

The Influential Factors of Spotify's Business Strategy

Ryan Ruiyang Mei *

Shanghai American School Puxi Campus, Shanghai, 200000, China

* Corresponding Author Email: ryan06px2025@saschina.org

Abstract. Spotify, being the leading audio streaming platform globally, holds a dominant position within the business. In spite of the upward trend observed in both income and user engagement metrics over the course of several years, Spotify has experienced a substantial increase in its operational expenses. Specifically, these costs have escalated from \$90 million in 2018 to a remarkable \$13.05 billion in 2022. The exponential increase in spending has had a substantial influence on Spotify's financial performance. During the present fiscal year, there was a decline of 14% in the stock price of Spotify, specifically in the month of June. Despite its dominance in the audio streaming industry, Spotify has consistently incurred financial losses, primarily due to its low-profit margin business model. This research paper aims to employ the SWOT methodology in order to conduct a comprehensive examination of the components inside Spotify's business model that have contributed to its financial deficits.

Keywords: Spotify, Music streaming, audio platforms.

1. Introduction

Spotify has established itself as a trailblazer in the dynamic realm of music streaming, revolutionizing the manner in which we engage with and discover music. The network, originating from Sweden and established in 2008, has rapidly gained international recognition due to its substantial user base and large collection of songs spanning all genres. Spotify has gained widespread recognition as a prominent platform for music streaming, primarily because of its intuitive user interface, personalized recommendations, and diverse range of subscription plans. Although the undeniable dominance of Spotify in the music streaming industry is widely recognized, the business announced in 2018 its strategic shift towards becoming an audio streaming platform. This transition entails a focus on expanding its offerings beyond music to include podcasts and various other forms of audio content.

Nevertheless, Spotify is experiencing financial losses as a result of several immutable factors. One of the primary factors contributing to this phenomenon is the increasing level of competition.

The streaming music industry has become very competitive due to the presence of numerous prominent firms competing for market dominance. Competing entities such as Apple Music and Amazon Music offer comparable services, hence posing challenges to Spotify in its endeavor to sustain its dominant market position. Spotify, as of 2023, has 551 million users [1]. There are 88 million users and 68 million users for Apple Music and Amazon Music, respectively [2, 3]. The intense competition between these entities results in increased expenditures on marketing and promotional activities, thereby exerting financial pressure on Spotify. Spotify's sales and marketing expenses increased by €437 million by the end of 2022, which is a 39% total increase compared to 2021 [4]. Specifically, €200 million was spent on marketing campaigns and sponsorships. 13%, 12%, and 13% of total revenue were spent on sales marketing for 2022, 2021, and 2020, respectively [4].

Furthermore, Spotify is already facing challenges due to the rising costs of content. Spotify remunerates artists, record labels, and other entities with substantial royalties in exchange for the streaming of their music on the platform. By the end of 2022, Spotify will have paid more than €34 billion to music record labels, music holders, and other rights holders. This is a 21% increase in comparison to the prior year [4]. The expenses associated with the acquisition and authorization of content exhibit a positive correlation with the influx of emerging artists and the expanding consumer base. Prominent musicians have the ability to impose a significant licensing price, exerting considerable financial strain on Spotify's resources.

Thirdly, this can be attributed to the conversion of free users into paying subscribers. Although Spotify has a free tier with advertisements, premium subscribers are what the company relies on for the majority of its income, accounting for 87% of total revenue specifically [4]. The process of converting those who utilize a service for free into paying subscribers might present challenges due to several factors. Firstly, free users often become acclimated to the presence of advertisements, which may deter them from transitioning to a paid subscription model.

Additionally, a significant portion of these free users tend to be young individuals who may lack the necessary financial resources to commit to a paid subscription. The expenses of Spotify are augmented due to the expenditures incurred in acquiring and maintaining consumers through marketing campaigns and exclusive content deals. Spotify is subject to the influence of investment in its growth and development. Spotify allocates significant resources towards research and development, as well as product breakthroughs and global expansion, in order to maintain its competitiveness and foster a culture of creativity. The allocation of resources towards these expenditures by Spotify may potentially lead to short-term financial setbacks since the company prioritizes long-term objectives such as market share growth and expansion of its user base rather than immediate profitability.

The goal of this article is to examine the benefits and drawbacks of Spotify's strategic initiatives and identify the elements that contribute to the company's financial deficit. To investigate the solution to this question, this article will employ SWOT analysis to examine Spotify's strategic policies and characteristics from 2022 to 2023. This will determine Spotify's strengths and limitations and the ideal strategy to work. Such research can not only provide a better solution for Spotify but also provide a reference for other companies.

2. Case Description

Spotify is a well-known music streaming service that has grown in popularity and notoriety since its inception in 2008. It provides customers with access to a large database of music covering multiple genres, artists, and albums. Spotify offers an easy platform for consumers to explore, stream, and share music online, with millions of songs available. Spotify's website claims that they have "100 million tracks, 5 million podcast titles, and 350,000 audiobooks." Spotify has a sizable user base, with "551 million users, including 220 million subscribers in more than 180 markets." These figures are far greater than those of Spotify's competitors, including Apple Music, Amazon Music, and YouTube Music. Spotify's personalized recommendation system, which uses user data and algorithms to provide music recommendations based on personal preferences, is one of the service's major features. This tailored approach improves the listening experience by introducing consumers to new bands and songs they might enjoy.

Spotify has improved as an audio content platform by including podcasts in addition to music streaming. Users can search a large library of podcasts covering a wide range of topics such as news, entertainment, education, and storytelling. One of the most notable and popular podcasts is JRE (Joe Rogan Experience).

Spotify's user-friendly interface and intuitive mobile apps allow it to be accessed from a variety of platforms, including smartphones, tablets, and PCs. Users can also follow friends, share playlists, and cooperate on curated music collections, which encourages social interaction.

Spotify subscribers can choose between two subscription plans: free and premium. Users can access Spotify's music catalog for free, but to listen online, they must subscribe to the subscription tier. The premium subscription, on the other hand, removes advertisements, gives superior download audio quality, and includes additional features such as offline listening and unlimited skips.

While the free tier draws a large number of consumers, it offers potential income issues for Spotify. Over 40% of Spotify's user population currently uses the free model, and this figure has been continuously increasing over time. [4] In reality, 330 million people use the free tier. Spotify's capacity to earn revenue from free users is mostly based on ad-supported revenue, which accounts

for approximately 13% of overall revenue. [4] However, premium accounts account for the vast majority of Spotify's revenue, accounting for 87% of total revenue. [4] These premium customers pay a monthly subscription for ad-free access, expanded features, and greater audio quality. As a result, as the number of free users continues to grow, Spotify's viability may be jeopardized, as the company's profit margins may shrink.

3. Analysis on Problem

3.1. Strengths

Spotify has a large selection of songs, which is one of its main strengths [5]. Spotify is well-known for its huge music collection, which includes millions of songs from various genres and so caters to a wide range of users. Furthermore, Spotify has a platform that has been created with the user in mind. The Spotify platform has a user experience that is both fluid and intuitive, allowing users to easily discover, organize, and access music. Furthermore, the use of personalized recommendations contributes to Spotify's beneficial situation. Spotify's recommendation system employs algorithms to recommend music to users based on their own interests. This method improves user engagement and contentment [6]. Spotify's strong brand recognition is one of its distinguishing features [7]. The company has established itself as a market leader in music streaming, owing to strong brand awareness and a large user base. Finally, it is critical to provide broad device compatibility. Spotify is compatible with a wide number of devices, including smartphones, tablets, desktop computers, smart speakers, and game consoles, allowing for broad accessibility. Spotify incorporates many prominent features, and it is critical to maintain and possibly improve on these abilities.

3.2. Weaknesses

Despite its many outstanding features, Spotify falls short of perfection. Spotify's reliance on licensing deals is one of the obstacles preventing further advancement. Shah and his colleagues have also shown that the rewards for licensing and innovation will increase, while more resources will be available for R&D [8]. Spotify's business model is based on acquiring licenses from record labels and publishers, making it vulnerable to increased royalty payments, resulting in significant income loss. As more established musicians post their music on Spotify, the firm will devote a larger portion of its earnings to this in order to support its enormous content base. Furthermore, Spotify is constantly confronted with the problem of resolving its tight profit margins. Spotify has a large user base, but it struggles to sustain a consistent level of profitability due to increased expenses related to content licensing and revenue-sharing agreements. Furthermore, Spotify is obligated to acknowledge the very competitive environment. The music streaming industry is characterized by tremendous competition, with various platforms vying for a larger share of the market. Exclusive content deals, pricing strategies, and the development of unique platform functionalities are driving this competition. Although Spotify currently rules the business, it must keep an eye on what other platforms are doing.

3.3. Opportunity

Given the market in which Spotify operates, there are several options for it to enhance its market position and value. Spotify should first assess its global expansion plan [9]. Spotify has the opportunity to expand its worldwide reach by capitalizing on rising demand for music streaming services in developing markets. Then, given the rapid growth of the podcasting industry, Spotify's entry into podcasting gives it an opportunity to widen its content offerings, attract new customers, and capture a piece of the rapidly expanding podcast market. India, with about 55 million active users, is an example of a recently entered market that is fueling Spotify's revenue. Third, the opportunity took the form of partnerships and collaborations. Collaborations with musicians, record labels, and other media companies can help Spotify expand its content library, enhance user engagement, and differentiate itself. Finally, Spotify may always strengthen its marketing strategy and raise premium subscription fees. Spotify's advertising possibilities may be expanded by utilizing its huge user data

to provide advertisers with targeted and customized advertising options; this can enhance profit for free users, and the price rise will allow premium customers to generate more profit for Spotify [6].

3.4. Threats

One primary concern that Spotify must be mindful of is the competitive environment. Rivals such as Apple Music, Amazon Music, and YouTube Music provide a formidable challenge to Spotify's dominance in the industry due to their well-established platforms, exclusive content offerings, and substantial financial capabilities. Furthermore, it is imperative for Spotify to closely monitor the ever-changing dynamics of the industry. The music industry undergoes continuous transformation, as alterations in consumer preferences, technological breakthroughs, and legislative developments have the potential to influence Spotify's business model and operational strategies [10]. Moreover, the dynamic nature of royalty distribution in the music industry may potentially pose a risk to Spotify. Potential alterations to royalty legislation, royalty rates, or artist remuneration frameworks possess the potential to exert an influence on Spotify's financial viability and its associations with rights holders.

4. Results & Discussion

Overall, Spotify's strengths lie in its extensive music library, user-friendly platform, personalized recommendations, strong brand recognition, and broad device compatibility. Spotify is the top audio streaming platform globally with the most users and still holds its reputation for platform dominance. However, the company faces challenges in terms of high royalties paid due to license agreements with artists, low profitability after paid licensing, and competition with other audio streaming platforms such as Apple Music and Amazon Music. By capitalizing on opportunities such as global expansion, podcasting growth, partnerships, and an enhanced advertising strategy, Spotify can mitigate threats and continue to evolve in the dynamic music streaming landscape. The fundamental issue with the business model of Spotify is that it has low profit margins, which is why it should earn more revenue by increasing its premium user base and content which is the quantity. Spotify can do this by expanding to more countries. Spotify should also increase its premium prices slightly in order to keep up with its expenses paid via royalties. Spotify should negotiate more with music labels to pay less royalties in order to decrease expenses, and figure out a way to make advertisements more personalized in order to profit more from free users. With these three solutions, Spotify will earn more money, increase its user base, and save more money.

5. Conclusion

In conclusion, a number of factors can be used to explain Spotify's financial losses. Rising marketing and promotional costs have had a negative impact on Spotify's profitability as a result of the fierce competition in the streaming music market and the emergence of several significant players. The rising costs of acquiring and licensing content, including significant royalties paid to artists and labels, have also put a strain on the company's financial resources. It has proven difficult to turn free users into paid subscribers, which has a negative impact on Spotify's profitability. Additionally, the company's substantial investments in product improvements and global expansion have resulted in upfront costs that could take some time to yield significant returns.

The study paper presents contributions that have the potential to enhance the comprehension of music label owners regarding strategies to prevent financial losses and enhance profit margins. Nevertheless, the presence of some constraints, such as the absence of comprehensive data in the financial statements, has the potential to lead to erroneous assessments and partiality in the evaluation of the organization's expenditures and income as a whole.

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