Exam Question – Spotify

Disclaimer: Although based on a real-world company, the case study below is entirely fictitious and should not be construed as reflecting the views or plans of the company in question.

Spotify has conquered the online music market. Their growth has been strong and they have entered more than 50 countries. Recently one of the vice presidents, Sven Svensson, suggested that they enter the market for educational talks. There are companies such as The Great Courses that produce high quality audio lecture on different subjects recorded by professors.

The content providers sell audio lectures via their webpage as downloadable audio files. These audio products are costly and many customers find alternative ways to access the files. Furthermore, customers prefer to have only one device for all their audio experiences.

Sven Svensson thinks this could be a profitable market segment. He needs to set up a business case to analyse the financial aspects of the investment.

Estimations show that Spotify will have 5 500 000 paying customers (subscription fee of 10 € per month) by 2016. In addition, advertisement revenues will account for 80 000 000 € (2016). The gross margin for both revenue streams is 6%. However, Spotify is growing fast and they estimate their annual customer growth rate to be 15 % and their annual advertising by 3 %.

Sven thinks they can launch the “AudioLecture” service on 1st of January 2017. They would need to make an initial investment of 4 000 000 € (2015) and an additional 5 000 000 € in 2016. The new part of Spotify service would require maintenance of 2 000 000 € per year once the service is available for customers.

Sven plans to market the product aggressively during 2017 and 2018 by investing 6 000 000 € for each of these years in advertisement and events. Their market analysis has shown that with such an investment, Spotify would increase their paying subscribers with 2 000 000 in 2017 but unlike the “music” listeners, these customers would only grow by 5 % per year. The AudioLectures would also have advertisement segments, which would generate revenues. It is estimated that the advertisement revenues be improved with AudioLectures. Their calculations show that advertisement revenues would increase by 5 % per year instead of 3%. The gross margin of AudioLectures is 11 % (of all AudioLecture related revenues). Use a discount rate of 25%. Sven wants to see if this investment will be profitable with three full operating years (2017 until including 2019).