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Apple Music may finally have the muscle to knock off Spotify

By Steven Zeitchik

The HomePod speaker is displayed on the first day of sales at an Apple Inc. store in New York on Feb. 9, 2018. (Mark Kauzlarich/Bloomberg)

Apple is turning up the volume on Apple Music, the streaming subscription that comes loaded on its devices, including the new HomePod smart speaker.

But that could mute the potential of Spotify, the independent music subscription service that aims to go public this year.

“We are at an inflection point in digital music,” said Lloyd Greif, who runs Greif & Co., a Los Angeles-based investment bank specialized in entertainment and media. “If Spotify doesn’t make a move, Apple could be dominating within 12 months. Apple is coming for them and they can’t stand still.”

Since it launched nearly three years ago, Apple Music has tried hard to make inroads against Spotify. The Swedish company, founded in 2008, entered the U.S. market in 2011 and quickly began accumulating subscribers with its tantalizing offer of millions of songs at the swipe of a finger. (It also offers an ad-supported service that generates far less revenue.)

As of late 2017, Spotify had 18.2 million subscribers in the U.S. compared to Apple Music’s 15 million, according to Billboard. Both charge $9.99 monthly for their primary service. (Globally, Spotify has a significant advantage — 140 million active users, according to the company, nearly twice Apple’s tally.)

But Apple is gaining on Spotify. According to a Wall Street Journal story, Apple currently has a 5 percent monthly growth rate in paid U.S. subscribers compared to 2 percent for its chief competitor. If that holds, Apple will surpass the Swedish firm by summer — especially salient given Spotify’s plans for a U.S. IPO in the coming months.

Apple and Spotify declined to comment.

Apple’s amping up of its music streaming business is the latest example of a tech giant tacking a side venture onto its existing platform – in this case, products such as the iPhone, Apple Watch and HomePod — but in the process greatly impairing a smaller competitor.

Facebook did this when it introduced a feature on several of its sites, including Instagram, that directly mimicked one of the most popular uses of rival Snapchat. The Instagram feature, known as Stories, last year surpassed 250 million daily users compared to 166 million people who used any part of Snapchat at least once a day for the same time period.

And when Amazon got in to meal kits last year, the announcement sent the stock of Blue Apron down more than 10 percent in one day.

Apple is bidding for a music-streaming edge by locking users into its universe of products. Apple Music works far more easily on HomePod, which debuted Friday, than other music streamers. That both incentivizes people to buy HomePod and, maybe more importantly, gives consumers who have HomePod reason to sign up for the service.

"Let's be candid — a lot of people are compelled to go to Apple because they're in the Apple ecosystem; without those restrictions, they wouldn't choose to go there," said Peter Fader, a Wharton School of Business professor who has studied consumer behavior and the music industry.

Apple Music makes up a very small sliver of the company's overall business. The division of which it's a part – which also includes such services as Apple Pay, iCloud and the App store – composed just 10 percent of overall revenue of $88.3 billion in the first quarter of 2018.

Still, the division's importance is growing — the year prior it composed about 8.5 percent of the company's overall revenue for the quarter — as growth for products like the iPhone and Mac have slowed.

"Apple has a strategic reason to have a robust streaming-music business," said Larry Miller, a professor of music business at New York University's Steinhardt School, alluding to the sector's health relative to Apple's hardware business. "And they have some very powerful strategic assets—like cash—to deploy and win the streaming-music arms race."

That money, he said, could be used to increase the marketing of — and technological bells and whistles on — the service, which would then attract and retain more subscribers.

Such a move could have deep implications for the music business. A powerful Apple Music would allow the tech giant to hold more sway over record labels or even raise prices to customers who've become hooked on the service.

Streaming now accounts for 62 percent of music revenue in the U.S., according to the Recording Industry Association of America, thanks to Apple Music and Spotify, as well as less popular services from Pandora, Amazon and YouTube. (Amazon's chief executive, Jeffrey P. Bezos, owns The Washington Post.)

If Apple seizes this business, it would mark a kind of back-to-the-future moment. The Cupertino, Calif., company once had a chokehold on digital music via iTunes, back when paid downloads reigned. It often used its leverage to extract higher royalties — until the market cratered due to streaming.

"Apple didn't ultimately win then but they see this as a chance to win now," Greif said. "This goes deep in the company's DNA."

Record companies don't wish for that dominance–and not just because it's Apple. Executives at the Big Three of Universal Music Group, Warner Music Group and Sony Music, speaking anonymously to not jeopardize their relationships with streamers, said multiple streaming players are in their interest. Such diversity increases innovation among the streaming platforms and prevents any one company from gaining too much leverage over them.

"We think a competitive marketplace is important to the health of the streaming business," one executive told The Post. "A single player is very unhealthy."

To stay competitive, Spotify needs capital of its own, which is where the IPO comes in. The company is likely to issue the offering this spring and plans on an unconventional Wall Street approach.

But Spotify may already hold an advantage, say some experts: superior personalization and user interfaces. Wharton's Fader notes that, despite Apple's ability to lock users into its ecosystem, Spotify knows its users better and can cater to them in both their design and their technology. "Apple has a home-field advantage but Spotify has the better team," he said.

Unlike video, where streaming giants such as Netflix and Amazon can boast very different content, music offerings are largely similar. Apple has an extremely large library of about 45 million songs, but Spotify still has 30 million songs, sufficient for most users.

So the companies have tried to distinguish themselves in other ways, like the customer experience. Because of its ease-of-use with playlists, Spotify tends to be more popular among those who prefer curating choices from diverse sources compared to Apple's more artist- and album-driven clientele. With its global bent, Spotify at times is more diverse in the music it promotes, veering from pop and hip-hop more often than Apple.

Amazon, meanwhile, has sought to sell its service in part on the ease of use with its Echo speaker.

With the number of streaming subscribers in the U.S. currently estimated at lower than 50 million, many new customers are still up for grabs. Data from Consumer Intelligence Research Partners show that comparatively few Americans now pay for streaming services — no more than 13 percent of iPhone users subscribe to any single service. For Amazon customers, the ratio is even lower, at 10 percent.

That means Apple still is far from winning. But it also means there's an opportunity for Spotify to fall further behind.

"We're in the late innings of early adoption," said NYU's Miller. "There's a lot of room for these companies to grow — or fail."