

## **Terms of reference**

The assistant to the Chief Executive Officer of Aspirational Sounds have been asked to write a report that describes the current position of Tower Records and explains why the company ended up filing for bankruptcy. Based on this, recommendations for how Aspirational Sounds should adopt to the ongoing changes in the external environment will follow.

## **Procedure**

The report is fully based on secondary data, primarily found on the Internet and various databases. Analysis has been founded upon information from newspaper articles and market researches.

## **Findings**

These findings will analyse the music retailing industry and declare past events leading up to the current position of Tower Records.

### ***Minor analysis of the music retailing industry.***

#### **Generally**

The past few years the music, video and book markets have had different growth, music has been struggling, video sales have increased strongly and book sales have had a steady growth. These patterns of growth are believed to continue (Mintel, 2002). Further on the Mintel report (2002) states that although the music market has declined in Europe as a whole the UK market has actually grown, especially the sales of classical music (Classical sales up by one million, 2004), due to a strong consumer economy.

Today there is a revolutionary change in the external environment of the music retailing industry. This is due mostly to the developments in the world of information technology and the rapidly growing supermarket chains.

#### **Internet**

There exist three factors within the Internet, illegal downloading and file sharing, legal downloading and Internet retailing.

As the computers have become more sophisticated and the speed of Internet connections has increased, it has become easier to download music files from the Internet.

In Britain will 30 million songs be downloaded legally this year (2004) by 5million computer users (Taher, 2004)

The vast majority of downloaded music is illegal and creates no profit for either the record companies or the retailers. In Britain only 2 per cent of the total downloading (Burrell, 2004)

is coming from legal downloads.

In the US six retail record store chains has formed a joint venture called Echo that offers their costumers to download individual tracks to their computer for a fee (Gentile, 2003). The illegal downloading always means a waste of potential profits for the music retail industry. Eventhough it also means a loss for the record labels they might have a profit in the long run since many of these companies also sells the computer hardware which is used when downloading and burning music (MacDonald, 2003).

There is a risk in illegal downloading though, the risk of being sued .In the UK there will not be any lawsuits against private persons in the near future, but the threat is still there (Weber, 2004). In the US lawsuits has had a desired effect, since the percentage of Americans who download music online has decreased by 50 per cent (European Business ASAP, 2004).

According to Mintel (2002) the E-commerce music, video and book sales have had a rapid growth since the beginning of the late 1990s. These products are ideally suited for Internet sales since they are easy to transport and they offer the customer the opportunity of an online sample. Internet companies such as Amazon creates fierce competition for traditional retailers. The Mintel report (2002) believes that the small E-commerce companies will be forced out of business due to growing competition. They also believe that the winners in the long run will be the clicks and mortar retailers and the pure-play companies with established brand names.

The reasons for using the Internet to purchase or download music are well expressed by these quotations from American students: "If you can order it online, why leave the house, go to a store and waste your time?" "I don't want to waste \$15 to buy 19 songs when I only want one." (Tower records to close in June 2004).

## **Supermarkets**

Some believe that the discount prices set by the supermarkets poses an even greater threat to the record retailing than the Internet downloading does. In the UK companies such as Tesco, Sainsbury's Asda and Safeway have become important competitors in music retailing. Some major artists in the top 10-album chart have made more than half of their sales in supermarkets. (Burrell, 2004) Also chains such as Starbucks will enter the music market by offering to burn CDs with mixed music while you are drinking your coffee. (Starbucks 'to offer music to go', 2004).

## ***Tower Records***

### **The bankruptcy of Tower Records**

Tower Records was founded in 1960 in Sacramento California and was up until recently owned by the Salomon family. On February 9<sup>th</sup> 2004 Tower Records filed for Chapter 11 bankruptcy (Christman, 2004).

Their worries began in the 1990s when Tower Records made some poor strategically decisions when the era of illegal downloading was commencing (Kasler, 2004). Tower Records desperately tried to pay their debts by selling their Japanese stores and issuing new bonds. The interest payments and the fact that the bonds were due to payment in May 2005 added to the problems with competition from illegal downloading, online retailers and supermarkets was overwhelming for Tower Records. (Kasler, 2004)

Tower records and their largest bondholders figured out a plan that would leave 85 percent of the ownership to the bondholders and in exchange reduce their debts by \$80 million. To make this deal they had to have 100 percent support, but they did only get 97 percent. This forced them to go to bankruptcy court, which approved their proposition. (Kasler, 2004)

## **Current position of Tower Records**

Tower Records emerged from bankruptcy only 35 days after the filing (Tower Records back from...2004), one of the fastest comebacks ever very much because of their valuable name and reputation (Kasler, 2004).

In 2003 Tower Records sold all their UK stores and is now in possession of 93 stores worldwide. During their bankruptcy there has been no change for their staff or customers, since all 93 stores has been open and salaries has been paid as usual (Tower Records declares...2004).

Regarding the ownership, Tower Records has converted a debt of \$110 million to an 85 percent equity stake for the bondholders, and they have issued new notes worth \$30 million. This leaves their former owners, the Salomon family, with a 15 percent ownership interest. Further on they have been given a new credit availability, which uses cash from the daily trade as collateral. (Christman, 2004)

Eventhough Tower Records has had losses during the last five years their cashflow is now positive. This might be an incentive for the shareholders not to sell the company which has been up for sale since May 2003 (Will Tower Records rise...2004).

## Conclusion

The Internet and the supermarket chains have created a new threat in the external environment of the music retailing business. Despite this there has actually been a growth in the market for music videos and books in the UK.

One possibility to enhance the quote of legal downloading might be to strengthen the legal actions.

In the future it will be important for the retailers to enter the state of clicks and mortar in order to compete with the supermarkets.

Furtheron, Tower Records failed because of the changes in their external environment and because of large debts created by poor investments and high interest payments of issued bonds.

They recovered fast mostly due to a good reputation, a positive cashflow and the fact that it was family owned which enabled them to sell a large part of the company in order to cover their debts.

## Recommendations

1. Embrace the technical revolution and become a clicks and mortar company, which offers both sales of the Internet and enables downloading of individual songs against a fee.
2. Create in-store kiosks where customers can burn CDs with their own selection of songs.
3. Focus on making it an experience to shop at Aspirational Sounds, by offering good and comfortable listening areas with couches and high standard cafés.
4. Aspirational Sounds should strive to have the best selection of independent- and classical music.
5. Aspirational Sounds have to assure itself of a sufficient profit in the UK, since it is one of the few growing markets, before expanding into new markets.

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