Contrary to popular belief, the 20th century did not end at the same time for everyone.

For those in the music business, it sputtered to a halt with the close of 1999 – the year recorded-music sales in the United States reached their all-time high of $14 billion; by 2012, sales had dropped to half that. For newspapers, the end of the century arrived a year later, when U.S. ad revenues hit nearly $49 billion; now they’re down to a mere $22 billion. Hollywood was able to stave off the century’s demise until 2002, when box-office admissions in the United States and Canada peaked at 1.6 billion; last year they were down 15 percent from that (which is not bad, considering).

Magazines, for their part, seemed to lead a charmed life – through 2006, anyway, when ad pages topped out at 253,000; since then, they have dropped by a third. As for television, the major broadcast networks have been on a slow, inexorable slide into the future for decades. In 1980, according to Nielsen, well over half the TV sets in America were tuned to ABC, NBC or CBS during prime time. By 2012, even with the addition of the Fox network, the portion tuned to a broadcast network was below one quarter.

As the industrial age gives way to the digital, we are rapidly moving from a period of mass production, mass consumption and (at its height in the 1950s) mass conformity to an era of networked production, unbundled consumption and personalization of just about everything. Yet in the media industries in particular, this transition is even now the subject of widespread confusion and denial. In their determination to stave off the demise of long-profitable 20th-century business models, media companies of every stripe have largely behaved as if they were sheltered from Joseph Schumpeter’s “perennial gale of creative destruction.”

The next industry to be ushered headlong into the 21st century will most likely be cable TV. Major companies, including Comcast and Time Warner Cable, continue to shrug off the threat of cord-cutting – subscribers dumping their expensive pay-TV packages in favor of streaming Internet services like Netflix and Amazon Instant.
True, the numbers don’t look terribly threatening at the moment; after years of talk and speculation, only 5 percent of U.S. households have made the move. Just this past spring, Nielsen played down the phenomenon, calling it one of several “interesting consumer behaviors that we want to keep an eye on.”

No cause for alarm, apparently. But just a few weeks later, Nielsen reported that for the first time ever, cable companies lost more subscribers than they gained, recording a net decline of 80,000 for the year ending in March. “Cord-cutting used to be an urban myth,” a cable industry analyst wrote in August. “It isn’t any more.”

Schumpeter’s insights were overshadowed in their time (the 1930s and ’40s) by the paramount specters of depression, totalitarianism and war. Today, his analysis of the role played by innovation and entrepreneurship in sweeping away the past seems prescient. Yet as the cord-cutting example suggests, technology itself is only one source of Schumpeter’s gale. An even more powerful factor is audience behavior, which is influenced, but hardly determined, by the available technology – and which in turn has a bearing on a welter of other variables, from means of distribution to modes of storytelling.

It’s not enough to keep up with technological change – though that in itself can seem overwhelming. Media companies need to evaluate their business strategies against a complex interplay of technological innovation, audience expectations and behavior, evolving entertainment forms and long-term cultural trends. The problem is that in the midst of the storm, many of these companies have become too insular to comprehend the forces of destruction they are prey to – much less know how to respond.

A REVOLUTION IN EXPECTATIONS

Let’s start with long-term cultural trends since, of all the forces at work, these are the most fundamental. Societies tend to resemble the technologies that define them. Industrial societies typically organize themselves one way, postindustrial digital societies quite another. Industrial production depends on large numbers of people taking orders from the top as they engage in repetitive tasks that yield only a small portion of the whole. Nearly everyone is a cog in the machine. Industrial-age companies – including newspaper publishers, movie studios and television networks – tend to operate accordingly, on a command-and-control model that relies on hierarchical thinking and strict categorization. Not for nothing was Hollywood once dubbed “the dream factory.”

Lines are drawn between author and audience, entertainment and advertising (or “church” and “state,” in the case of journalism), fiction and reality. Sometimes these distinctions are less than sacrosanct: we’ve had product placements in movies and TV shows for decades – but let one be too obvious and it will immediately be castigated as “blatant,” even in the ad industry trade press.

Digital societies are more fluid, with networked structures and a sense-and-respond mentality. In terms of organization, effective digital-age companies (for example, Apple) tend to resemble the Internet – decentralized and interconnected – while their less successful brethren (like Microsoft and Sony) remain hierarchical and disjointed. Control still exists at the successful companies, of course, but it’s not exercised through layers of middle
Individual product lines are not set up as profit centers—an organizational gambit that destroys any incentive for internal cooperation. What once were hard classifications tend to blur to the point that what seems natural, even sacred, to those on one side of the divide can appear all but incomprehensible to the other.

The United States is not at this point a digital society, but it's fast getting there. Last winter I designed a survey with the ad agency JWT to get at people's behavior and attitudes regarding the digital realm versus the physical. Unsurprisingly, the divide fell largely along generational lines: based on their shopping, reading and listening habits, “millennials” (people 18 to 34) were considerably more likely than older groups to be what we called “hard-core digital.” Yet, among those we surveyed, only 7 percent of the millennials and 4 percent of those in Generation X (35 to 48) fell into this category. Another 45 percent of both age groups were what we’d call “on their way” to digital. This means that even among millennials and Gen Xers, roughly half were merely dabbling with digital or were firmly anchored in the past. Among boomers (those 49 to 67) and silents (68 and older), that percentage was far higher.

Just as the future has been arriving unevenly among industries, then, it's arriving unevenly among populations—even populations in the same age cohort. Nonetheless, people's behaviors do fall into clear patterns. Even the least digitally inclined now use the Internet to research products they're interested in buying; many of them also use it for playing games and paying bills. Those dabbling with digital do these things and more: they chat and send e-mail; they share photographs; some buy books and music online; some even go there to get the news.

As we move up the digital adoption curve, these behaviors become ubiquitous and new ones come into play: listening to music, shopping for gifts—until finally, we reach the hard-core crowd and find large numbers of people reading e-books and tuning in to streaming music services like Spotify. Yet even among this group, only about two-thirds go online to watch TV shows—which explains why cable providers have been so slow to see cord-cutting as a threat. If past behavior is any guide, however, it could become a threat fairly soon.

With behaviors come expectations. Once people start to question their $100-plus monthly cable bills and realize that most of it goes for bundles of channels they don’t want, it’s all over.

The Schumpeterian gale carries many threats for established media businesses. Among them: constantly evolving technologies, any one of which could prove a dead end; a superabundance of ad inventory, which in turns leads to price collapses; the growing
realization by advertisers that they can create their own media and buy less of it from existing publishers. And yet the revolution in expectations may present the greatest danger of all.

As people change their behavior, adopting technologies they like and rejecting others, they develop new habits and wants. But since the transition to digital occurs in fits and starts, and invariably more slowly than its cheerleaders anticipate, media executives long found it easy to lull themselves into a false sense of security. To an industrial-age mindset, online behavior patterns seem all but inexplicable, anyway. Denial seems plausible, even prudent. In fact, it is neither.

THE SHIFTING AUDIENCE

Over the past few years, as more and more people have become comfortable with smartphones, tablets and services that let you buy or stream stuff online, three key expectations have emerged. Any one of these would be challenging to a 20th-century media company. Taken together, they require a total rethinking of the enterprise.

First, people are coming to expect an infinity of choice. They want news and entertainment on their own terms. They see no reason they shouldn’t be able to watch movies or TV shows or listen to music whenever they want, wherever they happen to be, on whatever device they have with them – and with a minimum of advertising, thank you.

The first glimmerings of this trend could be detected as far back as the mid-’70s, when Sony, Matsushita and JVC introduced reasonably priced home videocassette recorders. “Time shift,” as Sony’s cofounder, Akio Morita, called it, freed viewers from the tyranny of network programming schedules. Suddenly, people could record their favorite shows and watch them any time. Digital video recorders, introduced by TiVo in 1999 and eventually popularized by satellite and cable providers, made this even easier. By that time, however, time-shift was almost the least of it. The Internet was arousing a far more challenging set of expectations.

With the growth of broadband and the arrival of streaming video services like YouTube, Hulu and Netflix, it’s no longer enough to be able to record a show for future viewing, or try to locate a particular video-on-demand offering in the impossible-to-navigate haystack of cable lineups. Why should you have to deal with cable at all? And why should you be limited to shows that have recently been broadcast, or that networks make available through video on demand? For that matter, why should you be limited to programs that have been shown in the United States? Why shouldn’t you be able to watch any TV show that’s ever been broadcast anywhere? And movies – why aren’t they released on the same day the world over? And music albums? We all live on the same planet, and we’re all interconnected, so what exactly is the problem?

An intellectual-property lawyer could lay out in excruciating detail the tangle of rights issues and business interests that constitute the problem – but nobody wants to listen to corporate lawyers. People are here to be entertained.

Meanwhile, a second set of expectations has been developing. Humans have always wanted to somehow inhabit the stories that move them – to be spellbound, entranced, transported to another realm. Immersion, as James Parker put it in The Atlantic, is a state of altered consciousness – “not the prim suspension of disbelief, but its joyous capsizing.” Historically we’ve managed to plunge in with whatever technology is at hand, from books to film to TV. But digital raises the possibility of immersing ourselves even further, and in entirely new ways.
The Future of Media

Because this kind of thing often serves a marketing function, fueling engagement among committed fans and helping to bring in new ones, it’s turning up increasingly in connection with movies and TV shows. The Walking Dead, currently America’s most popular television series, offers a panoply of opportunities for involvement: not just the show itself and the comic series it’s based on, in addition, of course, to the now-requisite Facebook page, but also video games, mobile wireless games, online quizzes, webisodes that extend the main story through online video, novelization and even a weekly talk show about the series.

Other aspects of The Walking Dead saga don’t play out on screens at all. One of the more memorable events at last year’s Comic-Con, the annual geekfest in San Diego, was a live “zombie escape”; the AMC network even runs a zombie training course for viewers who want to be extras. Fans of the show can explore all or none of these, as they wish.

So we have audiences expecting an infinite lineup of choices and expecting to be able to immerse themselves in whatever type of story or entertainment they choose. But there is a third, closely related expectation as well: more and more, audiences expect some kind of active involvement. No longer passive consumers, they now want to be participants – critics, providers and (through the act of sharing on social media) distributors of information.

The age of the couch potato – the ultimate passive media consumer, tagged and identified in a 1987 New York magazine cover story on the social lethargy of middle-aged boomers – is now a memory, and not even that for anyone under 30. Now, with a keystroke, we can send out smartphone videos of a plane crash, an earthquake or a riot; we can share an opinion about the government, the restaurant down the street or the latest Brad Pitt movie. In the process, many of our most basic assumptions about media have been turned upside down. In a digital society, the role of the media is not just to speak but to listen; the role of the audience is not just to listen but to speak.

The Natural Order of Things?
The problem is that people naturally tend to assume that whatever they grew up with is the way things ought to be, and most of the people running media businesses today are products of the coach potato era. But no law of nature states that huge segments of the population shall zone out in front of the TV set for hours on end, or that people shall line up and pay money to sit quietly in a darkened theater with sticky floors and the ersatz-buttery aroma of diacetyl in the air, or that companies shall pay billions of dollars to newspaper publishers and television networks to advertise their wares.

In fact, there is little that’s traditional about “traditional” media. The media sector as it existed in the 20th century was an aberration – an accident at the intersection of economics and technology. Whether we like it or not, that accident is now being cleared by the inexorable forces of creative destruction and a new one is rising in its place.

To see things this way requires taking the long view. Starting in the 1830s, the Industrial Revolution made it feasible for the first time to print reading matter – books, newspapers, magazines – in very large quantities at very low cost and to distribute it quickly to very large numbers of people. A few decades later, inventions by Edison and others – electrical power, the phonograph, the motion-picture camera and projector – made it possible to package music and theater in a similar fashion. All this was enormously efficient in
terms of economics, and over time it spurred not only a series of very profitable businesses but a tremendous increase in cultural and political sophistication (the so-called “vast wasteland” of television notwithstanding). Even so, it came at a price.

Two factors in particular were troublesome. First, the advent of mass production made it prohibitively expensive for all but a handful of people to make themselves heard. Between 1835 and 1850, as the Harvard Law professor Yochai Benkler pointed out in his book *The Wealth of Networks*, the capacity of printing presses went from 1,000 sheets per day to 12,000, even as the cost of launching a New York daily newspaper shot up from approximately $12,400 in today’s dollars to $2.4 million. Each subsequent advance in technology made the process more expensive, not less – a development that would be celebrated as the barrier to entry that made industrial-scale newspapering viable and that has now been negated by the Internet.

At the same time, the rise of mass media severed the often-intimate connection that audiences had previously enjoyed with writers, orators and performers. Before, audiences had been a link in the creative process. In theaters, in music halls and even in print, they’d been engaged in a dialogue. Now they were being told to shush. So complete was the disconnect that when Richard Curtis (who went on to make *Four Weddings and a Funeral* and *Love Actually*) created the pioneering British comedy series *Blackadder* in 1983, he was reduced to peering into basement windows around London to see if anyone was watching his show.

Yet the idea that audiences should find their voices again has not been greeted with huzzahs from the mass-media establishment. Newspaper editors in particular have been aghast at the threat to their longstanding monopoly on information. Not that they put it that way, of course – to them, it’s a question of professionalism. Bloggers, untrained and unedited, just don’t cut it; never mind that some bloggers are, in fact, far more expert in the fields they cover than the average reporter. “If I need my appendix out, I’m not going to go to a citizen surgeon,” Bill Keller, then executive editor of *The New York Times*, declared in a speech three years ago.

Keller eventually moderated his attacks on “citizen journalism,” admitting that tweets from Tahrir Square, for instance, shed light on what was going on during the demonstrations against Hosni Mubarak. But his mistake all along was to paint the issue as an either/or situation. No reasonable person expects bloggers to take the place of journalists. But readers, like audiences of every sort today, do expect to have a dialogue with the professionals who tell them things. And journalists should recognize that this kind of partnership works to their benefit.

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Journalists can’t be everywhere and know everything. They need the help of people on the scene, people with special knowledge. In another context, these people would be called sources. It’s just that now, thanks to social media, the number of potential sources is almost infinite.

**GIVE PEOPLE WHAT THEY WANT?**

As goes newsgathering, so go the media industries in general. Audiences are coming to expect involvement, immersion and infinite choice. That has produced some interesting experiments, especially with regard to immersion. But in too many cases, media companies have been loath to give their customers what they want – especially when it interferes with their more immediate goal of maintaining long-profitable business models that are becoming increasingly obsolete.

A case in point is Hulu, the Web video site founded in 2007 as a partnership between News Corporation and NBC Universal. The idea was to port TV to the Internet. Tech bloggers all but hooted with derision, and with some justification: similar efforts by music labels a few years earlier had been almost comically inept, with online stores limited to the output of a single conglomerate and selling music that came so crippled with restrictions, both legal and technological, as to be all but unusable. But this time around, the two media companies made a smart move: they hired an Amazon executive, Jason Kilar, as chief executive, and they backed him on two important decisions. First, he insisted on including rival networks in the site’s search results on the grounds that to do otherwise would render it as useless as those early one-company music shops. And second, he asked for every show they could possibly license, on the grounds that to hold them back would be to invite piracy.

To television executives schooled in the economics of scarcity, Kilar’s moves were heresy. Scarcity has been extremely kind to TV and movie producers over the years, enabling them to limit access to their properties by funneling them into a series of highly lucrative distribution windows – theatrical, hotel pay-per-view, DVD, video on demand, pay TV, free TV and so forth. But in an age of endlessly replicable digital content, the old rules no longer applied. Enforced-scarcity strategies were becoming particularly untenable, so Kilar aimed to bypass them.

Within months of its launch, Hulu’s breadth of choice, together with its ease of use and clutter-free environment, made it one of the top-10 video sites in the United States. Within a year, it was No. 2 behind YouTube. The bloggers apologized. Hulu was a winner.

Or so it seemed. Things started to go wrong for Hulu when its top in-house proponent, News Corporation’s chief operating officer, Peter Chernin, left in 2009. The perception among most television and advertising executives was that, as an unnamed party to the industry conversation told the trade journal *Adweek*, “the more Hulu succeeds, the more its partners fail.”

It wasn’t only that online advertising was generally selling for a fraction of the price of television ads – though that in itself seemed reason enough to resist. Hulu was also seen as making an end run around cable and satellite providers, which were paying handsomely to carry the channels whose shows were now appearing online; as cannibalizing the by-now all-important home video market; and as hurting ratings (and therefore television ad rates) by cutting into broadcast viewing. Never mind that the DVD market was about to collapse anyway, or that, on a cost-per-thousand-viewer basis, Hulu commanded such a premium that it was actually selling its ad
inventory at prices comparable to television’s. With Chase Carey, the former chief executive of DirecTV, now in charge at News Corporation, a different attitude prevailed.

Kilar made his case – or threw down the gauntlet, depending on your point of view – with a lengthy post on Hulu’s blog. “History has shown that incumbents tend to fight trends that challenge established ways,” he wrote, “and, in the process, lose focus on what matters most: customers.” He predicted that “going forward, rapid innovation, low margins and customer obsession will define the winners in pay-TV distribution.”

You could almost hear the gasps of incredulity. Low margins – seriously? And who said anything about going forward? Within weeks, Fox moved to limit the availability of its shows on Hulu, denying subsequent reports of an immediate jump in online piracy. Then Hulu’s owners, which by this time included Disney in addition to NBC Universal and News Corporation, put it up for sale.

They soon changed their minds and announced they were keeping it after all. At the beginning of this year, after months of speculation, Kilar resigned. Hulu’s owners put it up for sale again, then pulled it off again amid unconfirmed reports that the bidding had barely topped $1 billion. Meanwhile, Netflix had gained a market cap of nearly $15 billion.

It’s unfortunate but understandable when mass media companies can’t find their way to the future. It is much worse when they are presented with it and reject it out of hand. At this point, only one thing about Hulu is clear: whoever disrupts television, it won’t be Fox and company.

**Piracy as an Indicator of Market Failure**

Refusal to meet audience expectations is one symptom of the entertainment industry’s disconnect. Another, closely related, symptom is the ongoing obsession with piracy. For years, the entertainment industry has been focused on stamping out illicit file-sharing through legal action – shutting down offending Web sites and randomly suing people who use them. Unfortunately, the whack-a-mole strategy has proven no more effective against piracy than it is against moles. But rather than lead the industry to reevaluate its efforts, this has mainly acted as a spur to intensify them.

The antipiracy campaign reached a high-water mark in the United States at the end of 2011, when Congress seemed poised to pass legislation intended to fight offshore file-sharing sites like the Pirate Bay. In fact, the Stop Online Piracy Act and its Senate counterpart went considerably further. The bills would have left Internet service providers, search engines, hosting sites like YouTube and online payment services like PayPal vulnerable to accusations of abetting piracy, regardless of whether the allegations were true.

Abandoning the principle of presumed innocence, the bills would have granted extrajudicial powers to accusers, enabling them to force Internet companies to cut off services to any Web site charged with copyright violation. Worse, technology experts asserted, technical provisions in the legislation would have compromised the security and even the functioning of the Internet.

Nonetheless, with cosponsors of every political persuasion, the bill seemed ready to sail through – until a last-minute mobilization by the tech industry and its supporters sent everything off the track. In a flash, or so it seemed, Google, Facebook, Wikipedia and their ilk were able to mobilize supporters online and render the legislation toxic. Deluged with phone calls and faced with a firestorm of protest on the Web, the bill’s Congressional
backers abandoned it willy-nilly.

Hollywood was stunned; that wasn’t how Washington was supposed to work. As a senior official at the Motion Picture Association of America, the movie industry lobbying arm, later admitted, “This was a fight on a platform we’re not at this point comfortable with.”

That much has been apparent from the start. Yet there is increasing evidence that the entertainment industry’s discomfort with the Internet exacts a heavy economic cost, not just in botched antipiracy drives but in lost revenues. In 2011, a five-year study conducted in six developing nations by the Social Sciences Research Center, a prominent New York-based think tank, concluded that “enforcement efforts have largely failed, and that the problem of piracy is better addressed as a failure of affordable access to media in legal markets.”

In some of the countries that were studied (South Africa, Russia, India, Brazil, Bolivia and Mexico), legal alternatives simply did not exist; in others, prices were too high for the locals to afford. One could argue that this situation doesn’t apply to more developed economies. Later the same year, however, an ad hoc survey in the UK found that, while nearly all of Time Out London’s top-50 British films were available on DVD – an increasingly unpopular medium – only 21 could be legally downloaded online. Ditto for more than 40 percent of the British Academy of Film and Television Arts best-film winners since 1960.

All this suggests that piracy really is a reflection of a market failure – and illicit downloads are a measure of audience dissatisfaction. Although direct causation can be difficult to prove, it is evident that as satisfaction goes up, piracy goes down. This is most obvious in the music industry, in which there has been a notable drop in piracy as legal download and streaming services have finally been made available.

The market-research firm NPD Group reported in February that only 21 million people worldwide were currently using illegal file-sharing networks, down from 33 million in 2005 – in spite of the enormous growth in people with access to the Internet. During 2012, the report continued, some 40 percent of the people who had been downloading from pirate sites at the start of the year either stopped entirely or did so less often. Of those, nearly half said they changed their behavior because they were able to get music legally through streaming services like Spotify and Pandora.

The industry’s own figures back this up. IFPI, the international music industry trade group, has reported regular year-over-year increases in digital revenues even as CD sales have collapsed. The digital numbers were minuscule at first, as new revenue streams almost always are. But last year they were enough to enable the world’s music labels to eke out a 0.3 percent increase in total revenues – their first since 1999.

Yet the appeal of antipiracy efforts to entertainment-industry executives is not hard to understand. As long as the problem is defined as a legal issue, the onus can be placed on consumers. But if there is a market failure – that is, if consumers are turning to piracy because...
it's the only way they can get what they want – then the problem is with the companies that supply the market.

To admit that they themselves are at fault would be tantamount to admitting that a media business based on industrial-era economics no longer works. It would mean that media companies would have to stop trying to defend the practices that made them so profitable in the past and start disrupting their own industries – a task for which they have shown very little appetite.

It's hard to blame them, of course. The problems facing 20th-century media enterprises are daunting, indeed. Business practices that have evolved over the past 50 to 100 years are failing to work, and in some cases it’s not clear what would.

For newspapers, the situation is particularly dire – consumer advertising melting away, once supremely profitable classified advertising gone to Craigslist, pay walls a dubious alternative for all but a few. The music business, fattened beyond recognition by the CD bonanza of the ’80s and ’90s, is making the painful adjustment to a new normal. The film business, so addicted to $200-million behemoths that it seems to be turning out more of them than there are summer weekends, is courting death by blockbuster. Broadcast television is a relic, its audience growing older by the day, its future as an ad medium evidently tied to the demand for statins and erectile-dysfunction drugs. The nimbler, more targeted cable channels are currently flourishing, but disruption waits in the wings; sooner or later they will almost certainly have to function without the economic cushion provided by intermediaries like DirecTV and Comcast.

There is no guarantee that any of these companies will survive – though some will doubtless live on as subsidiaries of, say, Google or Twitter, just as once-glamorous Paramount found itself a stepchild of the Nixon-era TV syndication outfit Viacom.

This is not to say that the industries themselves are doomed. If enough people want something – recorded music, say, or serial entertainment on the order of Breaking Bad or The Walking Dead – there’s very good reason to believe a market will emerge to support it. It may take a leap to imagine that market, much less create it. But people are taking such leaps already.

In the four years since Kickstarter, the online crowdfunding platform, was founded by a New York-based music journalist and two friends, it has provided financing for some 46,000 projects, including Oscar-nominated shorts; feature films by Brett Easton Ellis and Zach Braff, the Garden State director; and an Amanda Palmer album that debuted at No. 10 on the Billboard charts. “Hell, there are no rules here – we’re trying to accomplish something,” reads the epigraph atop Braff’s Kickstarter page, quoting a remark Edison made to a worker in his lab. By appealing directly to his fans (rather than submitting to financiers’ demands that he give up final cut), Braff raised $3.1 million in 30 days.

It’s up to incumbent media companies to prove their relevance in this new world. Meeting audience expectations is not in itself going to solve the economic problems these enterprises face. But if they fail to provide what people want, whatever else they do will hardly matter. In media, as in any other business, the companies that succeed are those that focus on satisfying the public, not on protecting obsolete business models. This seems to be a hard lesson to learn. But the conclusion is inescapable: executives who try to hang onto their jobs without pleasing their customers eventually find themselves with neither.