

## CHAPTER 3

### MODEL A:

### THE CURRENT LOCAL SUPPLY CHAIN

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### **3 MODEL A: THE CURRENT LOCAL SUPPLY CHAIN**

#### **3.1 Introduction**

This thesis concentrates on the conditions in the local South African market, as well as the production, selling and distribution of local South African music. The management of the local supply chain and the way in which it is *currently* operating in South Africa, is referred to as MODEL A, which is discussed here in Chapter 3. An alternative outsourced supply chain management model is researched and evaluated as the hypothesis statement in Chapter 5 and is referred to as MODEL B. The new outsourced supply chain management model is documented and explained under the conclusions and recommendations in Chapter 6 (MODEL C).

As a background study, six main processes (logistical processes and others) which are currently performed by a record company, but which do not necessarily form part of its set of core competencies, are discussed below (refer to points 3.2 to 3.7). These six processes are discussed throughout the thesis and in all three models (MODELS A, B and C) and are:

- The manufacturing process
- Warehousing and distribution
- Selling
- Marketing
- Debt collection
- Management of receivables

#### **3.2 The manufacturing process**

##### **3.2.1 Just-In-Time manufacturing**

In the competitive recording industry, the record company must first determine the existence of a probable expected consumer demand, before issuing an order to have

stock manufactured. Fortunately, it is possible for record companies to influence this expected demand through extensive marketing and visual advertising campaigns. The tastes of music listeners (the consumer or end-user) are very varied and change constantly. A title that might be selling thousands of units in one month may have nearly no sales in the following month. This is the main reason why record companies cannot afford to manufacture stock that might not sell – no company can afford to have their capital tied-up in un-sellable or obsolete stock.

#### 3.2.1.1 Just-In-Time principles

Just-In-Time (JIT) is a manufacturing concept of meticulously planned logistics and distribution operations, which helps to reduce stock, lead times and therefore, costs. Especially in the last two decades of the previous century, JIT as a business principle was widely researched and evaluated by various international authors (Bicheno 1991: 1 – 5; Fawcett, McLeish & Ogden 1992: 82 – 84; Cheng 1996: 1 - 10). With the pressures of increased competition, accompanied by the possible expected lowering of product costs and selling prices, it is crucial that materials, components and end-items are at exactly the right place at exactly the right time.

JIT creates a pull mechanism in the supply systems, whereby goods are drawn through the chain by a demand (or an expected demand) for products, rather than being pushed through to form work-in-progress or safety stock. The main prerequisites for its implementation are short, dependable lead times and high levels of quality (Johnson & Wood 1996: 69 – 73, 173, 327 – 328; Hugo & Van Rooyen 1997: 58 – 61). These ingredients reduce the need for stockholding for reasons of unpredictable demand, interrupted or delayed supply and poor quality. Fortunately, both the two pre-requisites mentioned above (*i.e.* short dependable lead times and high levels of quality) are present with the manufacture of a compact disc (CD). The two major South African CD manufacturers are discussed later in this chapter.

### 3.2.1.2 Information technology

Information technology (IT) systems which entrench JIT manufacturing disciplines in their management information systems (MIS), will help all South African industries weather the onslaughts of a slow or unpredictable economy, low customer spending and cheaper imports. At the same time, IT will also help to open doors globally - mainly through improved communication between different companies operating in different industries in different countries around the world. According to Clague (2000: 1 – 2) industries need to operate smarter and leaner, and must be flexible to meet customer demands - this can only happen with the support of IT systems that have been developed to meet all customer requirements (refer to the discussion on the customisable MIS developed by SAP in point 3.2.2 below).

When IT is implemented to facilitate the JIT operation, the whole communication chain has to become far more dynamic and reliable. Some players in the recording market have burnt their fingers because they tried to adapt generalised manufacturing systems to their needs, rather than opting for a specialised system. The key concerns are manufacturing and delivering on-time to their customers' specifications (*i.e.* meeting the trade's demands) with tightly defined cost criteria.

### 3.2.1.3 Customer service

One of the main causes of loss to a record company is late delivery into the trade (*i.e.* to the record company's customer), since goods are then returned or sometimes not even received. A classic local example is the music wholesaler *Reliable Music* in Johannesburg (as discussed in Chapter 2 under point 2.6.1). In a personal interview with the Managing Director and sole buyer at *Reliable*, he explained that his store only accepts deliveries that are delivered within 48 hours of placing his order. No late deliveries are accepted and the record company will have to cancel the order and lose the sale if they do not deliver before the deadline. It is thus imperative that goods be received and despatched on time – Clague (2000: 1 – 2) believes that this can only be

achieved if management at all levels in the company have accurate information on which to base their dynamic just-in-time decisions.

It is important to note that JIT cannot be applied to every single title being produced, particularly where the demand is seasonal (*e.g.* certain seasonal gospel albums which sell only in April during Easter, or in December at Christmas time). It is however still used in many areas of procuring or purchasing raw materials or components, as well as in general inventory management and distribution.

The basic principle of JIT is to have goods delivered exactly where and when required, literally just in time to make the next move along the supply chain, which is usually the distribution process into the market - this can only be achieved by detailed forward planning and extensive use of information systems. It is not merely a particular method of distribution, but a total logistics concept that, if conscientiously implemented throughout a supply chain, means drastically reduced inventory and costs as well as an improvement in levels of service. All record companies need to recognise that JIT is an extremely useful business technique, and should use it accordingly, in order to improve their value-added service offering to their clients.

### 3.2.2 Management Information Systems

It is imperative that every business operating in a supply chain uses IT to employ a customised management information system (MIS) to manage its entire business operation (Lynch 2000: 15 – 16). Such a software program will control all processes in its chain, from procurement right through to sales, distribution and debt collection.

Founded in 1972, *SAP* is the recognised leader in providing collaborative business solutions for all types of industries and for every market in the world. Headquartered in Walldorf (Germany), *SAP* is the world's largest inter-enterprise software company. *SAP* employs about 30 000 people in more than 50 countries ([www.sap.com/company](http://www.sap.com/company)), including South Africa.

‘mySAP Business Suite’ is a comprehensive business solution developed by *SAP* for today’s business economy. Its main function and advantage is that it allows employees, customers and business partners to work together successfully. ‘mySAP Business Suite’ is open and flexible, supporting databases, applications, operating systems and hardware from almost every major vendor. By deploying this technology, services and development resources, a business can have access to valuable information resources on which to base its JIT, forecasting, benchmarking and other management decisions. The program will also help to improve supply chain efficiencies (from procurement right through to delivery and debt collection) - this will in turn build stronger customer relationships and improve customer service.

### 3.2.3 Compact disc manufacturing

The first step in the processes of physical supply chain management is the manufacturing of stock. Of the various music formats currently being sold by South African record companies, the well-known CD (compact disc) is the most commonly used and sold music format at the moment - refer to its introduction into the market in 1982 by the *Sony* record company (as documented in detail in Chapter 2).

#### 3.2.3.1 Principles of CD manufacturing

Most local and global CD manufacturers around the world adhere to the same general set of uniform standards. *Sonopress SA*, one of the biggest CD manufacturers in South Africa, has listed the following four important principles on its company website ([www.sonopress.co.za](http://www.sonopress.co.za)):

(a) Lead-time

Under normal circumstances, a CD manufacturer usually quotes a ten working-day lead-time for all new orders placed (where glass mastering is required), and five working days for a repeat order. Refer to the *Sonopress* price list in Annexure E where the glass mastering process is described. This standard time

frame is calculated from the receipt of all necessary components, which generally include the following:

- The input medium *i.e.* the master CD (which was produced in a recording studio) and which is to be replicated
- The silkscreen label print positives for the printing on the CD itself
- The chromalin for colour-proofing the printing
- The printed packaging *i.e.* the front booklet and back inlay which are to be inserted into the CD jewelcase (the plastic casing)
- An official order with a PO (purchase order) number
- All the necessary copyright clearances, licences or agreements
- The *Ad Valorem* disclaimer (refer to the explanation on the *Ad Valorem* duty in point 3.7.1 below)
- A 50% deposit (this up-front payment is usually only required with new orders from new and unknown clients)

(b) Quantity variances

The final invoiced quantity may vary up to five percent from the client's original order quantity. This allows for process set-up, as well as for any rejects and manufacturing variances that may occur during the automated processes used to replicate discs.

(c) Printing

The disc label is printed using a complex and automated silkscreen print process. It is important that the client provide positives that conform exactly to the CD manufacturer's specifications.

(d) Packaging

Printed paper components for packaging usually consists of a booklet that is placed in the front of the jewelcase (the plastic casing), and an inlay in the back, under the tray. As the packaging process is automated, it is once again essential that these components conform to the manufacturer's specifications. If not,

manual packing will be performed and an extra charge will be levied to cover the additional labour costs (refer to the *Sonopress* price list in Annexure E).

There are currently two major local CD manufacturers in South Africa, being *CDT* (Compact Disc Technologies) and *Sonopress SA*.

### 3.2.3.2 Compact Disc Technologies

*Compact Disc Technologies (CDT)* has been operational since February 14, 1991 and the company was created by a joint venture between two record companies: *EMI* and *Tusk Music*, to fulfil their demand for local manufacture in South Africa. *CDT* has a manufacturing plant and warehouse in Midrand (Gauteng) and their current annual output is approximately 15 million CD's, although they have an annual capacity of more than 30 million CD's.

According to the Marketing Manager of the major South African CD replicator *CDT*, (electronic mail received August 2003), their biggest local order run for a single music title was for the Elton John single CD '*Candle in the Wind*', the tribute album to the late Princess Diana. The total amount manufactured in South Africa was 340 000 units, with millions more sold worldwide.

### 3.2.3.3 Sonopress SA

The other major CD replicator, *Sonopress SA*, operates out of a factory in Kya Sands, Randburg, near Johannesburg (Gauteng). *Bertelsmann AG* (who also owns the *BMG* record company discussed in Chapter 2) demonstrated its confidence in the future of South Africa by investing in this new, state-of-the-art compact disc replication facility. Investment in the South African facility was approximately R40 million, and *Sonopress SA* has an initial capacity of more than ten million CD's per annum. However, the building is designed to accommodate process expansion to a future capacity of thirty five million CD's per annum ([www.sonopress.co.za](http://www.sonopress.co.za)).

The manufacture of a CD is a very complex and intricate process. The record company must first create a CD master in its recording studios and this master will be delivered to the CD manufacturer, together with an order for a specific number of units to be manufactured. The CD master then undergoes a series of highly technological processes where after literally hundreds of thousands of the same unit can be replicated. Refer to Annexure E at the end of the thesis for a comprehensive *Sonopress* audio CD price list. The CD inlays or booklets must also be delivered with the original master CD, and they will be inserted into the jewelcase (the plastic casing), either by machine or by hand (depending on the nature of the printed inlay / booklet and any specific customer requirements – refer to the price list). These CD inlays or booklets are manufactured by independent printing companies such as *Artone* in Johannesburg, or *Creda Press* in Cape Town.

Lastly, the jewelcase is sealed with a plastic overwrap (also called ‘shrinkwrapping’), and any additional stickers (usually for marketing purposes) are placed on manually by employees working on a physical assembly line, where after they pack the CD jewelcases in standardised carton shipping boxes (also referred to as ‘shippers’).

### **3.3 Warehousing and distribution**

#### **3.3.1 Receiving**

After the CD’s have been manufactured (more correct terminology would be ‘replicated’, ‘duplicated’ or ‘copied’), the finished product is delivered back to the agreed delivery address, *i.e.* either to the record company’s allocated premises, or straight back to the individual artist who had his own master CD manufactured. For the purposes of this explanation, we will accept that the order was placed by a record company and not by an individual artist.

The goods are generally stored in secure warehouses from where they will be delivered directly into the trade. Usually no additional work needs to be performed on the received product. For the best functionality and capabilities, these warehouses should be

operated and managed by means of the complex technological management information systems (MIS) which were discussed earlier, which can track and trace individual units from their arrival into the warehouse, up to their delivery to a re-seller in the trade.

### 3.3.2 Picking

The trade (music dealers, retailers and others) fax, phone or e-mail their orders through to the record companies' data capturers. When the order processors enter these orders into the MIS, the stock is made available on the system and it can be drawn for the specific order.

Warehouses are divided into bins, with different titles consigned to different bins. When an order is entered, the MIS will automatically print a *picking ticket* in the warehouse, informing the pickers of the title and quantity to be picked, as well as in which bin in the warehouse those specific units are stored.

### 3.3.3 Physical distribution

Packers then make up the 'parcel' that is to be delivered to the dealer who placed the order. These packages are generally accompanied by a delivery note (a proof of delivery note or POD), as well as by an invoice. The POD must be signed by the dealer's receiving personnel and must be returned to the record company's warehouse as proof of delivery and its receipt of the ordered goods.

Most retailers follow a central buying philosophy (*i.e.* all orders are generated, sent and then managed from their head-office). The ordered goods are then delivered to the head-office or to the receiving and distribution depot.

Some retailers however, like the South African company *CNA*, expect their orders generated at head-office to be delivered to each individual store – which means about 150 separate deliveries to the individual *CNA* outlets nationwide. Often only a very

small amount of units are ordered for small outlying towns with small populations and little buying-power – these deliveries are clearly very costly to the record company.

Other local retailers have set-up their own distribution depots situated throughout the country. *Musica* has three of these depots, strategically situated in Midrand (Gauteng), Cape Town (Western Cape) and Durban (KwaZulu-Natal). Orders for the three regions are also generated at head-office, but the record company only needs to deliver three bulk orders to the three centres – *Musica* itself will split the goods received and deliver it to their individual nation-wide stores.

### 3.4 Marketing

Around the world, the marketing of music artists and their titles have become a very specialised and very costly necessity. Even locally, record companies spend millions of rands each year to produce and pay for TV-, radio- and press advertisements. Intense competition in the market implies that marketers need to use both the ‘push’ and the ‘pull’ mechanisms to achieve the greatest demand for their product:

#### (a) Market push

Marketers ‘push’ the title into the trade by incentivising the product, offering invoice discounts and other special deals to the trade. This is called ‘below-the-line marketing’, because its costs do not get added up-front to the initial cost of the production of the album (refer to the split in the cost break-down in Table 3.1 on page 75). Examples of these are:

- ‘Buy ten units and get one unit free’ is the most widely used incentive to push more titles into the store. Record companies want to make sure that the racks of the dealers are filled with their product, so there can be greater visibility for their titles
- In-store appearances or signing sessions by the artist in the store, which also creates visibility and familiarity for the artist and the release

(b) Market pull

Marketers simultaneously strive to achieve a ‘pull’ effect from the market, *i.e.* create a demand or a call for a specific title. This ‘above-the-line marketing’ is included in the initial cost calculations and is achieved by targeting the market (the end-consumer) directly through the above-mentioned TV and other advertising campaigns.

### 3.5 Selling

#### 3.5.1 Sales executives

The five major record companies all have dedicated, specialised and incentive-driven selling teams. These sales representatives usually earn a small basic salary and earn the bulk of their income from commission, an amount paid based on the number of units sold over a specific period of time. They have a very specialised knowledge of the music they sell. Record companies allocate their sales representatives in one of two ways:

- Purely by area, which means that the specific sales person must sell all genres of music to his / her allocated area, for example the Witwatersrand area, or the Western Cape area
- By area *and* by genre, meaning that the sales person only sells a specific *type* of music in his / her allocated area, for example only rap, hip-hop, jazz and blues into the KwaZulu-Natal area. If the record company has the necessary resources and manpower available, this more specialised approach is generally preferred

#### 3.5.2 Music For Pleasure

Years ago, every major record company had a small internal division dedicated to the budget reissue of its own back catalogue (*i.e.* the marketing and selling of their old titles that are in a declining product life cycle phase). *Music For Pleasure (MFP)* saw an opportunity in the international market and got involved with the worldwide selling of the *EMI* back catalogue ([www.vinylvulture.co.uk](http://www.vinylvulture.co.uk)). At its inception in 1965, the ‘*Music*

*For Pleasure Record Club* operated out of Middlesex (United Kingdom), formed as a joint venture with the massive *Hamlyn Publishing House*. The company caused a mighty media stir by simultaneously releasing 78 different long play records with the bargain price tag of 12s. 6d. (twelve shillings and six pennies). In those days, the price for a new vinyl record was 32s.

In the early days, things didn't always run very smoothly with the new joint venture (JV) - for example neither *EMI* nor *Hamlyn* shouldered the responsibilities for royalty payments, because each company thought that the other one was handling and managing this responsibility. Despite all their problems, many records still made it out to the shops and *MFP* did very well as a so-called 'loss leader'. Around 1973, a parallel series of *MFP* releases mysteriously appeared under another label, the '*Sounds Superb*' banner, which resulted in *Hamlyn* pulling out of the JV deal.

Around the turn of the 1980's, *MFP* started to struggle financially, mainly because of rationalisation and mergers occurring throughout the major record companies. It was also felt that the Majors nearly destroyed their own industry in their efforts to generate cash to pour into the development of compact disc technology (refer to the discussion on the inception of the compact disc in Chapter 2). *MFP* then turned into little more than a distribution network, albeit one that spanned the globe.

Nowadays, the only evidence of *MFP* is to be found in South Africa, where it is a merchandiser of all music formats for the modern audio / video age. *MFP*'s function is to be a 'middle-man' between the record companies and the major South African retailers, e.g. *Pick 'n Pay*, *Makro*, *Game* and *Dion*. *MFP* buys product from the record companies, and then sells it on to the retailers. Its main value-added service offering is that it also merchandises the stock, i.e. it physically packs the stock onto the store racks, organises in-store marketing as well as advertisements in press and on television and radio. It performs in-store stock-takes and manages the re-ordering process.

In 1999, *MFP* was bought-out by the major record company *Gallo* (refer to the detailed discussion on *Gallo* in Chapter 2, point 2.5.2.1).

### 3.6 Debt collection

The collection of debt is discussed below, because it is another crucial process that currently needs to be managed and executed by a record company, even though it is not one of its core competencies.

After the record company receives an order from a wholesaler, dealer or retailer, various order details are checked and verified if necessary:

- (a) The financial status of the outlet that placed the order (*i.e.* payment terms, credit worthiness, outstanding amounts still overdue and other important financial aspects).
- (b) The correctness of the order, for example the verification of the completeness and correctness of the delivery address, the part-numbers of the titles ordered and any other relevant order details.
- (c) Verifying and checking for the correctness of the PO (purchase order) number.
- (d) Checking for stock availability on the MIS (management information system), of the particular titles requested in the order.

If there is no stock of that particular title on hand, the order goes onto back-order and more stock will have to be manufactured before the order can be executed. If the necessary stock is however available to fulfil the order, goods are picked and despatched from the warehouse, along with a delivery note or a POD (proof of delivery) and an invoice. The recipient of the goods signs the POD and keeps a copy for himself, along with the invoice.

It is then up to the record company's financial department, more particularly the debtors clerks, to collect the monies due.

### 3.7 Management of receivables

The money received from the sale of a single unit, has to be divided into many receiving channels. For one unit sold by a record company, a simple example of the split is illustrated in table 3.1 below. In this example, when manufacturing a thousand CD units and then selling them to a dealer at a PPD of R50.00 per unit, the cost and revenue breakdown can be explained as follows (refer to the table below):

- The total costs incurred by the record company (including manufacturing, marketing, sales, distribution, duties and royalties) are +/- R35.71 per unit, *i.e.* the total order cost is R35 710.00
- The balance of R14.29 (R50.00 sales price less the R35.71 cost price) is the record company's profit. If all 1 000 units are sold, the record company will thus make a profit of R14 290.00 on this released title

**Table 3.1** Breakdown of the unit selling price of an average music CD

	TYPE OF COST	TOTAL COST	UNIT COST	PERCENTAGE OF COST
Glass mastering and testing	Manufacturing cost	R1 550.00	R1.55	3.505% of PPD
CD replication and CD label printing	Manufacturing cost	R3 790.00	R3.79	8.571% of PPD
Additional 2 colour print on the label	Manufacturing cost	R300.00	R0.30	0.678% of PPD
<i>Ad Valorem</i> duty	Manufacturing duty	R454.02	R0.45	1.018% of the manufacturing cost
Mechanical royalties	Royalty payment to governing body	R5 620.00	R5.62	6.250% of the retail selling price
Warehousing and delivery costs	Fulfilment fee	R500.00	R5.00	10.000% of PPD
Sales commission	Fulfilment fee	R500.00	R5.00	10.000% of PPD
Marketing	Marketing expense	R10 000.00	R10.00	20.000% of PPD
Artist royalty	Royalty payment to the performing artist	R4 000.00	R4.00	8.000% of PPD
<b>TOTAL COST</b>		<b>R35 710.00</b>	<b>R35.71</b>	

**Source:** Own research.

*Note:* In the example above, 1 000 units with a two-colour silkscreen print on the CD label were manufactured at *Sonopress SA* (refer to the generic Sonopress price list in Annexure E at the end of the thesis).

### 3.7.1 Ad Valorem duty

An *Ad Valorem* excise duty is levied on all audio components (CD's, cassette tapes, video's or DVD's), as well as on CD-Roms containing music, games or video clips. Copyright clearances for these audio components must be obtained from SARRAL and NORM (South African recording industry governing bodies described in Chapter 2). A copy of this clearance must in all cases be submitted to the CD manufacturer (*e.g.* *Sonopress* or *CDT*) when an order to manufacture is placed.

The *Ad Valorem* duty is payable to SARS (South African Revenue Service), and is payable whenever one of the above-mentioned music components are manufactured. This duty is calculated and payable on the manufacturing cost of the item, and not on the value or sales price of the component or the end-item.

*Ad Valorem* is payable exactly on the 25th day of the month, but only every three months for goods manufactured in the previous three month period, *i.e.:*

- January to March duties are payable in April
- April to June duties are payable in July
- July to September duties are payable in October
- October to December duties are payable in the following January

The *Ad Valorem* amount payable is calculated as follows:

1. Add the total amount of invoices made out to the principle over the applicable three month period (excluding VAT)
2. Add fifteen percent (15%) to this total - this amount equals **x**

3.  $x$  is multiplied by 0.07 and then equals  $xy$
4.  $xy$  is the *Ad Valorem* amount payable to SARS

Below is an example of a fictitious *Ad Valorem* calculation:

Manufacturing invoices for the three month period (excluding VAT):

January 2003:	R190 000.00
February 2003:	R240 000.00
March 2003:	<u>R320 000.00</u>
TOTAL:	<u>R750 000.00</u>

$$R750\,000.00 + 15\% = R862\,500.00 (x)$$

$$R862\,500.00 \times 0.07 = R60\,375.00 (xy)$$

This means that a manufacturer (the record company or artist that placed the order) must pay R60 375.00 to the South African Revenue Service (SARS) as a duty or tax for audio components manufactured with a manufacturing cost of R750 000.00.

### 3.8 Piracy

Piracy is a problem that affects every sector of the music industry, especially in Africa and other Third World countries where it is not properly monitored and offenders are not properly prosecuted. Record companies, artists, composers, publishers, distributors and retailers all lose out when customers buy a pirate / counterfeit copy rather than a legitimate recording.

The occurrence of piracy is discussed because it is a major problem in world wide recording markets. Especially traditional record companies (as in MODEL A), that replicate their own stock and manage their own inventory, often do not have the necessary resources to fight this external threat. In the proposed outsourced model

(MODEL C), even though the third party supply chain management company will probably not be able eliminate piracy completely, the fact that it is responsible for the manufacture and management of all inventory and because it has more resources available, leads to the conclusion that it will be better equipped to control the unlawful manufacture and distribution of copyrighted merchandise.

### 3.8.1 Piracy definitions

Piracy is a term used to describe all varieties of unauthorised recording and can be broken down into the following five main categories:

(a) Simple Piracy

Simple piracy is the unauthorised duplication of an original recording for commercial gain without the consent of the rights owner. The packaging of the pirate copy is different from the original, and often of inferior quality. Pirate copies in this category are usually much cheaper than the original.

(b) Counterfeits

These are items that are copied and packed to resemble the original as closely as possible. The original producer's trademarks and logos are reproduced in order to mislead the consumer into believing that they are buying an original product.

(c) Bootlegs

This term describes the unauthorised recording of a live broadcast performance. The recording is then duplicated and sold without the permission of the composer, artist or record company.

(d) Internet Piracy

This type of piracy most typically takes the form of music being compressed and posted and transmitted globally via the Internet, without the authorisation of, or payment of any royalties to, those who invested in the creation of the recording.

(e) MP3 Piracy

MP3 is a format used for compressing audio files. MP3 files are generated as follows: a computer user inserts a standard music CD into the CD Rom drive of a computer. It then runs an MP3 software programme that will ‘rip’ the audio signals in the tracks on the standard CD and compress them into MP3 files. These files are stored on the computer’s hard drive and can then be copied onto CD-R discs. The difference between the original standard CD and the CD-R is that the CD-R will carry many more recordings because the music has been compressed. An MP3 compilation CD-R could carry more than 150 tracks – which is equal to around eleven normal music albums.

The Recording Industry of South Africa (RISA) claims that the sale of unauthorised copies of copyright works in the MP3 format is without doubt a criminal offence, and not a ‘grey area’ as some users would like to think ([www.risa.org.za/piracy](http://www.risa.org.za/piracy)). Just because a consumer owns the CD doesn’t mean he also ‘owns’ the music. It is not allowed to put music on the Internet without permission of the copyright owners of the copyright in the sound recording and in the musical composition. It is a breach if sound recordings are uploaded or downloaded without permission of the copyright owners. Consumers should assume other people’s works are protected by copyright and can’t be copied or played over the Internet.

### 3.8.2 The effects of piracy

These are the four main effects related to the manufacture and sale of pirate music. Each of the four major players operating in the recording industry are negatively affected by the piracy of music:

(a) The artist

Firstly, the artist receives no royalty payments from pirated copies sold. When an artist does not also perform at concerts, on tours or at other public appearances, the income he or she receives as a royalty from the album sales is his or her only source of income.

(b) The record company

The record companies receive no return on its investments. It has invested money in the manufacture, marketing, sale and distribution of an artist's album, but will receive no money in return if the titles sold in the market are pirate copies. It will have lower sales figures and this all-together lower turnover may eventually even lead to staff retrenchments.

(c) The market

Dealers and retailers will not be able to compete with the low prices offered by the pirate merchants, even though they are often selling an inferior product.

(d) Consumers

Lastly, consumers will be buying copies of inferior quality. If tracks are missing or the sound quality is poor, the buyer will not be able to make any exchanges or receive any refunds. The consumer may even be contributing to organised crime syndicates that are heavily involved in international music piracy.

### 3.8.3 The Counterfeit Goods Act

The Counterfeit Goods Act (CGA) is now being utilised to fight piracy in South Africa. Members of the South Africa Police Service (SAPS), the Department of Trade and Industry (DTI) and Custom Officials are all empowered to seize counterfeit copies in terms of this law. Counterfeits include CDs, cassettes, MP3 and CD-R copies. The penalties when caught for piracy are very steep ([www.risa.org.za/piracy](http://www.risa.org.za/piracy)):

1st Offence: Maximum fine of R5 000.00 or three years imprisonment or both for each counterfeit copy.

2nd Offence: Maximum fine of R10 000.00 or five years imprisonment or both for each counterfeit copy.

### 3.9 Summary

In Chapter 2 the major players operating in the local record industry were discussed. In Chapter 3 the classic way in which the entertainment industry processes are currently managed in South Africa (MODEL A), were researched and documented. In short, it can be summarised as follows: a record company will contract an artist or a band and will record an album in its recording studios. The record company will then have a certain amount of CD's, tapes, video's and / or DVD's manufactured of this recorded master CD. The record company will then warehouse, market, sell and distribute this title. After invoicing, debt will be collected and the received monies will be managed and allocated in the correct ways. Throughout this thesis, this supply chain management process is referred to as MODEL A.

As can be seen from this short summary, record companies have generally kept most or all logistical functions in-house, managing processes that are not at all part of their core competency - which is purely the recording and publishing of music. In Chapter 4, two processes related to logistical management, being outsourcing and integrated supply chain management, are researched and documented. The research methodology in Chapter 5 serves to design and describe the hypothesis statement researched as MODEL B. MODEL C then describes the new tested model derived from the hypothesis statement, and documents the research methodology applied to the development of the new streamlined and outsourced supply chain model.