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THE PRICE OF FREE. SPOTIFY'S BATTLE FOR PRODUCT-MARKET FIT IN THE
STREAMING WARS OF 2015. – PRICING STRATEGY

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Abstract Group Part (100 words maximum)

This case study examines Spotify's strategic challenges during the 2015 streaming wars, using tools such as PESTEL, SWOT, and financial analysis to understand its quest for sustainable product-market fit amid Apple Music's entry. It highlights Spotify's reliance on the freemium model, balancing user acquisition and profitability while managing rising licensing costs and artist dissatisfaction. Insights include the critical role of free-to-premium conversion, pricing strategies, innovation and marketing tools. By analyzing consumer behavior, market dynamics, and the evolving digital music landscape, the study reveals strategies for surviving in a highly competitive market and adapting business models to ensure sustainable growth amidst constant industry transformation.

Abstract Individual Part

In 2015, Spotify faced challenges in its pricing strategy due to high licensing costs, competition from Apple Music, and a low conversion rate from freemium to premium users. The company operated on a freemium model, but with 70% of its revenue directed towards royalties, profitability remained a significant issue. To improve Average Revenue Per User (ARPU) and achieve financial sustainability, Spotify could explore several adaptive pricing strategies, including tiered pricing, regional pricing, and usage-based models. Additionally, employing psychological pricing techniques, offering bundled services, and providing discounts could help increase user conversions. By implementing these strategies, Spotify can optimize its revenue while maintaining a competitive edge in the ever-evolving music streaming market.

Keywords

FREEMIUM BUSINESS MODEL

FREE-TO-PREMIUM CONVERSION

PRODUCT-MARKET FIT

CONSUMER BEHAVIOUR

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1. Case Study Situation

It was a typical early morning in Stockholm on 8 June 2015, with a grey blanket of clouds hanging over the city, accompanied by a light drizzle against the windows. Daniel Ek, the CEO of Spotify, was in his minimalist office, wearing his usual casual outfit of jeans and a plain black T-shirt. His closely shaved head and neatly trimmed beard gave him an intense appearance. A steaming mug of strong black coffee sat on his desk, the steam mingling with the scent of rain wafting through a slightly open window.

His mobile phone buzzed loudly, breaking the silence. A headline on the screen read, "Introducing Apple Music: All The Ways You Love Music. All in one place." The rumours had been circulating for months, but now it was there in front of him, undeniable. At the recent Worldwide Developers Conference, Apple announced the launch of Apple Music. With a three-month free trial followed by a \$9.99 monthly fee, it was clearly gearing up to take on Spotify. Apple wasn't just launching a streaming service; it was tapping into its vast ecosystem to offer seamless integration with iOS devices and artist friendly features like Beats 1 Radio and Apple Music Connect (Apple 2015).

His stomach twisted with a mixture of fear as he tried to comprehend what was about to unfold. This wasn't just a challenge - it was a declaration of war. He took a slow sip of his coffee, allowing the bitterness of the drink to sharpen his focus. Apple wasn't there to play, not with billions in cash reserves and direct access to hundreds of millions of iPhone users. It was there to conquer, and Daniel understood that Spotify was in a delicate position despite its success. It had grown impressively under his leadership: 75 million users worldwide, but only 20 million paying subscribers (Statista 2024g). The rest enjoyed it for free, while Spotify's costs, especially music licensing, continued to skyrocket (Statista 2024i). The company relied on advertising revenue, but this was barely enough to cover its costs (Hugh McIntyre and Forbes 2014).

Moreover, with Apple entering the competition, Daniel felt he had a ticking time bomb on his hands. How would Spotify survive this battle?

He leaned back in his chair and watched the raindrops make their way across the glass. Ek could feel the walls closing in, the pressure building from all sides. The investors, who had been patient, perhaps too patient, were eager for returns and worried about the competition. Spotify had been the darling of the tech world, but the profitability was still a key question that was raised on every board meeting. Now the calls were louder, the demands greater: "Where's the profit, Daniel?".

But it wasn't just the investors. The very listeners who had driven Spotify's phenomenal growth were a double-edged sword: years of piracy via services like Napster had created a generation that believed music had a right to be free. Thus, millions of users were streaming on Spotify endlessly without spending a penny. Now, the slightest hint of opening their wallets sent them running since these users resisted the idea of paying for something they had long taken for granted.

Artists' voices also were growing louder. Taylor Swift pulled her entire catalog from the service the year before, attacking on the freemium model: "I'm not willing to contribute my life's work to an experiment that I don't feel fairly compensates the writers, producers, artists and creators of this music, and I just don't agree with perpetuating the idea that music has no value and should be free (Kevin Noonan and Variety 2014)." She was not alone. A whisper among artists about unfair deals had turned into accusations for devaluing their work.

A new giant appeared on the horizon. Apple was entering the arena, with Drake and Pharrell as its leading ambassadors. This wasn't just about launching a competing service; the tech giant was about to change the game completely. Spotify's freemium model was about to face its

biggest challenge yet, and Daniel could feel the pressure building. The stakes had never been higher, and the future of his company was at risk.

Memories he had long tried to keep at bay began to resurface unexpectedly. They took him back to his younger years - the time when everything he had built was on the verge of collapse. In his late teens and early twenties, he had been a reckless entrepreneur, launching a series of tech ventures with the naive optimism of youth, without a clue about the importance of financial planning. He recalled the suffocating feeling when he received the letter from the Swedish tax authorities detailing the massive debt he owed. The fear, the shame, and the crushing realization that he could lose everything he had worked tirelessly to build. Years later, as CEO of Spotify, those same fears returned with even greater intensity. Spotify was no longer a small startup; it had grown into an international tech company with more than 1,500 employees. Each of them had their own stories, families, and dreams tied to the success of the company they were building from scratch. The thought of letting them down was almost unbearable...

2. Industry Background

2.1 The Global Music Industry Transformed By Streaming.

In 2015, the global music industry underwent a major transformation with the rapid rise of digital streaming platforms. As consumers shifted from owning music to accessing it, these platforms gained popularity by providing instant access to music libraries for affordable subscriptions and free ad-supported options. This shift not only lowered production and distribution costs for record labels and artists, but also gave listeners a more flexible and convenient alternative to purchasing physical formats or digital downloads (IFPI 2015). It was the year when global digital revenues exceeded physical sales for the first time. Digital sales reached \$11.7 billion, while physical sales were \$10.3 billion. In 2014, subscription revenues grew 39% and accounted for 23% of global digital revenues, up from 18% the previous year (See Figure 1).

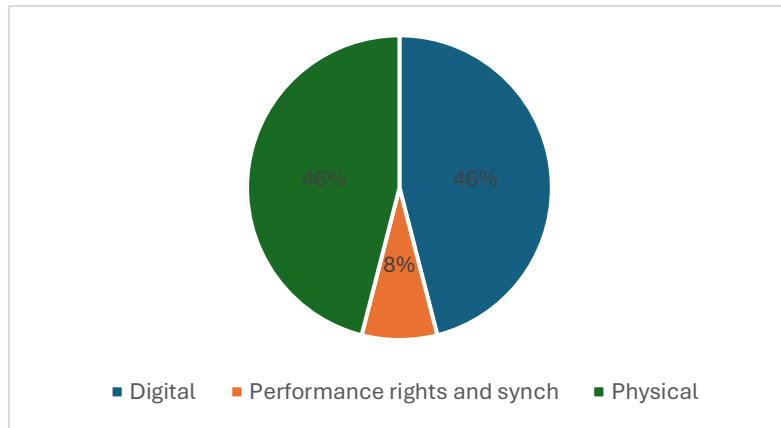


Figure 1. Share of Industry Revenues 2014. Source: IFPI 2015.

As shown in Figure 2, the number of paying subscribers also grew sharply, reaching 41 million in 2014, up from 28 million in 2013 and 8 million in 2010 (IFPI 2015). Although downloads still accounted for 53% of global digital revenues, they experienced an 8% decline in 2014. The rapid adoption of Android smartphones and tablets was partly responsible for the decline. However, the strength of physical format sales varied from country to country. In markets such as Germany (70%), Japan (78%) and France (57%), physical sales remained dominant. In addition, vinyl records, though still a niche, experienced a comeback, with sales growing 54.7% in 2014 and accounting for 2% of global music revenues (IFPI 2015).

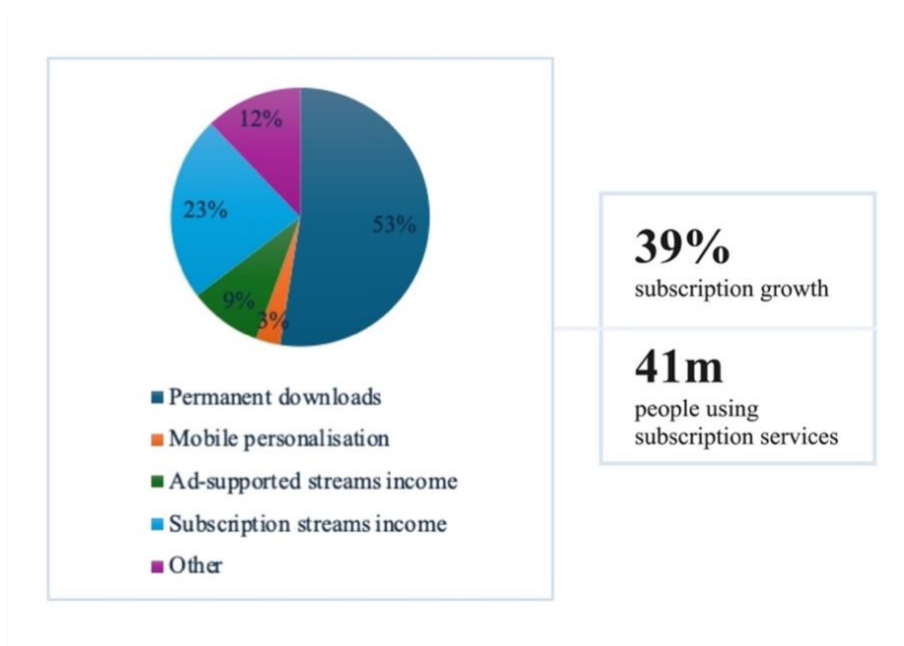


Figure 2. Global Digital Revenues by Sector (2014). Source: IFPI 2015.

Piracy remains a significant problem, with 20% of the world's wired Internet users regularly accessing services that offer copyrighted music, and 4 billion music downloads occurring through BitTorrent alone. Ipsos research across 13 countries found that 52% of respondents consider unauthorized downloading or streaming to be theft. In addition, 53% believe that licensed services should rank higher than pirate sites in search engine results, 52% believe that companies should avoid advertising on pirate sites, and 43% believe that ISPs should take more responsibility for preventing illegal music distribution (IFPI 2015).

2.2 Surviving the Streaming Wars.

In 2015, the streaming music services market could be broadly divided into two main categories: on-demand services and digital radio, as you can see on the Table 1.

Table 1. On-demand and Digital Radio Services

Category	Description	Examples	Additional notes
On-demand services	Allows users to select specific songs or albums for playback; available in paid and free versions.	Paid: Spotify Premium, Apple Music, Rhapsody, Tidal Free: YouTube, Spotify Free, Vevo	RIAA revenue includes some revenue from premium internet radio services (e.g., Pandora One).
Digital radio	Streams curated playlists or stations based on user preferences without allowing track selection.	Internet Radio: Pandora (free), iTunes Radio Other: Satellite radio, pay-TV music channels	Different monetization approach compared to on-demand services.

Source: Bill Rosenblatt and Forbes 2016.

Competition is fierce globally, but attention is now turning to the key players that are either entering new markets or strengthening the ones they already occupy (IFPI 2015). While some players were flourishing, others encountered considerable obstacles. Table 2 provides an overview of the key players.

Table 2. Overview of Key Players

Company	Overview	Details
Apple	Enters the streaming market.	Acquired Beats for \$3 billion in early 2015; launched Apple Music by integrating Beats Music into iOS, leveraging 800 million credit card accounts.
Rdio	Files for bankruptcy.	Rdio, a competitor to Spotify, filed for bankruptcy with \$220 million in liabilities; assets acquired by Pandora for \$75 million.
Deezer	Postpones IPO.	Deezer postponed IPO after investors rejected its \$1.1 billion valuation, raising concerns about its financial stability.

Tidal	Faces criticism.	Purchased by Jay Z for \$56 million; faced criticism for its artist-friendly positioning as a populist money grab. Still achieved 1 million subscribers despite challenges.
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Source: Ben Sisario and NYT 2015.

2.3 Apple Music's Bold Entry to Challenge Spotify.

At the 2015 Worldwide Developers Conference in San Francisco, Tim Cook announced Apple Music. The launch marks the successful integration of the Beats Music streaming service into the Apple ecosystem. While iTunes sales continue to perform well, revenue from downloads has declined, presenting a prime opportunity for Apple to move into the streaming market. During the WWDC event, Apple CEO Tim Cook urged attendees to consider subscribing to the service rather than buying individual tracks, pointing out that a month of streaming costs the same as a single album on iTunes (Amanda Schupak and CBS News 2015).

Apple Music gives users access to a huge library of over 30 million songs, as well as the ability to play their own music library and custom playlists whenever they want. However, the company emphasizes that the true essence of Apple Music lies in the curated playlists created by Apple's music experts. The app is designed to adapt to your preferences, presenting albums, playlists and new releases tailored to your musical tastes in the 'For You' section. Siri is also integrated into the platform, allowing you to use voice commands such as "Play me the best songs from 1994" or "What was the song from Selma?" to find specific tracks to play (Amanda Schupak and CBS News 2015). See Table 3 for the overview of the other main features.

Table 3. Overview of Apple Music's Main Features

Feature	Details
Streaming service	Access to over 30 million songs; ability to stream unlimited music on multiple devices.
Music library and playlists	Includes a huge library of 30 million songs and allows users to play their own library and custom playlists.
Curated playlists	Curated playlists created by Apple's music experts, tailored to user preferences in the 'For You' section.
Siri integration	Voice commands via Siri to find and play specific tracks (e.g., 'Play me the best songs from 1994').
Apple Music Radio	24-hour live radio broadcasting to 100 countries with curated genre-based stations and handpicked DJs.
Apple Music Connect	Platform for artists to share updates, lyrics, backstage photos, exclusive videos, and unreleased tracks; fans can comment, like, and share.

Source: Amanda Schupak and CBS News 2015.

Regarding pricing, a monthly subscription to Apple Music is available for \$9.99 on iPhone, iPad, iPod Touch, Mac, and PC starting June 30. The Apple TV and Android versions are supposed to release in the autumn. Apple is offering the first three months free and has a family plan for \$14.99 a month for up to six users (Amanda Schupak and CBS News 2015).

2.4 Artists Rebel Against the Current System.

The growth of streaming platforms in 2015 also resulted in rising tensions between platforms like Spotify and artists, particularly due to concerns over low royalty payouts. The criticism of streaming platforms was not limited to Taylor Swift only. Her decision has further intensified industry debates about the sustainability of freemium models. Radiohead's Thom Yorke previously described Spotify as "the last desperate fart of a dying corpse." The overwhelming consensus among musicians is that they are underpaid by these services. Artists often argue that the low per-stream payouts from on-demand platforms undervalue their hard work and make it difficult to earn a sustainable income (Jason Koransky and ABA 2016).

The fundamental issue at the heart of the dispute was the considerable gap between the perceived value of music and the low per-stream remuneration. For instance, Spotify paid rates ranging from \$0.006 to \$0.0084 per stream, a figure that was considerably lower than the revenue streams available to artists through album sales or digital downloads (Bill Rosenblatt and Forbes 2016).

3. Company History

3.1 The Birth of a Giant

The way of listening to music today is totally different. With just three tools (smartphone, internet, headphones) you can have access to an infinite amount of music. All in a few simple seconds, in just a few gestures. Spotify is not simply a streaming music platform, but a real technological revolution that owes its success to several factors. With program-based targeting and cutting-edge advertising technologies, Spotify has revolutionized music access and the way that the general public listens to music through its platform model and subscription-based business model (Vonderau 2019).

To fully understand Spotify's impact on the music industry, it is worth investigating the origins of the platform, how it came into being and what its main purpose was. The idea of creating a platform like Spotify came from Daniel Ek with the aim of eliminating piracy in the music industry by offering a legal and affordable alternative. In the 2000s, it was very easy to be able to download music illegally, and this was because of the rather high cost of buying a CD. Against this backdrop, Daniel saw an opportunity to be able to create a service that offered an unlimited catalog of tracks on affordable terms. In this way, it was possible to combine the co-founder's two main passions: music and technology (Redazione Cutowl 2022).

Daniel envisioned music as a journey of constant discovery, where users could explore new songs, expand their tastes, and enjoy diverse musical genres. At its core, Spotify aimed to combat the piracy that disrupted the music industry in the early 2000s (Marino 2023).

Spotify's mission was shaped by the rise of piracy in the late 1990s and early 2000s. In 1999, Napster introduced digital music sharing, allowing users to trade and download music peer-to-peer for free, bypassing traditional album sales. Clearly, this business violated copyright rights, resulting in piracy. Despite the illegal intervention on the music industry landscape, Napster

gained great popularity very quickly and its success led to a revenue loss of as much as \$2 billion from 1999 to 2002. Daniel was convinced that if music was easily accessible and enjoyable for free, users would become regular listeners and eventually be willing to pay for a streaming service (Marino 2023).

Despite artists and record companies were sceptical, Daniel believed that offering a better user experience would persuade customers to switch from free to paid memberships (Robert Safian 2018). He hoped that by providing this avenue, musicians would be able to reach a larger audience and discover new revenue streams. To win over artists and labels, he needed to demonstrate that the internet could greatly benefit their businesses rather than pose a challenge. Spotify could be a platform that benefited everyone, particularly the musicians who produce the music, by collaborating with the industry and providing a steady business model through advertising and subscriptions.

In 2006, Daniel Ek partnered with Martin Lorentzon to found Spotify in Stockholm, Sweden. Both co-founders came from the background of advertisement technology (Marino 2023). Lorentzon made money from affiliate marketing with TradeDoubler, gaining expertise and notoriety in the entrepreneurial world. By investigating the origins of the platform, it is possible to discover that Spotify is a macedonia word between “spot” and “identify” (Wikipedia 2024). The primary challenge for the founders was securing licenses from major music rights holders. Their goal was to establish strong partnerships with artists and record companies, ensuring fair revenue distribution. They needed to show them that the internet could be a huge help to their business, not a problem. By joining forces with the industry and offering a sustainable revenue model through advertising and subscriptions, Ek aimed to show that Spotify could be a platform that benefited everyone, especially the artists who create the music (Sarah Lacy and Startups.com, n.d.).

Spotify launched in October 2008 and quickly struck a chord with users who appreciated its seamless music experience. Despite initial research suggesting that people wouldn't pay for music access, Ek's strategy proved successful. Users were willing to pay for the convenience and quality that Spotify offered. Within its first year, the platform gained millions of users and hundreds of thousands of paying subscribers. Even before its official U.S. launch in 2011, Spotify had already developed a cult following among American tech influencers (Robert Safian 2018).

The mission of Spotify extended beyond building a successful business. By focusing on user experience, accessibility, and industry collaboration, Daniel sought to create a platform that could grow the industry and benefit everyone involved. He believed that the evolution of the internet could not only stabilize the music business but also lead to its growth. In essence, his values centre around innovation, a passion for music, and technology for positive change. Through perseverance and a willingness to challenge conventional thinking, Ek has led Spotify to become a global force, fundamentally changing how the world listens to and values music (Robert Safian 2018).

3.2 Spotify's Freemium Business Model

Spotify's choice of business model was conditioned by the need to find a dynamic paradigm that could adapt to changes in the phonographic industry and new modes of consumption. Unlike piracy sites like Napster, Spotify had license deals with major music labels. These license arrangements allowed to legally supply customers with copyrighted music from a number of renowned artists, including Coldplay, Miles Davis, Frank Sinatra, Madonna, and Snoop Dogg (Schmid & Romey 2022).

As shown in the Table 4 Spotify consented to give the major labels equity holdings to lower the amount of royalties paid to them. Since the music industry was suffering severe revenue losses due to piracy, most record companies had finally signed licensing agreements with Spotify. The

decision to affiliate with Spotify was due to increased use of smartphones and the Internet, and the platform would have the strength and ability to create a positive consumer experience (Schmid & Tobias, 2022).

Table 4. Record Label Ownership of Spotify Shares in 2009

Record Label	Shares in Spotify (2009)
Sony BMG	5.8%
Universal	4.8%
Warner	3.8%
EMI	1.9%
Total	16.3%

Source: Schmid & Tobias, 2022.

The business model on which Spotify was formed was dictated by two basic factors: offering a free platform and a premium version. When analyzing the causes that prompted Spotify to adopt this business model, the desire to want to allow anyone to enjoy a free service and formulate a value proposition that could meet the needs of a variety of consumers with different needs and different music tastes certainly stands out. The factors that drove Spotify to undertake this business model always lay in the fight against piracy. Free accounts were available only through an invitation, while paid subscriptions were available to everyone. The strategy implemented by the founders is related to growth hacking and customers acquisition and conversion (Azzalin 2018).

The key role in Spotify's steady growth has been played by its business model and investment in advertising. The key to the platform's success was certainly the founders' ability to exploit the external environment (the macro environment) as a starting point to end the music industry crisis due to piracy. Unlike earlier models, in which music was paid per track or album, Spotify's freemium model allows users to access millions of tunes for free in exchange for listening to commercials while playing. The role of such a business model is certainly to attract as many users as possible and increase registered users (Azzalin 2018).

To properly analyze Spotify, it is therefore necessary to understand its logic behind the different strategies the platform has put in place to achieve such success. See Table 5 for the company’s timeline.

Table 5. Timeline of Spotify's Milestones

Year	Milestone	Key Strategy
2008	Formal introduction in Europe	Focused on cutting-edge features, intuitive user interface, and tailored playlists to attract users.
2011	Entry into the US market	Resolved complex licensing agreements with major record companies to launch in a new market.
2013	Integration with mobile devices	Expanded accessibility to the platform, increasing the user base.

Source: Vonderau 2019.

As the company expanded, the focus changed to subscriptions as the principal source of revenue. The freemium model, in which users could listen to music for free with advertisements or pay for an ad-free experience, was key to Spotify's success. This approach used an ad-supported version to attract users who may not be willing to pay right away, with the option to upgrade to a paid subscription later. Spotify is described as a "two-sided market" or platform that connects advertisers and users (Vonderau 2019).

3.3 Financialization of Spotify

One of the early backers of the Spotify platform was Sean Parker, the founder of Napster, who allocated as much as 15 million in investment to rapidly grow the Swedish startup (Possagnolo 2022). As shown on Figure 3, Spotify raised \$1.6 billion in seven rounds of funding. To gain greater credibility, during this period, the company attracted big stakeholders such as Coca-Cola, Goldman Sachs, and several venture capital firms (Schmid & Romey 2022).

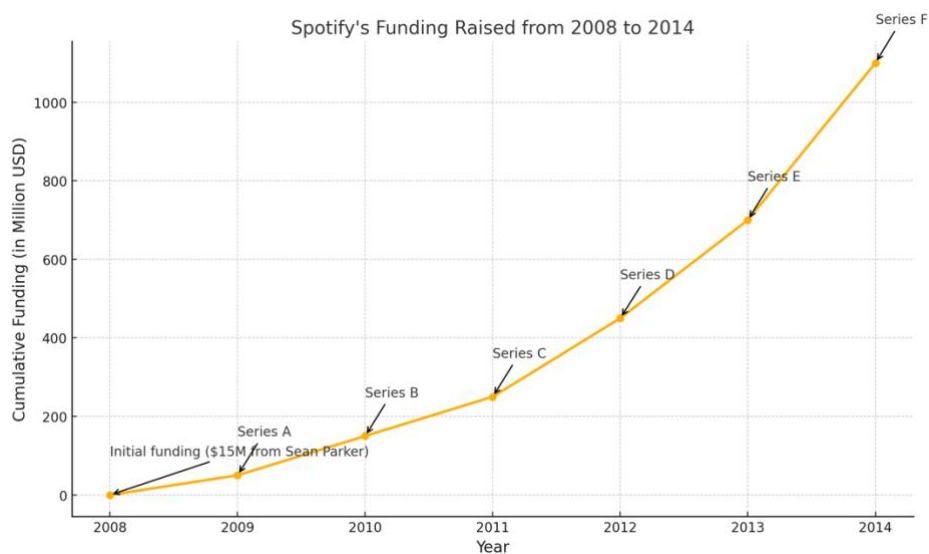


Figure 3. Spotify's Funding Raised from 2008 to 2014. Source: Possagnolo 2022; Schmid & Romey 2022.

While this infusion of finance allowed Spotify to expand quickly and remain operational, it also generated an underlying demand for ongoing user growth. Investors had high expectations for the company's price, prompting Spotify to expand its user base and investigate additional revenue streams to justify its financial position. Venture financing was crucial in defining Spotify's business strategy. Unlike traditional businesses, which prioritize quick profitability, the venture capital model focuses on rapid expansion and market dominance, frequently at the price of short-term earnings. This strategy was common among tech companies, where the primary focus was on growing a large user base and generating a compelling story about future income prospects (Vonderau 2019).

Spotify made the concept of "future income streams" a key part of their investor appeal. The company positioned itself as capable of consistently generating revenues by growing its user base, capitalizing on advances in advertising technology, and introducing new services. This story of growth and promise was essential in increasing the company's valuation, reflecting a business model that was less about immediate financial returns and more about predicting long-term profitability and market leadership (Vonderau 2019).

3.4 Spotify's Global Expansion and User Acquisition

See Table 6 for a timeline of Spotify's expansion worldwide. The service was initially offered in a few European nations. These early areas were carefully selected; Sweden, the home nation of Spotify, was a perfect testing ground due to its high internet penetration rate and tech-savvy populace. Launching in the UK, one of the biggest music marketplaces globally (Verma 2015), was also a calculated move that gave the business a chance to make a name for itself in a cutthroat field. Freemium business model reduced the barrier to entry for consumers accustomed to free, albeit illicit, music-sharing techniques, which was crucial for its success in emerging economies (Verma 2015).

Table 6. Spotify's Global Expansion 2008-2015

Year	Region	Details
2008-2010	Initial European Launch	Launched in Sweden, UK, France, Spain, Norway, and Finland. Adopted a 'freemium' business model combining free ad-supported and paid subscriptions. Secured licensing deals with major record labels. By 2010, expanded to the Netherlands, Denmark, Austria, and Belgium.
2011	Entry into the U.S. Market	Entered the highly competitive U.S. market in July 2011. Negotiated deals with Universal, Sony, Warner, and EMI to secure a broad catalog. Partnered with Facebook for social media integration. Reached 1 million U.S. users within months.
2012-2015	Rapid Global Expansion	Expanded into Australia, New Zealand (2012), Latin America (Argentina, Bolivia, Chile, 2013), and Asia-Pacific (Malaysia, Hong Kong, Singapore, etc., 2013). Partnered with local telecoms like Globe Telecom in the Philippines to bundle Spotify with data plans, overcoming data consumption barriers. Expanded into key European areas such as Italy, Poland, Portugal, and Iceland.

Source: Possagnolo 2022; Verma 2015

Spotify's entry into the United States market in July 2011 was one of its most significant accomplishments. By this point, the company had established itself as a major player in Europe, with over 10 million users and approximately 1 million paid members. However, the American music market was very competitive, dominated by players such as Apple's iTunes, and governed by intricate license arrangements. The agreements with record labels and partnerships were critical for acquiring a broad catalog that could compete with existing businesses. For example, a partnership with Facebook that was allowing users to directly share what they were listening to with their friends, was critical in swiftly boosting Spotify's U.S. user base, allowing the firm to achieve 1 million users in the country within its first few months (Schmid & Romey 2022)

After making its entry into the United States and Europe, the service was launched in emerging countries due to higher use of smartphones. Spotify's strategy in these areas frequently included agreements with local telecoms firms. For example, in the Philippines, Spotify collaborated with Globe Telecom to bundle its service with mobile data plans, allowing customers to sample the platform without worrying about data charges. These agreements helped Spotify overcome

possible barriers associated with data consumption concerns, making it easier to obtain (Mix of Everything 2015).

4. Status of Spotify in 2015

In 2015 Spotify has reached over 75 million users worldwide, a loyal user community and a solid brand identity as a go-to platform for digital music streaming (Wagner, Benlian, and Hess 2014). However, Spotify's success came with significant challenges, notably its struggle to achieve profitability. While the freemium model was key for attracting users, only approximately 20 million of Spotify's 75 million users were paying subscribers, i.e. most of its user base was in the free tier and was generating ad revenue only. The difference between the number of revenues collected from free users and the number of revenues collected from premium users caused a substantial gap between revenue. As a result, Spotify faced the complex challenge of monetizing a massive base of free-tier users without alienating them. This delicate balance became even more challenging as competition intensified (Yngvar 2016).

The freemium model, although successful at growth, came at a high cost. Although Spotify platform free users generated a much lower revenue compared to premium users, primarily because of advertising hits (Mäntymäki, Islam, and Benbasat 2020). Due to a lack of sufficient advertising revenues to cover the high costs associated with music licensing, Spotify's financial model was disastrous (Sletten 2021). In 2015, Spotify was required to pay record labels, artists, and songwriters significant royalties based on music streams, regardless of whether the listener was on a free or premium plan (Hesmondhalgh et al 2021).

This financial strain was exacerbated as Spotify grew. As more users streamed music, Spotify's licensing costs rose, and the model produced a profitability paradox. While increased users were beneficial for brand exposure and business reach, they led to an uptick in financial strain, especially when the users were not paying subscribers (Richardson 2014).

In addition to external competition, investor expectations were mounting. Spotify had been relying on venture capital to drive its growth, but as of 2015, investors were asking for more concrete profitability indicators. Amplifying pattern of losses despite the rising of revenue created ambiguity as to whether Spotify's freemium business model may be sustainable for the period beyond the short term (Mei 2024).

Investors looked for proof that eventually Spotify could grow a bigger number of free listeners to paying subscribers or that it could rely on a new revenue stream to make up for the cost of its licensing. Low conversion rates and high licensing costs associated with the freemium model created a daunting prospect for potential profitability (Mai Hu 2023). Supporting competitive pressure from Apple Music's model of solely paid subscription and addressing investor concerns, Spotify found itself on the cusp of 2015, and growth-fuelled strategy met its challenge of sustainable financials (Mok 2022). Apple Music's market entry sparked investor worries about the long term sustainability of Spotify. The competitor's subscription-only model and proprietary release of top artists' work (e.g., Taylor Swift and Drake) created an explicit competitive pressure on Spotify's user acquisition plan (Scharf, 2022).

4.1 High Cost of Music Licensing

Spotify's dependence on music licensing agreements was an important ingredient in explaining its financial difficulties. Unlike traditional record labels or music distributors, Spotify did not own the music it streamed, which meant it relied on deals with record labels, music publishers, and artists to make its platform viable. Based on these licensing terms, Spotify was required to pay royalties for every piece of music played whether the recipient was free or premium (Savoia 2021).

Global revenues for Spotify amounted to the impressive figure of 1,084€ million 2014, largely because of growth in the user base and premium subscribers (Statista 2024). However, as revenue rose, so did its licensing costs. Spotify's net losses continued to increase to nearly 225€

M at the end of 2015, mostly due to licensing increases that followed user increases, an uncompensated growth phenomenon. This paradoxical effect of growth (increasing number of users on the free tier resulted in higher and higher licensing dues but not higher revenue) made it hard for Spotify to narrow the profitability deficit (SEC 2018).

In response to increasing financial pressures and investor expectations, Spotify is negotiating with rights holders in an effort to improve their negotiating power and obtain more favorable licensing conditions. The objective is to decrease the amount of revenue that it paid to record labels and publishers, which in turn might allow it to keep more of its revenue and profitability (Ramos&Blind 2022). Nevertheless, these negotiations were difficult because music industry revenues have been declining for the last 10 years.

Such companies as Universal Music Group, Sony Music, and Warner Music Group are controlling a significant portion of Spotify's catalogue, which gives them considerable leverage in negotiations. This limited bargaining power is adding complexities to Spotify's status (Prey, Esteve Del Valle, & Zwerwer 2020)

4.2 The ARPU Decline

Spotify's Average Revenue Per User (ARPU) was another concern. As it expanded into new regions, particularly emerging markets where it needed to charge lower subscription fees, ARPU began to decline. In Latin America and Southeast Asia, Spotify, in contributing to local market conditions, provided significantly reduced subscription costs to gain on premium user revenue (Threechownon 2021). While successful in boosting user acquisition globally, this pricing strategy exacerbated profitability issues as it lowered the overall average revenue per paying subscriber.

Moreover, Spotify's ARPU dropped by approximately 12% from 2014 to 2015, a concerning trend given that the company's financial model relied heavily on converting free-tier users to premium. With the addition of more users from areas that required low pricing, Spotify's

revenue per user decreased and exerted further pressure on Spotify to look for other sources of revenue or to renegotiate its licensing contracts (SEC 2018)

However, for Spotify to expand into new markets, it needed to adjust its pricing to match the economic situation of the new territories it gained access to, hence impacting ARPU. As shown in the Figure 4, in Brazil, India, and Indonesia, Spotify offered lower subscription prices to make a pitch to a society that is accustomed to affordable goods. While this pricing model supported the growth in the number of users rapidly, it also reduced the ARPU in the countries under review compared to premium markets, such as in the US and the Western Europe (Schmid Romey 2021).

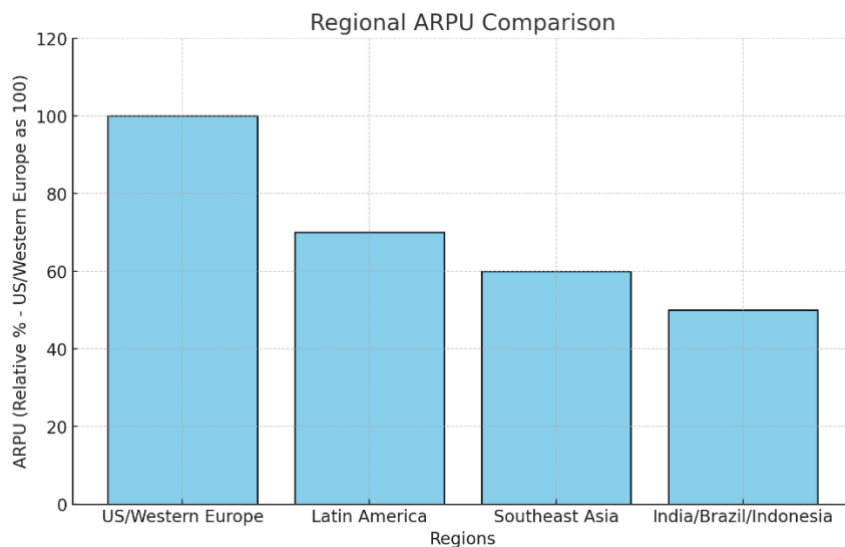


Figure 4. Spotify’s regional ARPU Comparison. Source: Schmid Romey 2021

Despite the increase in users from emerging markets, the decline in ARPU meant that Spotify faced the challenge of maintaining a profitable balance. However, for example, as Spotify grew its premium subscriber base worldwide, the lower subscription price points in some markets put downward pressure on overall Spotify revenue. These further complicated efforts to achieve profitability, as the company now had to explore alternative revenue streams and optimize its advertising model to offset the revenue loss from regional price adjustments (Ramos Blind 2022). See Table 7 for Spotify’s metrics.

Table 7. Spotify’s Metrics in 2015

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Metric	Q1 (2015)
Monthly Active Users (MAUs)	68 million
Premium Subscribers	18 million
Ad-Supported MAUs	51 million
Content Hours Consumed	3.7 billion hours

Sources: SEC (U.S. Securities and Exchange Commission). 2018. Form F-1 Registration Statement for Spotify Technology S.A

Notes:

- Monthly Active Users (MAUs) include both premium subscribers and ad-supported users.
- The Ad-Supported MAUs category represents users utilizing Spotify's free tier.
- Content consumption refers to the total hours users spent streaming on Spotify each quarter, reflecting user engagement.

4.3 The Challenge of Monetizing Free Users

A vital issue undermining Spotify's profitability was the vast revenue discrepancy between its two user groups: free-tier users and premium subscribers (Sletten 2021). The revenue generated from free users primarily came from advertising, yet this income was notably lower than the subscription fees collected from premium users.

Spotify's difficulties monetizing its large base of free users compounded its financial pressures. Although Spotify pioneered streaming and established a solid advertising infrastructure, it faced challenges in growing its ad revenue at a rate that would sustain its business. The digital advertising market was highly competitive at that time, with platforms like Pandora also vying for a share of ad dollars. Audio ads, Spotify's major revenue stream for free users, typically yield less engagement and advertising tracking capabilities than other ads (video or display) favored by advertisers on platforms like Facebook and Google (Carraro 2022). By 2015 Spotify's advertising revenues made up less than 10% of all revenue (a small amount in comparison with ad-led companies such as YouTube, which used video advertising to much greater benefit. See Appendix A for the company's financial metrics in 2015.

Migrating from free tier to premium was a major objective for Spotify. By 2015, around 26% of Spotify's total users were premium subscribers, a rate higher than some competitors but still

insufficient to compensate for free users' low revenue (Sletten 2021). Conversion rate improvements became a focus for Spotify, as they directly impacted the company's ability to generate consistent income from its user base. Spotify also contemplated to introduce tiered functionalities with premium conversion incentives like offline listening, ad-free streaming or exclusive content to increase the participation rate (Wagner, Benlian, and Hess 2014).

4.4 Spotify's Tiers and Features

Spotify offers two plans: Free and Premium. The Free tier offers basic access with ads, standard audio quality, shuffle-only playback on mobile devices, and a limited number of skips. The Premium tier offers an ad-free experience, superior audio quality, offline listening, unlimited skips, and access across multiple devices. Premium subscribers also enjoy unique features such as personalized playlists, Discover Weekly, Running Mode, and access to video and podcast content. See Table 9 below for a detailed comparison of the two plans.

Table 9. Spotify's Free and Premium features in 2015

Feature	Free Tier	Premium Tier
Ads	Contains ads (up to 6 times in a row every 5-8 songs)	Ad-free listening
Audio quality	Standard audio quality	Higher audio quality
Playback mode	On-demand playback on desktop/web; shuffle-only on mobile	On-demand playback on both desktop and mobile
Skips	Six skips per hour on mobile	Unlimited skips
Offline listening	Not available	Available (up to 10,000 songs)
Cross-device access	Not available	Available (up to 5 devices)
Exclusive features	Basic personalization with access to Discover Weekly and curated playlists; no additional exclusive features.	Enhanced personalization with Taste Profiles, daily routine-based playlists such as Wake Up Happy, user-created playlists with community engagement, personalized Discover Weekly, Running Mode for fitness enthusiasts, video and podcast content with partnerships like ESPN and BBC.

Sources: Bill Rosenblatt 2015; Josh Constine 2014; Jordan Crook 2015; Sam Thielman 2015; Stuart Dredge 2015; Spotify Community 2014.

In addition to technological features, the platform had social networking features that were controversial. Some users appreciate them as a new way to connect with others through music, while others question their effectiveness. Proponents see features like these as valuable tools for building community and discovering new music. On the other hand, critics state they are

underutilized and lack the engagement and depth in contrast with traditional social media platforms. Some users feel that the platform's efforts to incorporate social elements fail to create a truly interactive experience. In addition, the visibility of listening habits can feel invasive to some, raising privacy concerns (Paul Ford and The new republic 2015).

Spotify notes that mobile devices now account for the majority of listening among its users, demonstrating the growing trend of music consumption on the go. Specifically, 42% of listening takes place on smartphones and 10% on tablets. In contrast, desktop software accounts for 45% of listening. The web player accounts for just 3% (Josh Constine and TechCrunch 2015).

Alongside the music streaming itself, the platform also offered a forum, which was created to give users a dedicated space to help each other, discuss music and give feedback on the product. The Spotify Community was launched on 8 February 2012, replacing the former GetSatisfaction site (Spotify Community 2022).

4.5 Advertising Technology

Spotify's ad-supported tier was built on the foundation of programmatic advertising, a complex technology that uses real-time bidding to buy ad space. Advertisers may use this technology to efficiently target consumers based on a variety of data points, including demographic information such as age and location, music tastes, and even inferred moods based on the playlists they choose. In this structure, advertisements are regarded similarly to commodities in financial markets, where transactions are frictionless and quick. Spotify collaborated with a network of SSPs, DSPs, and Ad Exchanges to make this process easier. This cooperation enabled Spotify to increase the efficiency of its ad inventory by guaranteeing that each ad spot was used and sold to the highest bidder in an automated, simplified manner.

In fact, the platform allows advertisers to segment audiences based on demographics such as age, gender and location and through listening behaviour. For example, advertisers can decide to show their advertising only to certain segments of users who listen to that particular genre of

music or at specific times of the day. The more data that can be collected, the more precise and specific advertisers can be. Despite the vast amount of data available to Spotify, the system encountered significant hurdles in ad efficiency.

Initially, Spotify had a limited number of ads (1-3 at a time) during Free tier listening, with ads spaced every few songs, which many users found tolerable. However, according to user feedback in 2014, Spotify began introducing longer commercial breaks, sometimes with up to 6 ads in a row which drew criticism from free-tier users. They expressed frustration with describing ad placements as annoying and excessive. Premium subscribers, on the other hand, were often supportive of the increase in ads. As one user noted, "As a premium user, I'm glad they're increasing ads instead of increasing monthly fees..." This indicates that Premium users view the increase in ads as a reasonable trade-off to keep subscription costs down (Reddit 2014; Spotify Community 2014).

4.6 User Segmentation by Different Markets

Spotify's global market can be divided into four key regions: Europe, North America, Latin America and the Rest of the World. In Europe, the service has the largest presence in the UK: 56% of digital music users prefer curated playlists, smartphone use, and genres such as pop and rock. In North America, the U.S., with 44% of users, likes content discovery and personalized features, especially among Gen Z users. Latin America, with Brazil's 68% user share, highlights a younger, urban demographic that is passionate about gaming and discovering new content. Meanwhile, India, representing the rest of the world with 62% engagement, is characterized by its premium audio preferences, tech-savvy users and high receptivity to new features (Statista 2024f). See Appendix B below for a detailed overview of each region.

5. Daniel Ek, the Co-founder and CEO of Spotify

5.1 The Early Entrepreneurial Journey

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Daniel Ek is a co-founder and CEO of Spotify, a major figure in both the music and technology industries. Born in Stockholm, Sweden in 1983, he discovered his love of technology early on and often reflects on how his childhood influenced his connection to both technology and music. In the late 1990s, Sweden had fixed broadband with speeds of around 10 megabits per second, allowing him to explore platforms like Napster early on. This access to fast Internet allowed Daniel to discover music from all over the world. Thus, he found himself trusting complete strangers who shared music online and exploring vast number of new songs and artists through peer-to-peer connections (Sarah Lacy and Startups.com, n.d.).

The entrepreneurial journey of Daniel began when he was just 14 years old. He was already programming in C++, HTML and CGI. In the late 1990s, there was a huge demand for websites, and in Sweden, companies were charging around \$50,000 for a basic two-page site. Daniel saw an opportunity and started making websites for just \$100. He raised his prices, eventually charging up to \$5,000 for a website. By then, while still in school, he had more clients than he could manage (Sarah Lacy and Startups.com, n.d.).

As the demand for his website building services grew, he realized that he needed to expand his skills. He taught himself and his classmates Photoshop to help him to process the clients' requests. Interestingly, instead of offering cash, he was paying with items like iPods, mobile phones and video games that were more valuable to his young employees. At the time Daniel was earning close to \$50,000 a month (Sarah Lacy and Startups.com, n.d.).

Around this time, Ek began to take on bigger projects, building SEO and SEM businesses and seeing the potential in search engine rankings. By the age of 18 or 19, he was essentially replicating what Google was doing. One day, however, he received a letter from the Swedish tax authorities informing him that he owed hundreds of thousands in back taxes. In his late teens and early twenties, Ek was pursuing various projects, but he hadn't yet understood the importance of financial planning. Instead of saving, he spent most of his earnings on servers,

hiring programmers (25-30 employees), and pursuing projects that interested him, even if they weren't always profitable. It wasn't the potential bankruptcy that bothered him the most, but the thought of having to lay off his employees. He was feeling depressed during this time, worried about the livelihoods of those who depended on him (Sarah Lacy and Startups.com, n.d.).

Fortunately, things took a positive turn in 2005 when the sale of Skype to eBay set off a wave of acquisitions across Europe. In six months, he sold four companies and went from the edge of personal bankruptcy to millions of dollars in the bank (Sarah Lacy and Startups.com, n.d.).

5.2 Leadership Style: Inspired by the Scandinavian Model

Daniel's leadership style draws heavily from the Scandinavian management model, which values humility, delegation, and a flat organizational structure. Instead of a top-down, leader-centric approach, he focuses on empowering his team to make decisions and take ownership of their work, as opposed to more hierarchical companies where the CEO has ultimate control. As Daniel himself says, "In many ways, I'm probably the least powerful person at Spotify, and I probably make the fewest decisions" (Fortune 2024).

The CEO of Spotify is known for his emotional intelligence and humility. His statement, "I'm really happy when my team proves me wrong," reflects his belief in listening to others and being open to new perspectives. He considers listening to be one of the most undervalued skills in society and often reminds himself to continually improve in this area (Justin Bariso and Inc. 2023).

Another key aspect of his leadership is his commitment to long-term vision. He and co-founder Martin Lorentzon had several opportunities to sell Spotify early on, but they resisted because they wanted to show European entrepreneurs that it's possible to build a global leader without early buyouts. At the 2018 Slush Music event, Daniel expressed his frustration with fellow entrepreneurs who sell too early, saying, "Spotify wouldn't be where we are today... if we had listened to the many people who said we should sell (Murray Stassen 2020)."

Furthermore, his belief in the power of collaboration and distributed decision-making aligns with Spotify's progressive policies, such as a generous parental leave plan and a work-from-anywhere policy, both inspired by Scandinavian work models (Fortune 2024).

6. Conclusion

Daniel rose from his chair and walked to the window overlooking the city. Took a deep breath and tried to calm himself. Outside, the rain began to fall harder, each drop hitting the glass like a small hammer. Daniel felt a cold sweat break out on his forehead.

His head was filled with what-ifs. What if investing more in marketing could provide deeper insights for better conversion? What if the company should embrace open innovation to stay ahead of Apple? The pricing challenge, however, remained a major concern. He wondered how to get users to pay for services they had long enjoyed for free. What if the stricter free plan discouraged them? What if it was time to adjust the business model to survive? The stakes had never been higher, and Daniel knew that every decision from this point forward would shape Spotify's destiny, for better or worse...

He looked once more at the rainy cityscape outside. The storm would pass, like all storms do. In its way, the air would be clearer, the horizon wider. Daniel sat back down at his desk, a newfound clarity settling over him. He took a sip of his now cold coffee and made a face, then chuckled softly. "Time for a fresh cup," he thought.

7. Teaching Note

In 2015, Spotify faced the challenge of balancing rapid user growth from its freemium model with the need for profitability. Despite having over 75 million users, only 20 million were paying subscribers. Investors were demanding profits, artists were dissatisfied with the low payouts, users were used to free music, and competition from rivals such as Apple Music was intensifying. The core issue was to determine how Spotify could significantly rethink and adjust its product, pricing, and marketing strategies to achieve sustainable product-market fit.

7.1 Learning Objectives:

- Define and adjust product-market fit in a dynamic competitive environment.
- Adapt the product strategy to align with market trends while ensuring the business model's sustainability.
- Evaluate pricing strategies and optimize the balance between customer acquisition and profitability.
- Drive growth and competitive advantage through product innovation.
- Align marketing with product-market fit to drive differentiation and profitability.

7.2 Target Audience:

- Advanced undergraduate students in management, product development, or digital business models.
- Master's level students pursuing degrees in business, management, entrepreneurship, or marketing.
- Entrepreneurs and startup founders who want to learn from strategies on product-market fit, pricing models, and market competition.
- Professionals responsible for overseeing product development, market expansion, or pricing strategies in technology-driven industries.

7.3 Assignment Questions:

Exploring the Marketing Strategy

- How does Spotify leverage marketing tools to gain insights into market trends, and in what ways do these tools help the company understand and anticipate consumer preferences in the music streaming industry? And how these marketing strategies could help Spotify to converse freemium in premium users?
- In what ways do cognitive biases influence user behavior on Spotify, and how does the platform utilize or address these biases to enhance user engagement and satisfaction?

- How has Spotify implemented open innovation strategies, such as collaborating with external developers and integrating third-party technologies, to drive innovation and maintain a competitive edge in the streaming market?

Pricing Strategy

- What were the key drivers and constraints shaping Spotify's pricing strategy in 2015?
- What are the various pricing strategy options that can be considered to enhance Average Revenue Per User (ARPU) and overall profitability?
- What forward-looking pricing tactics can enhance profitability?

Navigating the Business Model

- How can Spotify improve users' willingness to pay (WTP) for its services?
- How can Spotify balance its Free plan to attract and retain users while ensuring that it does not hinder premium subscription growth?
- How can Spotify optimize its freemium business model to ensure long-term growth and competitiveness in the streaming market?

Pricing Strategy

Spotify's freemium business model for acquiring users was sustainable; however, the high costs associated with licensing music put significant financial pressure on the company. Since royalties and fees for rights holders accounted for approximately 70% of Spotify's expenses, the firm faced challenges in becoming profitable (Dempsey & Kelliher 2017). Also, the difference in revenue generation between the free tier and paid tier users increased the problem because free users generated much less revenue than paying users. Nevertheless, services availed through the platform have a low proportion of freemiums to premium users, as seen at a 26% conversion rate in 2015.

The pressure on Spotify's business model ramped up with the introduction of an Apple Music service in June 2015 a direct competitor with a much more focused subscription-based model. Leveraging Apple's ecosystem, guilt by association, and some artists' exclusivity made Apple Music avoid most of the freemium model's profitability barrier, attracting a group of consumers willing to pay for better quality music streaming services. This strategic differentiation put Spotify on the spot regarding the financial drawbacks of the freemium model paired with the need to sustain its competitive advantage.

1. What were the key drivers and constraints shaping spotify's pricing strategy in 2015?

Spotify was firmly established in the competitive music streaming market, contending with several key players, including Apple Music, Pandora and Tidal. Spotify's pricing model, consisting of a freemium approach with a free tier and a paid premium option, allowed it to cater to casual listeners and serious music fans. Spotify's Premium Individual plan was priced at \$9.99 monthly, like its competitors. Apple Music, launched in mid-2015, followed a similar pricing strategy, offering a \$9.99 subscription with a 3-month free trial and a family plan priced at \$14.99 for up to six users (Apple 2015). Spotify's value proposition in 2015 was centered

around its personalized user experience, which set it apart from competitors in the music streaming space. Key features like Discover Weekly, a curated playlist of 30 songs based on individual listening habits, and personalized recommendations helped Spotify attract over 40 million new users in 2015 (Possagnolo 2022). The service's intuitive interface, social sharing capabilities, and playlist creation tools allowed users to seamlessly interact with the platform and share music. Additional attributes like offline mode, podcasts, and an increasing library of original programming like Spotify Singles only added to the platform's utility. For instance, Apple Music was more inclined toward device synchronization and special content. On the other hand, Tidal was inclined towards sound quality and artists' proprietary content, and Pandora was inclined towards the radio-like model (Possagnolo 2022).

Spotify's branding and differentiation strategies were integral to its market positioning. The company revamped its logo, introduced a more vibrant color palette, and adopted a fresh visual identity to align itself with its youthful, millennial audience. Key partnerships with brands like Starbucks, Uber, and Sony accompanied these changes, which helped the company expand its reach and visibility across multiple platforms and devices (Mohammad, Mehak, Riaz, Farooq and Adhia 2021). The ability to integrate with diverse devices, such as smartphones, smart speakers, and gaming consoles, solidified its reputation as the “most personalized music experience” in the industry. By focusing on personalization and a rich, social, and integrated user experience, Spotify built a strong competitive edge in 2015, further supported by its marketing and partnerships (Possagnolo 2022). As Apple Music launched, Spotify adjusted its approach, increasing its focus on content differentiation and partnerships, but its pricing remained largely unchanged in the short term. The introduction of Apple Music, with its exclusive artist collaborations, likely pushed Spotify to enhance its content offerings and refine its pricing strategy to retain market share.

1.1 Spotify financial metrics

Spotify's cost structure was heavily influenced by its licensing agreements with major record labels, which formed a significant portion of its operating expenses. The company paid roughly 70% of its total revenue to rights holders, a substantial portion directed towards royalties for streaming music. Licensing agreements were tiered, with separate royalties for "sound recording" and "music publishing" rights. However, it was possible to maintain contracts with major labels like Sony Music, Warner Music, and Universal Music Group. Royalty payments amounted to about \$1.83 billion, representing over 80% of its revenue. This heavy reliance on royalty payments left Spotify with limited pricing flexibility. The company's operational costs included significant investments in server maintenance and employee salaries, categorized as fixed costs. These costs remained constant, regardless of user activity, providing some stability in budgeting. On the other hand, variable costs, such as the expenses tied to free-tier users receiving ads and premium subscribers, fluctuated based on user engagement and subscriber growth (SEC 2018).

Despite these substantial costs, Spotify increased his revenue, reaching 1,940€ million in 2015, up from 1,084€ million in 2014 (Statista 2024). However, this increase was insufficient to turn a profit, as the company struggled to balance growing costs with its aggressive expansion strategy. These financial pressures directly shaped Spotify's pricing decisions, particularly its freemium model.

Table.1 – Spotify operating expenses as % of gross profit and revenue

Income statemet	Value (€M)	As % of Gross profit	As % of revenue
Revenue	1,940	-	100.00%
Cost of Revenue	1,714	-	88.35%
Gross Profit	226	100.00%	11.65%
Research & Development	136	60.18%	7.01%
Sales & Marketing	219	96.90%	11.29%
General & Administrative	106	46.90%	5.46%
Total Operating Expenses	461	204.42%	23.76%
Loss Before Tax	-225	-99.56%	-11.60%

Source: Analysis made with table (A) – source based on SEC (U.S. Securities and Exchange Commission). 2018. Form F-1 Registration Statement for Spotify Technology S.A.

The financial results indicate a significant challenge with its operating expenses in relation to gross profit and revenue, primarily due to high licensing costs and operational spending. In 2015, Spotify generated €1,940 million in revenue. However, the cost of revenue stood at €1,714 million, which accounts for 88.35% of total revenue. This highlights the substantial payments made to music rights holders for licensing content, leaving Spotify with a narrow gross profit of €226 million, or 11.65% of revenue. The company's operating expenses, totaling €461 million, represent 204.42% of gross profit and 23.76% of revenue, showing financial strain. The most significant costs include:

- Sales & Marketing (€219 million) this expense consumes 96.90% of gross profit, demonstrating Spotify's heavy investment in user acquisition and retention amidst competitive market conditions.
- Research & Development (R&D) (€136 million) At 60.18% of gross profit, this reflects the company's dedication to innovating and enhancing its platform.
- General & Administrative Expenses (€106 million) These expenses add further financial pressure, accounting for 46.90% of gross profit.

As a result, Spotify reported a loss before tax of -€225 million, which is -99.56% of gross profit and -11.60% of revenue. This indicates that current revenue levels are insufficient to cover both licensing and operational costs. This analysis suggests that Spotify needs to address its high-cost structure by exploring strategies such as increasing subscription prices to meet expenses. Additionally, while the freemium model is essential for attracting users, it contributes minimally to revenue and needs to be better monetized. Without a balanced approach to these elements, Spotify risks prolonged financial instability despite its leadership in the streaming market.

1.2 Premium and freemium financial discrepancy

A significant challenge in Spotify's pricing model is the barrier preventing free-tier users from converting to premium subscriptions (Schmid & Romey, 2022). The public is still unwilling to pay for music streaming due to low income per capita and because there are other similar services available. Furthermore, the ads in the free tier do not necessarily compel users to purchase the paid services as some users have already gotten used to disruptions from ads or do not consider such features necessary (Pratama & Narimawati 2023).

One of the major conversion factors is presence of other paid services such as Apple Music and that occasionally provide exclusive benefits, that are not available to Spotify premium users. For example, Apple Music's compatibility with Apple products and devices and the release of their exclusive content will interest users using Apple products (Bratteng & Sæther 2023). Nevertheless, this competitive differentiation undermines the conversion process because people can get more value with other services that meet their needs or preferences. Therefore, these aspects have restrained Spotify's potential to monetize users and generate subscriber revenues, which consequently impacts its revenues and profits (Rajala & Korhonen, 2020)

In 2015, Spotify generated a total revenue of €1,940 million, which can be divided into two segments: Premium subscription revenue €1,744 million (90% of total revenue) and the Ad-supported revenue €196 million (10% of total revenue). The Premium segment highlights its role as Spotify's primary source of revenue. This revenue reflects the platform's growing subscriber base, although it comes with significant cost pressures. In contrast, the Ad-Supported segment contributes less to total revenue, indicating untapped monetization potential.

Table.2 – Spotify premium subscription and Ad-supported revenue as % of total revenue

Category	Value (€M)	Insights
Total Revenue	1940	Spotify's total revenue for 2015, reflecting its strong market presence in music streaming.
Premium subscription Revenue	1744	The Premium segment dominates revenue, contributing 90% of total revenue, driven by subscriptions.
Free version Ad-Supported Revenue	196	Ad-Supported revenue represents 10% of total revenue, indicating underutilized monetization potential.

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Gross Profit Margin	226	Gross profit margin is 11.65%, reflecting high content acquisition and delivery costs, leaving limited profitability.
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Source: Analysis made with (table 1) and SEC (U.S. Securities and Exchange Commission). 2018. Form F-1 Registration Statement for Spotify Technology S.A.

Spotify's cost of revenue amounted to €1,714 million, representing 88.35% of total revenue and resulting in a narrow gross profit margin of 11.65% (€226 million). This high cost is primarily due to licensing fees and streaming delivery expenses: premium subscription cost of revenue: €1,487 million, which is 85% of Premium revenue and ad-supported cost of revenue: €227 million, equating to 116% of Ad-Supported revenue, highlighting negative margins for this segment. The elevated cost structure emphasizes Spotify's challenge in achieving profitability, particularly due to content acquisition costs associated with rights holders, which are directly tied to subscriber growth and ad-supported usage.

Table.3 – Spotify premium subscription and Ad-supported cost as % of total cost of revenue

Category	Value (€M)	Insights
Total Cost of Revenue	1714	Represents 88.35% of total revenue, leaving narrow margins.
Premium Cost of Revenue	1487	86,76% of Premium revenue spent on costs.
Ad-Supported Cost of Revenue	227	13,24% of Ad-Supported revenue spent.

Source: Analysis made with (table 1) and SEC (U.S. Securities and Exchange Commission). 2018. Form F-1 Registration Statement for Spotify Technology S.A.

1.3 Competitors analysis

Porter's Five Forces framework offers a structured analysis of the competitive pressures affecting Spotify's pricing strategy (Ramos & Blind 2020). The anticipated closeness between existing competitors is high, as observed by many industry players, such as Apple Music who are willing to offer same prices as Spotify and unique content in a bid to gain market share. The threat of new entrants is moderate since great capital investment is required, and extensive licensing is also required before a competitor can be allowed to join the industry (Giacomo 2024). The threat of suppliers, or more accurately, music labels and publishers, is high due to their ability to demand high license fees, which puts pressure on Spotify's profitability. On the other hand, the bargaining power of buyers (Spotify users) is also moderate. The concept of

switching costs is low, which makes consumers shift to other competitors and compels Spotify to remain affordable and offer an enhanced user experience. Ultimately, the threat of substitutes is also moderate, as streaming has faced competition from radio, downloaded music, and pirated content. Spotify can easily handle risks and improve its pricing plans by knowing these dynamics (Murray-Noel 2018).

Table.4 – Spotify Porter's Five Forces framework

Forces	Description	Level of Intensity
Threat of Existing Competitors	High level of competition from players like Apple Music, offering same prices and unique content to capture market share.	High
Threat of New Entrants	Moderate due to high capital investment and extensive licensing requirements needed to enter the industry.	Moderate
Threat of Suppliers	High because music labels and publishers can demand high license fees, putting significant pressure on Spotify's profitability.	High
Bargaining Power of Buyers	Moderate, as switching costs for users are low, making it easy for them to shift to competitors, forcing Spotify to remain affordable and provide an enhanced experience.	Moderate
Threat of Substitutes	Moderate due to competition from radio, downloaded music, and pirated content.	Moderate

1.4 Spotify SWOT analysis

The SWOT analysis framework is crucial for understanding Spotify's internal strengths and weaknesses and external opportunities and threats. The main critical strength factors of Spotify are the vast market coverage the company enjoys, the incredible brand recognition it has among its users, and the algorithms that propel the users' engagement (Corelli 2023). Nonetheless, the weakness of this company is its high dependency on licensing music from the major record labels, which in turn increases the operational expenses and low profit margins as we could see in (table 2). Furthermore, it also has a freemium strategy that has exhibited weakness in converting the number of free users to paid subscribers, thereby resulting in low ARPU (Marshall 2015). In terms of opportunity type, Spotify can expand its income-generating services and product line, including exclusive content creation and partnership opportunities, as well as diversified service plans at different price levels to improve user value and

positioning (Sletten 2021). Podcasts and audiobooks are also other growth opportunities since their market is starting to grow. However, challenges include competitor pressures in of Apple Music, as well as dynamic data privacy laws that would affect Spotify's collection of users' data for recommendation use.

Table.5 - SWOT analysis

Strengths	Weaknesses	Opportunities	Threats
Broad user base and well-established brand.	Heavy reliance on expensive music licensing fees.	Expansion of income-generating services and product lines, such as exclusive content and partnerships	Strong competition from Apple Music.
Sophisticated personalization and user experience.	Limited success in converting free users to premium subscriptions resulting in low ARPU	Forming exclusive content agreements.	Regulatory hurdles around data privacy laws. As pointed out in the Marketing Strategy.
Wide reach across international markets.	High operating expenses and narrow profit margins.	Diversified service plans for improved user value and positioning	

Spotify’s strong user base and global reach are balanced by high licensing costs and competition, while opportunities in podcasts and exclusive content help mitigate these threats.

Competitor analysis based on the financial comparison highlights the key issues of the offered model of monetization, including ARPU and profitability at the level of the competing companies. The results of this analysis can be complemented with the SWOT analysis to discover further internal strengths, including Spotify's use of personalization, and external threats, including competitive pricing strategies (Vonderau 2019). Measuring the conversion metrics across geographical locations and users' demographics would enable to optimize its approach to fulfil users' needs and create a perfect roadmap for freemium to premium conversion.

2. What are the various pricing strategy options that can be considered to enhance Average Revenue Per User (ARPU) and overall profitability?

Pricing sensitivity analysis is essential to determine the effects of different pricing strategies on Spotify's profitability and ARPU, conversion rate, and competition. In the base case, there is no

change to Spotify's existing \$9.99 Premium subscription (Kabir 2019). The main benefit of this approach is its simplicity, which is used throughout the industry to various degrees (Sletten, 2021). However, it tends to dampen ARPU growth because of its inability to vary its rates in the manner it seeks to enhance its revenues. The base case shows a sustained level of revenues in initial consumers. Still, the preservation of the free users is rather difficult since they dynamically transform for a while extremely slowly.

Table.6 - ARPU impact comparison for each pricing scenario

Pricing Scenario	ARPU Impact	Conversion Rate from freemium plan	Revenue Growth	Challenges
Base Case (\$9.99 Premium)	Low ARPU growth due to high prices and limited conversion	Low	Steady revenue, slow conversion from the free tier	Minimal premium conversion, high licensing costs
Tiered Pricing (proposed in table 2)	Higher ARPU from mid-tier users, balanced conversion	Moderate	Increased revenue from more users	Potential cannibalization of premium users
Regional Pricing (\$4.99–\$6.99)	Lower ARPU in emerging markets, higher conversion	High	Increased user base, offset by lower ARPU	Operational complexity, competitive threats
Usage-Based Pricing	Higher ARPU from heavy users, lower from light users	Moderate	Increased ARPU from power users	User resistance, complexity in billing models

Each model presents unique advantages and challenges, highlighting the trade-offs Spotify must consider optimizing profitability and user engagement.

2.1 Tiered pricing

A tiered pricing model introduces a multi-level subscription plan. This model removes adverts and thus has fewer or no premium features, such as quality audio and the ability to download for offline use (Kabir 2019). A diversified subscription plan is always attractive for those who don't want to pay the premium price but want to eliminate the ads. The addition may greatly propel the conversion ratios of the company from free to paid consumers, especially the sensitive price consumers. In contrast, \$9.99 can lower the premium conversion rate since some users will be willing to take a mid-tier alternative to the full premium plan.

However, by segmenting the customer using a tiered pricing model, it will be possible to target a broad range of consumers with tailored pricing plans. *Premium Individual* subscribers, paying

\$2.99 per month will receive ad-free listening, offline access, and higher audio quality, appealing to music enthusiasts willing to pay for a better experience.

Premium Family plan, priced at \$6.99 per month, allowed up to six users to get premium features, targeting households or groups and offering an attractive discount for multiple accounts under one subscription. The *Premium Student* plan, priced at \$2.30 per month, catered to younger users by providing all the benefits of Premium at a discounted rate, making it highly attractive to college students.

Table.7 – Tiered pricing based on customer segmentation

Plan	Price (USD)	Features	Target Segment
Current Premium	\$9.99 month	✓ Full-service subscription	All
Premium Mini	\$1/week	✓ 20 song downloads to one mobile device ✓ Unlimited ad-free music on one mobile device, Free experience on non-mobile devices	Casual listeners
Premium Individual	\$2.99/month	✓ Ad-free music listening ✓ Download to listen offline ✓ Play songs in any order ✓ High audio quality ✓ Listen with friends in real-time ✓ Organize your queue	Individual users
Premium Duo	\$3.99/month	All Premium Individual features, plus two users	Couples/Roommates
Premium Family	\$6.99/month	Ad-free music listening Play offline Unlimited skips For up to 6 accounts	Families
Premium Student	\$2.30/month	All Premium Individual features, available to eligible students	College students

Considering this model, there will be a flexible approach to enhance Average Revenue Per User (ARPU) following diverse customer needs. By introducing multiple pricing tiers, businesses can target different segment pushing higher conversion rates from the free tier. The multilevel plan can attract price-sensitive users, while premium plans will still give high-value customers who seek exclusive features. However, it poses challenges, including the potential cannibalization of premium subscribers (De Giovanni & Ramani 2017). Customer segmentation is also an informative tool that can help Spotify adjust the price and the advertising campaigns

according to the users' age, income, and geographical location. This segmentation can then be used to create specific campaigns aimed at milking the largest chunk of those likely to switch to paid. Furthermore, by applying the conversion rate analysis the company will be able to determine factors that discourage users from going premium (Mohamed & Alrached 2024).

2.2 Regional pricing

Regional pricing can be defined as changing subscription prices corresponding to the economic conditions of the specific geographical location. In the case of Spotify, increasing the availability of affordable pricing plans in emerging markets such as Southeast Asia and South America can widen market accessibility, boost the proportion of the reduced price of the hired base summit, and convert more free users to paying ones (Banerjee, Siddhartha, Riquelme, and Johari 2015).

For regions where it is simply impossible to pay \$9.99 for the premium, it can be assumed that introducing lower-priced premium options will enlarge the customer base. This segmentation may increase the number of Spotify consumers in price-sensitive areas where close rivals offer similar subscription tariffs (Bonfré and Adolfsson 2020). The pricing model in these regions may be adjusted to lower rates, which could lead to an increase in the number of subscribers to the company's premium service, resulting in higher overall revenue. Different pricing strategies across various locations present challenges, but the company can address these issues by expanding its market coverage (Banerjee, Siddhartha, Riquelme, and Johari 2015).

Geographical differentiation might drive Spotify's subscribers in various regions and improve user uptake and conversion in emerging markets (Badr, Sharaf, and Mahrous 2024). However, while this could moderately bring the ARPU down in these regions, the overall subscriber numbers would add up to higher total revenue. Further, regional pricing minimizes the threat from local competition, which may likely simulate pricing strategies (Riesewijk 2017).

2.3 Usage-based pricing

The usage-based pricing method allows to price subscriptions differently depending on users' usage levels. Power listeners, those who stream frequently and utilize extra features like offline listening would be willing to pay more than regular users who engage less and use fewer features. Implementing a usage-based pricing model could benefit the business by generating higher profits from heavy users while remaining affordable and accessible for casual users with minimal engagement. This model is designed to increase the ARPU from power users while also retaining light users. However, widespread implementation of the pricing structure may face resistance from power users who are accustomed to flat-rate pricing. To effectively introduce this model, it is essential to collect and analyze data regarding user activities and usage behavior (Florez Ramos and Blind 2020). Usage-based pricing can be complex, but it offers flexibility that can enhance user satisfaction across different segments. With pay-per-use pricing policies, users are charged based on their level of service usage. For instance, heavy streamers may incur higher costs, while lighter users benefit from lower subscription costs (Dempsey & Kelliher 2017). This consumption-based approach has the potential to generate more revenue from heavy users while making services more affordable for those with lower usage. It encourages higher utilization among subscribers by offering different subscriptions level for various usage levels. However, practical application may be challenging due to factors such as changes in flat subscription, which could lead to user dissatisfaction (Bonfré and Adolfsson 2020).

3. What forward-looking pricing tactics can enhance profitability?

These psychological pricing strategies are in line with the goals of Spotify, promoting high conversion rates and absolute user engagement. Spotify's pricing strategies must align with its long-term goals of profitability, user growth, and brand differentiation in the competitive streaming market (Guo & Luo 2024). The tiered pricing and regional pricing models, as well as other attempts to increase the value generated by listeners, should complement the issue of

revenue and organizational costs, especially those associated with licensing and royalty payments for musical content. This alignment requires delicate tuning of the business model to ensure that the value for segments such as premium users offset the fixed costs while delivering value to a large base through affordable prices (Skog et al. 2021). The promotion of user engagement and retention is, therefore, crucial to Spotify's growth strategy, especially since the company relies on subscription as its main revenue model. Spotify can exploit some psychological pricing strategies like charm pricing and bundling to increase the perceived value by its customers leading to a reduction in churn rate among its subscribers (Guo & Luo 2024). These goals of raising user retention are consistent with Spotify's long-term goals of being a long-term audio streaming platform since higher retention levels mean a stable revenue stream and reduced customer acquisition costs in future.

1.1 Psychological Pricing Tactics

Spotify can use psychological pricing to subtly influence user perceptions and encourage upgrades from free to paid tiers. **Anchoring** is one strategy Spotify can use effectively by presenting its premium plan alongside a mid-tier option, making the premium plan appear more valuable by comparison (Ramos & Blind 2020). With a mid-tier subscription with limited features, and at a lower price, Spotify makes its premium plan look better. **The downside of anchoring is** that it highlights the benefits of avail the premium plan that in turn may help in improving the conversion of the free to paid users (Lozic 2020). Spotify may be using the **charm pricing** technique .99 cent rates. Furthermore, consumer research is one way of showing that consumers tend regarding \$9.99 cheaper than \$10, despite the change in a decimal figure. Spotify may use number trick and provide its premium and mid-tier plan to appear cheaper by rounding them to end in .99 (such as \$4.99, \$9.99). Perhaps this small change in the price will affect the customer's decision-making since some of these options will seem cheap without requiring one to plunge into a huge expenditure.

1.2 Discounts and limited-time offer

Discounts and limited-time offer could be strategically deployed to convert more users to premium, especially during peak seasons or promotional events. Including incentives, for instance, providing a lower price for the first three months of the premium service, she uses the concepts of time pressure and scarcity (Kuyucu 2024). Such promos can make free-leveled users try and enjoy the features of the paid tier which will, evoke an emotional positive response that may keep them paying even after the bonus duration. Ultimately, **bundling** could increase perceived value by including, for instance, **podcast or audiobook** access in the price of the premium subscription. This bundle gives the listener the feeling of 'extra' for a relatively marginal increase in Spotify's cost (Corelli 2023). The offer of different content types in the same price range speaks to consumers' self-actualization, making the idea of the paid subscription worth it and giving the users more for their money.

2. Recommendation

Global market expansion is a priority for Spotify, and regional pricing strategies allow the company to adapt to economic differences across markets, increasing accessibility in lower-income regions. This approach helps Spotify achieve its goal of delivering audio content to numerous groups of listeners while preserving affordability in developing countries (Corelli 2023). Similar regional adjustments also offset competition from domestic players, which helps Spotify in its long-term strategy to become the leading streaming service worldwide. Consequently, it means that the key to sustained high levels of innovation on the music streaming market is not only the existing pricing models, but the capacity to fund the growth of user personalization and technological advancements at Spotify. The accrued amount from such adaptive pricing models can be used to finance research and development, hence such developments as betterment of algorithms and increase in content (Saygın 2022). To support the company's goal to revolutionize music and audio streaming, pricing is tied with innovation

objectives, making the service valuable and popular among users. However, Spotify has a major issue in achieving the growth of active users and minimizing its burn rate because of its freemium model and high cost of royalties. The three strategies of tiered pricing, regional pricing, and usage-based pricing present avenues for increasing profitability. Thus, using a variable, geographically differentiated approach to pricing, Spotify can at once discuss affordability issues in emerging markets and maximize the ARPU. The mid-tier pricing strategy means that the machine is easy on the pocket, which attracts users who cannot afford the premium accounts but excludes the free version's power users, which serves the purpose better than a diluted premium account (Mei 2024). Regional pricing helps Spotify enter new markets, and usage-based pricing, in turn, fits pricing to customer interaction with the service, encouraging Power and on-and-off users. The new pricing strategies and personalization will help shape the market's future and establish Spotify as a long-term market leader enhancing user conversion rate.

What happened

Since the launch of Apple Music in 2015, Spotify has managed to maintain its position as the market leader while experiencing significant growth and strategic success. Apple Music has emerged as a strong competitor in the streaming market with Apple's vast ecosystem. However, Spotify's quick adaptations and innovative strategies allowed it to meet this challenge head on and fueled its rapid rise.

Spotify implemented localized pricing strategies to make subscriptions more affordable in areas with lower purchasing power such as Southeast Asia and Africa and introduced Student and Duo plans to target specific audiences (Spotify Community 2021). Moreover, the service's cross-platform approach became a key differentiator, which broadened its audience (Spotify, n.d.). In contrast, although Apple Music also introduced Student and Family plans, it remained tightly integrated with the Apple ecosystem, which limited its appeal to users outside of Apple's platform (Apple, n.d.).

By the third quarter of 2023, Spotify had a commanding 31.7% share of global music streaming subscribers, well ahead of Apple Music, which had 12.6% (Statista 2024h). On the financial front, Spotify's revenue skyrocketed from €1.94 billion in 2015 to more than €13.2 billion in 2023, driven largely by its premium subscription model (Statista 2024j). The company reached a significant milestone in 2024 by becoming profitable, reporting a net income of €274 million, a remarkable turnaround from previous years of financial losses (Todd Spangler and Variety 2024). While Apple Music grew steadily to 93 million subscribers by mid-2023, it fell short in market share, user engagement, and overall influence (Statista 2024e).

Spotify has strategically diversified its offerings to reach a broader audience. The company acquired podcast networks like Parcast and Gimlet Media and established itself as a leader in podcasting (Johan Moreno and Forbes 2022). Although Apple Music introduced podcast

integration, it couldn't match Spotify's impact in the space. As for marketing, Spotify used user data to create highly personalized campaigns like "Spotify Wrapped" in 2016, which turned individual listening habits into shareable moments, generating viral engagement (Spotify 2024). Apple Music, on the other hand, found it difficult to compete with Spotify's level of virality and deep personalization, despite its curated playlists and exclusive content.

To find a balance between monetization and user satisfaction, Spotify has made some strategic changes to its Free tier. In April 2018, it improved the Free plan by allowing on-demand playback for select playlists, giving users more control over their listening experience. In May 2023, Spotify attempted to limit Free users to viewing lyrics for just three songs per month. After significant backlash, the company reversed this decision by July 2024, making lyrics available to all users worldwide, regardless of their subscription (Lauren Forristal and TechCrunch 2024).

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Appendix

A. Spotify's financial metrics in 2015

Category	Metric	Value (€ millions)
Premium Segment	Revenue	1,744
	Cost of Revenue	1,487
	Gross Profit	257
Ad-Supported Segment	Revenue	196
	Cost of Revenue	227
	Gross (Loss)/Profit	(31)
Consolidated	Revenue	1,940
	Cost of Revenue	1,714
	Gross Profit	226
Reconciliation of Gross Profit	Segment Gross Profit	226
	Research & Development	(136)
	Sales & Marketing	(219)
	General & Administrative	(106)
	Finance Income	36
	Finance Costs	(26)
	Share in Losses/Earnings of Associates and Joint Ventures	-
	Loss Before Tax	(225)

Sources: SEC (U.S. Securities and Exchange Commission). 2018. Form F-1 Registration Statement for Spotify Technology S.A.

B. Overview of consumer behavior across different markets

Region	Key insights	Demographics and preferences	Segments
Europe	UK is a key market with 56% of digital music users preferring Spotify. Smartphones (70%), with laptops (36%) as a secondary choice. Users primarily listen to music at home while engaged in activities such as relaxing, doing housework or walking. Podcasts are increasingly popular for entertainment, relaxation and learning.	More popular among Gen Z; 54% male user base. Higher income users value success, fitness, and tech engagement.	Social sharers, tech-savvy discoverers, cost-conscious users.
North America	Spotify leads with 44% user share in the U.S., particularly among Gen Z. A mix of devices is used. US users listen while gaming, watching TV or movies, and other leisure activities.	Balanced gender distribution; higher-income users. Entertainment is prioritized over traditional values.	Content explorers, convenience seekers, tech-lagging listeners.
Latin America	Brazil is a dominant market with 68% user share. Users are Millennials, urban-based, and value content discovery. Smartphones are the	Primarily millennials (53% male) in urban areas; gaming and	Urban millennials, gamers and digital

	dominant device in Brazil. Listening while playing games, leisure activities or while commuting.	eSports are prevalent interests.	enthusiasts, cost-sensitive listeners.
Rest of the World	India shows high engagement with 62% user share. Smartphones are the primary device for Spotify users in India, who often listen while commuting, relaxing at home, or watching movies and TV shows. Tech-savvy users prioritize high quality audio during these activities.	Male-dominated user base in megacities; tech-savvy audience prioritizing sound and image quality.	Quality seekers, entertainment-focused listeners, young explorers and students.

Sources: Statista 2024c; 2024d; 2024a; 2024b.

C. CX profiling of Spotify

Dimension	Current performance	Upside potential	Strategy
Cognitive – What people think	Spotify held the largest customer base and was perceived as innovative, intuitive, and user-friendly with access to the largest music library.	Limited potential as further improvements would not significantly enhance customer perceptions.	Defend (yellow): Maintain current levels of performance without unnecessary investment.
Physical – How people interact	Through desktop and mobile phones. Free-tier users face stricter limitations on mobile without on-demand playback.	Moderate potential to educate users and improve awareness of Premium features over time.	Defend (yellow): Maintain current standards and gradually building attractiveness of Premium for listening on-the-go.
Sensorial – What people experience	High-quality sound for Premium users and standard streaming for Free-tier users, with audio quality as an incentive to upgrade.	Limited potential as further improvements can hinder Free-to-Premium conversions.	Defend (yellow): Maintain current gap to keep differentiation between two plans and an incentive to upgrade.
Emotional – How people feel	Positive emotional connections with Premium users through personalization but Free-tier users frustrated by frequent ads.	Significant potential to emotionally connect Free-tier users and create a sense of belonging.	Build (green): Develop new capabilities to deepen emotional engagement for Free-tier users.
Social – How people share	Critics and media rate social features like music sharing and friend-adding as controversial and underutilized.	Minimal potential as social connectivity is not highly valued by all users.	Ignore (red): Prioritize resources elsewhere, as enhancing this dimension has minimal impact.