This question requires an understanding of artistic motivation and its response to monetary reward, a topic that has been studied in cultural economics by Bruno Frey (1999). He has adapted the theory of intrinsic and extrinsic motivation and reward to hypothesise that inappropriate matching of the two would lead to 'crowding out', so that, for example, an artist who is driven by inner motivation is not only *not* stimulated to produce work by monetary reward, but she is so to speak insulted by it. Incentive and reward must conform. Copyright (and especially authors' rights) offers artists recognition of their status and protection of their moral rights that enable them to control the use of their work even after they have had to part with the economic rights. Control of the artist's reputation and of the integrity of their works is an incentive to create. Thus, copyright law satisfies both intrinsic and extrinsic motivation and reward with its combination of moral and economic rights.

All told then, the case for copyright as an economic incentive encouraging the creation of works of art by *artists* is not strong. On the other hand, if copyright is meant to strengthen the industry side of the creative industries, then copyright law serves it very well. With the WCT and the WPPT, copyright has broadened in scope and now includes the protection not just copyrights but also the means of protecting them from digital theft and it has been extended from 50 to 70 years for authors, to 50 years for performers and broadcasters, record labels etc in Europe and many other countries, and in the US to 95 years for company copyrights eg Disney Corporation. There is an irony here, though, for the topic of copyright and creativity: copyright protection is in fact a two edged sword. As Landes and Posner (1989) pointed out nearly 20 years ago in their seminal article on the economics of copyright, overly strong copyright inhibits creativity because it imposes higher costs on later generations of creators. Copyright law therefore has to find a balance between the incentive to create now and the access of later creators.

It has been argued that an unintended consequence of copyright is that it has facilitated the development of large multinational corporations in parts of the cultural sector of most countries by the creation and protection valuable, tradable assets. This has lead to artists' bargaining power being increasingly weakened with the growth of large firms that are strengthened by copyright law. Though there is mutual interest between author and publisher to produce successful works that earn them the greatest return, there is huge scope for friction between them within that general proviso, as Caves' book shows The royalty system of payment goes some way to secure a mutual interest because it ties author and publisher in to joint entrepreneurship and risk sharing. However, the share of revenue and of outlay is almost certain to be unequal and the contribution of one party rather than the other to the eventual success or failure of the product difficult to gauge.

The mirror image of the weaker bargaining power of authors is the stronger bargaining power of publishers. The private industries that make up the cultural sector have a typical oligopolistic structure, i.e. a few large firms dominate, there is little price competition and many small firms are tolerated as long as they only occupy niches in the market and do not contest the position of the dominant firms. The firms in these industries are multi-national and multi-product. Their growth has been assisted by the amalgamation of assets that are copyrights (playing much the same role as patents in manufacturing industries).

Risk is not symmetric between firms and artists because firms have far greater advantages in the marketplace. Artists cannot spread risks as firms can because they have a limited portfolio of their own copyright assets whereas a firm can spread risk over many artists' works. Artists' assets are often concentrated in human capital, which means they have little collateral to offer the capital market, by contrast to firms, which have capital assets as collateral. Artists make a considerable outlay of training, time and forgone income in developing unique works; they bear the burden of research and development in the arts. Firms can pick the lines they think will be successful without financing the R&D. If markets were competitive, artists would be compensated in the price paid for their work (whether royalty rate or spot price). One reason why markets are uncompetitive is because copyright law makes them so, strengthening, as I have argued (Towse, 2001; 2006), the position of firms (publishers) *vis á vis* artists (authors).

Conclusion

The current debate about copyright law, is whether it will work with digitalisation. This is a debate to which economists can make a valuable contribution: copyright is, after all, not only a matter of legal principle but also one of economic pragmatism.

Part of that pragmatism is measuring the economic contribution of the creative industries to the economy. But what these measures do not and cannot prove is the causal effect of copyright: it is one thing to define the creative industries as being based on copyrightable content and another to say that copyright is the cause if the growth of the creative industries and that without copyright or with weaker copyright, these industries would decline. The fact that most of the creative industries have grown up with copyright law in existence not only does not prove it was needed for their development but it also means that firms have not had to explore the full range of business models as they could rely on copyright. This has been characterised as a moral hazard problem, meaning that the intended incentive has led to unintended outcomes. Some economists (now and in the past) believe that its economic role is overrated and that copyright law errs on the side of over-protecting firms in the creative industries at the expense of authors and of consumers. The music industry is now beginning to look to new pricing strategies, for example, earning revenues from merchandising and concert tours rather than relying on sales revenues. Those are the kinds of strategies that economists, going back all the way to Adam Smith, have always looked to provide a market-based incentive for the encouragement of the creation and publication of new work. In economic terms, copyright is a delicate and ever-changing balance of costs and benefits and so are its effects on creativity and the incentives it offers to artists; this is the contribution of cultural economics to the debate.

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