

Spotify vs Apple's iTunes: A Value Chain Approach.

Section 1: Introductory Paragraph

The ever changing music industry is at a crossroads once again when it comes to pricing and distribution. Two distinct avenues have emerged, the digital pay as you go model adopted by iTunes and others, and the new unlimited access but monthly fee model used predominantly by Spotify and Pandora. In this fast paced market, innovation is key and no one has an indefinite lock on the market. This paper will predominantly focus on the primary value activities in each company's value chain.

Section 2: Industry and Competitors

The music industry is in a constant cycle of change as firms vie for competitive advantages. New innovations constantly improve the industry, and if competitors are not careful and do not keep up, they will be left behind. Cassettes were replaced by CDs, which were replaced by mp3s which appear now are being replaced by streamed content. The current players in the music industry are Spotify, Pandora, Google Play Music, and Apple's iTunes. Both Spotify and Pandora use a subscription based or ad supported model. iTunes uses a purchased per song model. Google play uses both a subscription model and a purchased per song model.

Section 3: Value Chain of Apple's iTunes

Apple's iTunes do not produce a product from raw materials but instead provide the service of outbound logistics as they distribute music in an innovative way. Their 2002 innovation in the ever changing music industry has been met with much competition. iTunes method of distribution is to sell each song for a small fee per song. Gone are the days of buying an album just for two or three songs which dynamically has changed the music industry. Once

the customer purchases the song, they have access to the song as often as they like and for as long as they want the song.

Apple uses many different ways to support the customer after purchase. Their support page has several FAQ sections and ways to directly contact Apple via telephone or email if needed. Apple also uses a community forum or “Support Communities” to allow customers to help each other.

iTunes has exclusive rights to a variety of artists including The Beatles which is a major draw to the baby boomer generation. These type of contracts make their service harder to imitate and adds value as the competition is eliminated in these specific areas.

Apple’s marketing strategy is to produce a high quality product that once purchased leads to other purchases thus getting the customer to invest more and more into their ecosystem. “The truth is, iTunes is not a large moneymaker. Its contribution to Apple’s success is slim, if at all” (“The-apple-marketing-strategy”). iTunes is more of a support activity to help the sales of Apple’s other more profitable items such as their iPhone which makes over fifty percent of their revenue while iTunes contributes around 9 percent of the company’s total revenue (Mitchell). For instance, last weekend this author attended a birthday party where the musical entertainment was provided by iTunes played on an iPad. The gifts given included gift cards for iTunes.

Section 4: Value Chain of Spotify

The outbound logistics is key when it comes to Spotify’s distribution network and their primary value adding activities. “The Spotify service is a peer-assisted system, meaning it has a peer-to-peer component to offload backend servers” (Yanggrotke). This peer-to-peer system significantly reduces the strain on Spotify’s servers. It also greatly reduces the time required to

deliver the music to the customer. Time is an important factor to keep a competitive edge.

“When a client plays a music track, its data is obtained from a combination of three sources: the client local cache (if the same track has been played recently), other Spotify clients through peer-to-peer technology, or the Spotify storage system in a backend site” (Yanggrotke).

The other key value adding activity is Spotify’s music, which is distributed in two main ways: ad supported and subscription based. The ad supported option is free for the listeners, but the advertiser provides Spotify with revenue. The listener is limited to how many plays per song per month. The subscription based option has no ads but the listener directly provides Spotify with revenue and plays per song is not limited.

Spotify’s direct support is limited. While they do have FAQ pages, getting into direct contact with a Spotify employee is very difficult. The best way to get help would be to contact other Spotify users through their community forum. This technique is an interesting way to reduce support cost, while still providing some support to their customers.

According to Spotify’s website which explains how their business model works, Spotify retains 30% of their total revenue and pays 70% to the music rights holders (“Spotify Explained”). This speaks well of Spotify’s respect for the talent of the artist and their music as the music is being obtained legally and not pirated.

Spotify’s marketing strategy is more of a grass roots, word of mouth campaign. Friends tell friends about a playlist they created, or they tell them about a new playlist created by a celebrity that they enjoyed. This form of marketing is very low cost and can be very successful.

Section 5: IT Innovation of both companies

iTunes, by choosing a digital distribution model, was able to use IT innovations to significantly reduce their costs by cutting out the manufacturing costs of CDs. Spotify, using their peer-to-peer system, was able to reduce their costs significantly by offloading the usage of their servers by allowing data to be transferred from person-to-person. “Radically unlike all of its Web-based music streaming peers, Spotify only gathers 8.8% (on average) of its data from Web servers. An additional 35.8% comes from peer-to-peer networks, with the final 55.4% coming directly from locally cached data” (Haupt).

Customers have the opportunity to create their own playlist of songs by grouping together a number of songs which can be shared with others or kept for personal use only. Sharable playlists are an innovation to Spotify’s credit that iTunes has yet to duplicate. “Playlists are the most important element of Spotify’s functionality for users—they are used as a place to remember interesting tracks, learn about new music, and create mixes for experimentation and sharing with others”(Haupt). These playlists can be created by the user, or can be created by others such as celebrities.

Section 6: Impact of Spotify’s Innovation on the industry

Spotify has over 60 million active users and over 15 million paid subscribers (“Spotify Explained”). These 60 million subscribers could have been pirating the music they listen to but thanks to Spotify’s innovative business model, they now contribute to the music industry’s revenue by either listening to ads or paying a monthly fee. In 2011, Strategic Minds reported that, “iTunes very existence has driven out all competition, and Jobs has dominated that portion of the music industry. It may be a marginal earner now. But what about next year” (“The-apple-marketing-strategy”)? It turns out that next year Spotify had gained 5 million users and steadily increases every year (“Spotify Explained”).

Section 7: Apple's Reaction and Forecast

On Monday, April 13th 2015, Apple updated their iOS with a few changes; one of which being an updated look at its music app. According to Business Insider “An updated music app might not seem like a big deal, but it's the first tangible sign that Apple is preparing to dramatically shake up iTunes, changing the platform to focus on streaming rather than downloads” (Cook). This authors agrees that iTunes will eventually release their own version of Spotify's streaming service. With the amount of capital that Apple has, their entry into the streaming market should shake up that sector.

Section 8: Concluding Paragraph

This is the first time that Apple has not been on the cutting edge of innovation. Steve Jobs died in 2011, which is the same year that Spotify launched in the United States. This author believes that even if Steve Jobs was alive, he would not have been able to stop Spotify's climb. However, he may have been able to slow it down and release an alternative service much sooner.

iTunes still rides its wave of success, yet they need to not just ride their wave as RIM did with their now irrelevant Blackberry innovation. iTunes need to step up their game with new innovations. Time has proven that iTunes exclusive rights to certain popular artists is not enough to keep the competition out indefinitely. Spotify has found a way to break through iTunes hold on the market with its sharable playlist, peer-to-peer system, and their focus on their service. If Apple continues to take steps towards adapting to a more streaming focused service model, they should be able to continue their position in the digital music distribution market. iTunes has the financial strength of Apple to back it up while Spotify is dependent on its sole source of revenue.

Section 9: Bibliography

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