

To what extent was Apple acquiring Shazam a profitable investment?

Business and Management Standard Level Internal Assessment

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1. Introduction

Apple is a technology giant operating in the tertiary and quaternary sectors. Apple's business model is based on its customers being Apple-device users. On their devices Apple offers unique software and premium options for extra payment. To keep their devices attractive to customers Apple constantly develops their devices and software.

Shazam, before the acquisition, was a software company also operating in the tertiary and quaternary sectors with a single application - Shazam. Shazam "*name(s) any song in seconds*"¹ from audio - users just press a button. This requires top-notch sound analysis software. Shazam already collaborated with Apple. Still Apple spent \$400 million USD on Shazam, closing the deal in September 2018.

Apple wanted to increase their competitive advantage in the music streaming industry and Shazam provided a strategic integration that filled gaps in their current model. This commentary will analyse the benefits of this investment to find "to what extent was Apple acquiring Shazam a profitable investment" and will be largely based on the supporting documents listed separately in the bibliography.

2. Commentary

2.1. Company Analysis: Apple SWOT

The following SWOT analysis of Apple, with main focus on Apple Music, shows that Shazam could improve Apple's position in the music industry since they, compared

¹ www.shazam.com

to Spotify, lack in recommendation systems and personalisation of the service. Additionally Apple aims to take advantage of the opportunity presented by the growing music streaming service market.

Apple (Music) SWOT

Strengths <ul style="list-style-type: none">- Large Apple device user base- Reputation	Weaknesses <ul style="list-style-type: none">- Lack of personalisation of music streaming experience
Opportunities <ul style="list-style-type: none">- Expanding market	Threats <ul style="list-style-type: none">- Competition in limited market- Public opinion

2.2 Benefits of Acquiring Shazam

2.1.1 Increasing Market Share

The Acquisition's primary goal was likely to increase Apple's market share in the music streaming business via increasing the popularity of Apple Music, making the acquisition a growth strategy. In Ansoff's matrix the strategy would be market penetration, since Apple music was an existing product and the goal was to increase market share in the established market. This is generally a low risk strategy, here the Apple only risked the \$400 million.

Shazam earned revenue primarily through advertisements², before and after it completes a search - being used over 20 million times every day³ this amounts to significant revenue. However advertising on Shazam is not Apple's priority - Apple swiftly announced that it would remove advertisements from Shazam entirely⁴, showing interest toward increasing the applications popularity with a potential loss of direct profit. Shazam also generated revenue from contracts with companies such as Spotify and Apple music⁵. Shazam would refer its users to Spotify or Apple music after finding the song, growing the user base of said services. By acquiring Shazam Apple enabled Apple music's more prominent role within Shazam⁶ - essentially other music streaming services are behind an additional button press compared to Apple Music. Since the users already enjoy an easy music identification experience, they just might click the first button they see in order to listen to, or save, the song. Apple also gained the possibility for synergy between Shazam and Apple music⁷ - Shazam now directly uploads songs any Apple Music user identifies to their Apple Music account. All of this could make Apple Music a more attractive product compared to Spotify, the currently clearly largest music streaming service⁸.

It would seem that the effort to increase the market share of Apple Music with Shazam has been a success in providing a competitive advantage to Apple Music - Apple Music saw a 36% increase in subscriptions in 2019⁹. Partially this can be

² Kolodny, 2017

³ Supporting Document 1

⁴ Supporting Document 2

⁵ Kolodny, 2017

⁶ Supporting Document 4

⁷ Supporting Document 4

⁸ Supporting Document 3

⁹ Supporting Document 3

attributed to overall growth of the music subscription market, which grew 32%¹⁰. Proportional to its size Apple outgrew its competition which means that Apple Music's market share increased - Spotify grew by 19%, proportionally second to Apple¹¹ and since Spotify is the only true threat from competition to Apple Music. This means that Apple Music's competitiveness with Spotify as a product has improved which was the goal of the acquisition though other factors play toward this improvement, too.

A long-term goal of Apple's could be creating an end to end user experience via Apple - a user hears a song, identifies it with Shazam, finds it on Apple Music and listens to it with sound equipment from Beats or Apple.¹²

A pipeline like such offers great opportunities of expanding on the particular market by creating a great user experience only available via purchasing all of Apple's products. This extensive synergy between products could down the line make Apple the music industry giant, which is something a company the size of Apple could plan for. This pipeline would easily make the acquisition cost worthwhile.

2.1.2 Access to Data

Apart from its advertising, referring and integrating potential Shazam has an enormous data collection potential - it can log the user's approximate location, what they're listening to and often even the user's age demographic. And it isn't only the potential data Apple gains. With the acquisition Apple bought all the data Shazam

¹⁰ Supporting Document 3

¹¹ Degre, 2020

¹² Supporting Document 4

has collected during its almost two decade existence¹³. Data is an increasingly valuable resource, referred to as “*the new oil*”¹⁴ by Clive Humby. Apple can use the collected data to build on existing data to further optimise recommendations, something Spotify is famous for¹⁵, on Apple Music to make Apple Music more attractive and for further use on other aspects of the Apple software experience. It could even be used to predict music trends and hits¹⁶. This improves Apple Music’s product appeal and hence competitiveness with Spotify. Shazam’s value in particular to Apple is from it’s cross platform nature. Shazam is accessible by Apple and Android users equally as well as to users who can’t afford an iPhone. This means that the data is probably “new” to Apple, who has already collected large amounts of data from its own users. To appeal to Android users, Apple must be able to optimise its products to this new audience, which can be done with Shazam’s data. Shazam’s data has already directly powered new playlists on Apple Music¹⁷.

2.2 Financial analysis

The following is an analysis of the financial aspects of the acquisition. This section considers the financial health of Shazam and direct return on investment for Apple.

Before 2018 Shazam had never turned a profit¹⁸. From the statement of changes in equity it also appears that the company was £51 million in debt 1st of

¹³ Supporting Document 4

¹⁴ Haupt, 2016

¹⁵ Supporting Document 1

¹⁶ Supporting Document 1

¹⁷ Perez, 2019

¹⁸ Supporting Document 2

January 2017 which grew to £69 million at 31st of December 2017¹⁹. It is clear that Shazam had been indebted for a while in 2017. However it is also clear that Shazam had significant existing equity, since the total equity of the company was still positive²⁰. This is likely at least partially from the \$143 million Shazam had raised as venture capital²¹. Shazam's situation did seem to be improving, though, as can be seen from the increasing revenue and decreasing added debt in 2016, which was only a quarter of that added in 2015²². Yet in 2017 Shazam returned to levels of loss more similar to 2015²³. After the acquisition Shazam, for the first time in its existence, turned a profit in 2018 boosted by Apple's acquisition payment - the income for the financial year was positive due to "Income from the disposal of intangible assets"²⁴, or Apple's money.

However the operating losses of Shazam are effectively inconsequential to Apple. The purchase price of \$400 million is a small amount for a trillion dollar company like Apple, which covered the acquisition in profits in about two days with their yearly gross profit of over \$100 billion in 2018²⁵. The price is also trumped by public opinion concerns since due to Apple's size a minor drop, maybe from a negative news article, in Apple's stock price is far more serious than a loss of \$400 million.

¹⁹ Supporting Document 5

²⁰ Supporting Document 5

²¹ Supporting Document 2

²² Supporting Document 2

²³ Supporting Document 5

²⁴ Supporting Document 5

²⁵ "Apple Gross Profit 2006-2020", 2020

3. Conclusion

In conclusion in terms of direct profit, the acquisition was likely not a profitable investment. Shazam had been operating at a loss for years and the removal of ads after the acquisition definitely does not help, Shazam made a profit in 2018 only by sale of intellectual assets to Apple. Nonetheless the decision as a whole was a profitable investment due to the potential for growth of Apple Music, hence the acquisition was a success. Shazam can refer people to Apple Music after they have identified a song and provides possibilities for improving the competitiveness of Apple Music. Also importantly by acquiring Shazam Apple gained access to Shazams data on music trends, optimizing Apple Music's recommendations system and predicting hits. All this has improved the Apple Music experience and subscriber count and is partially responsible for the increase in Apple Music's market share within the music streaming business. Since Apple is a massive company its goals are also far beyond what Shazam can alone offer: perhaps aiming for a music pipeline, an end to end Apple experience, rendering the \$400 million a small investment. To answer the question, acquiring Shazam was a profitable investment via increasing Apple's total revenue and profit.

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