

Apple's Beats buy is two-sided for music streaming

May 29 2014, by Ryan Nakashima

Apple's [\\$3 billion purchase](#) of headphone maker and streaming music company Beats Electronics sheds light on a rarely recognized reality in the music streaming industry: It's hard to succeed in the business without offering other products and services.

Streaming [music companies](#) like Beats Music, which charge users up to \$10 a month, can sometimes pay as much as 70 percent of their revenue in artist royalty fees. That leaves little left for advertising and promotional campaigns to explain to consumers the benefits of paying for a music service.

"The only people that can afford to get into this business have other main businesses," says Mark Mulligan, a music industry analyst and blogger with MIDiA Consulting. "Every service ends up putting itself into significant debt just to cover its basic operating costs."

Even [streaming](#) leader Spotify—with 10 million paying customers worldwide—is reportedly burning through cash as it seeks to attract enough subscribers to help it turn a profit. With just 250,000 subscribers, analysts say Beats Music is even further from that goal.

Although analysts say Apple's purchase is largely an acquisition of talent and a way to offset the declining popularity of iTunes song downloads, the company notes its main source of revenue has always been from devices. Music is just a hook to make those devices more usable and attractive.

Observers believe Apple's purchase of Beats could have both positive and negative effects for other streaming companies.

On the one hand, if Apple Inc. pushes hard to promote streaming music subscriptions and makes it the idea more acceptable to a broader audience who currently purchase downloads or acquire pirated music, the company's efforts could help all [music services](#).

After all, Apple has been the driving force in many new product categories. It popularized digital music players with the iPod, gave birth to the smartphone era with the iPhone, and was instrumental in creating customer demand for tablets with the iPad.

"We're cheering from the sidelines," says Paul Springer, [senior vice president](#) of the Americas for Rhapsody International, which has 1.7 million paying music subscribers worldwide. "When the most valuable company in the world says that music subscriptions are strategic to its future, that's great for our sector. That's great for customer awareness."

Even so, there's a downside for the industry. Apple could easily devalue music subscriptions by running the service at a loss because it makes plenty of money elsewhere. Apple is likely to advertise and possibly offer bundled discounts to make Beats Music a bigger force.

Already, prices across the industry for unlimited streaming plans are starting to drop from the original price of \$10 a month. Beats itself offers a family subscription for \$15 a month for up to five people, as long as they're on a group account with cellphone operator AT&T. For a limited time, mobile carrier Sprint has cut Spotify Premium prices to \$5 a month per person as long as six people are on a family plan.

If Apple creates an even more attractive bundle for people who buy Beats headphones or Apple devices, stand-alone music services may find

it tougher to compete.

"It makes Spotify nervous," says James McQuivey, a digital content business analyst with Forrester Research. "They only have the one revenue stream. It would be harder for them to compete in a marketplace against someone that doesn't have to return the same cash."

Even before Apple jumped in, the paid streaming music business was in a tight squeeze. Spotify, based in Sweden, reportedly lost about \$80 million, despite more than doubling revenue to around \$590 million, in 2012. Its results for 2013 are expected in the next couple of months, although Spotify said earlier this month that its paying subscribers jumped 66 percent over the last 14 months.

Rdio, the streaming service backed by Skype co-founders Janus Friis, last year sold a 15 percent equity stake to radio station network operator Cumulus Media Inc. in exchange for \$75 million of on-air advertising. The deal was an acknowledgement that cash flow from operations wasn't enough to pay for marketing.

It's unclear what Apple's purchase price means for the value of other streaming operators, because Beats' \$3 billion purchase price includes some amount for the hugely popular headphone portion of the business, which is profitable and posted \$1.1 billion in revenue last year.

What is clear is that music streaming is just a part of the mix for Apple. Figuring out how best to match [music](#) with its devices could help Apple stand out in an increasingly crowded consumer electronics market.

"Apple always bundled software well with hardware," says Moshe Cohen, an assistant professor at Columbia Business School. "That is a big advantage. How to create those bundles is important to producing a superior product and a much bigger business."

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Citation: Apple's Beats buy is two-sided for music streaming (2014, May 29) retrieved 25 June 2024 from <https://phys.org/news/2014-05-apple-two-sided-music-streaming.html>

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