

The Daily: Spotify surprises itself, AI tools for Google ads, and is Peacock sustainable?

Audio

On today's episode, we discuss how Spotify beat expectations, why a price hike is inbound, and the audio streaming company's relationship with artificial intelligence (AI). "In Other

News," we talk about AI-powered ads for Google and whether Peacock can survive the streaming wars. Tune in to the discussion with our analyst Daniel Konstantinovic.

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Episode Transcript:

Marcus Johnson:

Hey gang, it's Thursday, May 4th. Daniel and listeners, welcome to the Behind the Numbers Daily, an eMarketer podcast. Made possible by InMobi. I'm Marcus. Today I'm joined by one of

our analysts on the marketing advertising briefing based out of New York. It's Daniel Konstantinovic.

Daniel Konstantinovic:

Oh, hi. Sorry.

Marcus Johnson:

Hello.

Daniel Konstantinovic:

Hello. I'm happy to be here. Happy to be here.

Marcus Johnson:

Right? We're off to a great start.

Daniel Konstantinovic:

Yeah.

Marcus Johnson:

Today's fact. Which country, Danny, has the longest coastline?

Daniel Konstantinovic:

Oh. Oh, shoot. I feel like this was the final jeopardy answer at one point and I-

Marcus Johnson:

Oh, was it.

Daniel Konstantinovic:

... forgot it, isn't it? Is it Chile?

Marcus Johnson:

No, that's a heck of a guess though.

Daniel Konstantinovic:

Shoot.

Marcus Johnson:

It's Canada.

Daniel Konstantinovic:

Oh. I guess that makes sense.

Marcus Johnson:

Canada's this coastline is... it's insane how much bigger it is though than everybody else in terms of how much longer it is, the coastline than everyone else. So its coastline is 150,000 miles long, including the mainland coast and the coasts of offshore islands as well. That's 50 times the length of the US from left to right. 50 times if you went back and forth and back and forth, back and forth. 50 times. That's the length of Canada's coastline. Indonesia's coastline in second place is five times shorter, Russia in third, US and fourth, China in fifth.

Daniel Konstantinovic:

I feel like once we get into, we're counting islands, coastlines and bays and stuff like that. It feels like they're fudging the numbers a little bit.

Marcus Johnson:

They're cheating.

Daniel Konstantinovic:

They're cheating [inaudible 00:02:27]

Marcus Johnson:

Canada. Some cheating.

Daniel Konstantinovic:

They got to reel it in.

Marcus Johnson:

Canadian territory with the most coastline? Newfoundland and Labrador in the top right-hand corner of Canada. A beautiful country.

Today's real topic. Spotify surprises itself.

In today's episode. First in the lead will cover Spotify's surprising Q1. Then for In Other News, we'll discuss AI tools for Google Ads and whether Peacock is a sustainable streaming service.

So Danny, the lead, we're talking Spotify. How have they been doing in the first couple of months of the year where they added 26 million monthly active users MAUs to reach 515,000,000. 5-1-5. That's 15, 1-5, million above guidance. Those 26 million net additions was Spotify's largest ever Q1 growth and second-largest quarterly net addition since going public in 2018. So the best Q1 they've had and the second-best quarter of all the quarters that they've ever had. But Danny, how is Spotify able to beat expectations and register a record Q1?

Daniel Konstantinovic:

I think what we're seeing with Spotify is just a continuation of seeds that they planted really early on. I think by offering such a cheap subscription service and so many deals to onboard young users, like cheaper access for college students, tie-ins with services like Hulu, they were able to onboard a lot of users and really are responsible, even more than I think a service like iTunes back in the day for making audio something that consumers consider a staple of everyday life. Something that they expect to always have access to. I think that they've really established that as a bare minimum that consumers are willing to pay for even when there are tough economic times.

Marcus Johnson:

Yeah. And we'll come on to the price in a second. You talked about a staple of everyday life when you stack them up against other media that people consume, some of those brands that are front of mind when you think about media consumption, people like TikTok, people like Netflix, people like YouTube. Spotify is, it's right up there. Time spent with Spotify by adult listeners, it's just shy of an hour this year. So an hour per day spent on Spotify by adult listeners. More than people will spend watching YouTube. The same amount of time as people spend on TikTok and nearly as much time as Netflix viewers spend watching Netflix. So it is really well established in terms of people's media diets.

Daniel Konstantinovic:

Yeah. I think it's incredibly easy. I think they benefit from audio just being an incredibly easy medium to interact with. You don't have to have your eyes locked on something. You don't have to be sucked into an endless feed like TikTok-

Marcus Johnson:

Yeah. Passive consumption.

Daniel Konstantinovic:

... People who are listening to this might be listening to it while they're driving, while they're working. Spotify has done a really good job keeping people in network, so to speak. There's great discovery for music on there. It's constantly surfacing new music to you, recommendations to you. It's very personalized. People love the Spotify Wrapped at the end of the year. They love to show their music tastes. It's like a social thing.

Think they've done a really good job of keeping people hooked on Spotify and it's been so effective that not just other music services, but other services across media are beginning to mimic some of that same personalization and shareability of things like Spotify Wrapped at the end of the year.

Marcus Johnson:

Yeah. One of the main reasons you could assume that people have stayed around is because the price has stayed so low as a lot of subscription prices have climbed. You write that Spotify will see a price hike in 2023. It's premium no add subscription is currently \$10 a month. A price hike, Danny, that's what you're expecting this year from Spotify. Why now?

Daniel Konstantinovic:

Well, I think it's the same reason that you're seeing streaming services start to do more price hikes. I mean, they've done it almost year over year, and Spotify's following a similar path where these streaming services started out at a low cost. It was like a low alternative to cable, and then over time they started upping the price as they got more and more users on board to eventually increase the margins, I guess. It was a long road and I think Spotify's going down that same long road.

But I also think it's a couple things. I think there are market pressures. We've seen, to compare to streaming services again, streaming services have been pretty much punished in the market for slower revenue growth, even when subscriptions go way up. If you look at Disney's last quarter in 2022, subscriptions were way, way up, but revenues were not up according to expectations and Disney stock went way down in the wake of those earnings.

And I think Spotify's fearful of something like that. They want to show that they can turn the faucet on higher, but I also think Spotify is in this interesting place where they are one of the clear winners of that generation of media service companies. They have this great financial model that is not just dependent on ad revenues. Which has hurt so many companies that are solely dependent on ad revenues. But they have a really healthy subscription revenue stream as well. And while all these other companies, Snapchat, Twitter, maybe Twitter's an anomaly, but all these ad dependent companies have started to shrink and perform really, really poorly quarter after quarter after quarter. Spotify maybe because of the nature of audio that I was just talking about, has managed to do really well and thrive or at least stay pretty stable despite that.

Marcus Johnson:

Right. They said they wanted to focus on profitability this year, like a lot of companies have said. They want to focus less on user growth, more on making money from the current users while still trying to grow users to a certain extent. But yeah, some of the reasons to hike the price, Apple and Amazon raised the price on their respective music services. Also, they bumped up the price of their family plan, which helped boost subscription revenue. So they've already done that, so they can't pull that lever anymore. So looking to pull another one. And then also total revenue growth that slowed from last Q1 to this Q1 from 24% to 14 with paid subscriber revenue growing a little faster than the ad supported dollars. So also needing to make more money is a reason to increase the price.

Danny, what'd you make of Spotify's Financial health? Just over \$3 billion made in Q1. Now it's made just over 3 billion the last two quarters, Q4 and Q3 as well. Total revenue up 14%. Most of that coming from the premium side, the paid side, about 89, 90% of the money coming from the ad-free users. What'd you make of where Spotify is financially?

Daniel Konstantinovic:

I think they're in a pretty solid position financially, but I think things like a price hike make that a little less certain. It's hard to gauge what the effect of a price hike would be on their financial health because so much of their revenue, the vast majority of their revenue comes from subscriptions. And if they increase the price, the question is, well, how many people will just decide it's not worth paying, so I'm going to cancel the service or just switch to the free ad supported version? I think there'll definitely be some kind of a drop-off, but I also am not so convinced that there's going to be a drop-off so significant that it'll really shake up or damage Spotify's position unless they raise the price to some exorbitant amount, which I don't think they will be so foolish as to do.

Marcus Johnson:

Yeah. Can't see it going over 15.

Daniel Konstantinovic:

Yeah, I mean even 15 feels like a lot. You know?

Marcus Johnson:

Yeah. Well they said... So yeah, most of the money, 90% of it pretty much coming from the ad free, the premium subscribers and then it makes the rest, the other 10 11% of Spotify's dollars coming from advertising. Spotify was noting revenue gains from its premium subscriber growth in Q1 won't be recognized until Q2 when promo pricing expires. So there's that to keep an eye on as well. Now Danny, finally in the lead, I want to quickly talk about AI because, did you write a piece about this recently? Right?

Daniel Konstantinovic:

We've written a couple pieces about AI features that they've launched. It was mentioned in the story we did on earnings, and then we wrote a story about this AI music controversy that they had.

Marcus Johnson:

That was it. Yeah. So tell me and the listeners about Spotify's relationship with AI thus far, because it seems like there's definitely some benefits here, but also some potential drawbacks.

Daniel Konstantinovic:

Yeah. So Spotify has dabbled with some AI features. The big most notable one is this AI DJ that they've launched. You can basically turn on a virtual radio station and it'll play you recommended songs, just like a lot of existing features on Spotify. But this AI DJ will cut in like a radio DJ and I don't know, segue into the next song or say something. And that's been sort of well received. I don't know any figures about how widely that's been used or if that's driving a lot of revenue for Spotify, but it does kind of seem like an obvious extension of the personalization that is such a defining part of using Spotify.

And it's easy to see how they could use AI for some of those processes if they're not already. Even outside of this AI voice, human voice DJ. Maybe your Discover Weekly is AI generated, or recommendations curated by an artificial intelligence. I think there are obvious ways for them to use it. The DJ is a good example of the other side of the coin. It's been criticized a lot as feeling cold and impersonal and a little bit ghostly. There's this feeling of, even if it sounds convincing, you know it's not a real person who's doing this and there's like an uncanniness there. So I think this is like Spotify experimenting with what AI looks like on their service.

Marcus Johnson:

Right. But also some concerns around copyright as well.

Daniel Konstantinovic:

Yeah, so there was a issue a couple weeks ago where a song that was by Drake and The Weeknd under an artist collab name, and it wasn't say by Drake, and by The Weeknd it was some group name started going viral on TikTok and was put on Spotify and very quickly reached almost a million streams on Spotify before Spotify and the record label caught wind of it and said, this actually isn't by Drake in The Weeknd. It's fake and this is AI generated and AI is mimicking their voice and it tricked people basically.

And the record label Universal Music Group wrote this open letter to Spotify and Apple Music and some other audio streaming services basically saying it's on you guys to make sure that you have systems in place to detect when fakes this are uploaded. And that's just not something that I think Spotify is prepared to handle. It's not something the record labels are prepared to handle because the technology is just developing so fast. If you listen to that AI generated song, it's very bad and it doesn't sound convincing. I mean the Drake part sounds a little bit convincing, but when it gets to The Weeknd, it gets into actual singing, it completely

collapses. But it managed to fool this huge number of people and that's got to be a concern for Spotify and for the record labels.

So the concern there is who has responsibility for stopping these things? There's not really a clear answer. There aren't any systems in place to prevent it. And could it, I guess as a question, could it lead to some potential litigation down the line? Could Spotify be held responsible for damages for hosting this on their platform? Because it's very easy to upload music to Spotify. So this could just keep happening over and over and over again and probably will and who knows if Spotify will be able to keep up with the pace of it.

Marcus Johnson:

That's it for the lead time. Of course, for the halftime report.

Danny, a quick takeaway from you for the first half please.

Daniel Konstantinovic:

I think Spotify has done really well so far and has come out of this, I hate to say web and anything with the number after it, but like Web2 era-

Marcus Johnson:

Web, anything

Daniel Konstantinovic:

... on its feet. Yeah, it's come out of the web something era like pretty sturdy and pretty stable. And I think now what we're going to see and what we're already starting to see with some of this short form video stuff and this AI stuff and a price hike, is Spotify trying to figure out what's next. Trying to figure out how to get ahead of whatever the next big driver of innovation and revenue is going to be for media services and also try and satisfy a market that is just really, really hounding companies for growth.

Marcus Johnson:

Spotify expects to add another 15 million MAUs, monthly active users and 7 million net new paid subscribers that would be roughly on par with previous Q2s, maybe a little bit better than the last one. And they're also expecting a Q2 revenue growth of 11%. That would be down though from the over 20% it saw last Q2.

Time now for the second half of the show. Today In Other News.

AI tools for Google Ads and is Peacock sustainable?

Story one. Danny, for our marketing and advertising briefing you just wrote that in a presentation called AI Powered Ads 2023, Google said it would launch generative AI tools for Google Ads allowing advertisers to produce creative campaigns. This was according to the Financial Times. Google's generative AI can create text images and videos based on material from advertisers, you point out. But Danny, the most important part of this article about AI tools for Google Ads is what and why.

Daniel Konstantinovic:

I think the most important sentence is with Google's announcement, the industry is fully racing toward widespread use of generative AI. So I think it's important to note that Google isn't the only company doing this. The other big one is Meta. These are the two biggest forces in advertising or in digital advertising. And there are all these big concerns about the legality of using these generative AIs, right? Is it legal for them to train the AI on images without the consent of the copyright holder? And it's just very unclear.

There are some rules coming out of the EU, but it's still a big question mark that has frozen advertisers in regards to using this. But with Google and Meta doing it, I think advertisers, especially smaller ones, will start to become a little bit more comfortable with the idea. I think this really has the most appeal for small advertisers, ones who can't spend big on creative and can easily produce a creative ad campaign.

Marcus Johnson:

I thought your point about, so legal issues surrounding generative AI, but also so Google side stepping those by putting the onus on advertisers to provide material that the AI is trained on for specific cases. So saying, look, you got to give us the right kinds of stuff because if you don't, then it's your fault.

Story two. Is peacock sustainable? Danny, you recently wrote that streaming service Peacock saw subscribers grow 60%, 6-0 year-on-year, reaching 22 million. Revenues were also up close to 50% nearing 700 million. However, Peacock's losses mirrored how much they made in revenue. So they also grew over 50% to over 700 million. Parent Comcast still expects

Peacock to rack up 3 billion in losses this year. But Danny, the most interesting sentence in your article on Peacock is what and why.

Daniel Konstantinovic:

I think that the company will have to turn on the revenue faucet eventually to prove it can stand its ground. I'm really interested to see Peacock continue to lose more and more progressively every quarter and not really see NBC punished in the same way that companies like Netflix or Disney have for overspending. Not that Peacock is really overspending. They're spending really heavily on content and on user acquisition and they are making big gains, a lot of new users are signing up for Peacock and it's rapidly climbing up there. But you still have to wonder how long it can go on, at what point will NBC start to worry that it's spending too much? They've warned investors upfront like, we're going to lose 3 billion this year, and I just wonder at what point that goodwill might run out and they might feel the pressure to really crank up revenues and if they'll be able to do it in time to avoid consolidating.

Marcus Johnson:

Yeah, you know 46% of brands and advertisers say they're allocating spending to Peacock for this year's upfronts making it the third most desired platform behind YouTube TV and Hulu, interestingly. And then I was looking at Nielsen's Gauge, which looks at TV consumption. Where are people spending their time when they're watching TV? 1% of all TV consumption is on Peacock. That includes streaming and also cable as well. And 1% of all TV's consumption is on Peacock. That's the same as HBO Max, but about half that of Disney+.

If you'd like to sign up to our marketing advertising briefing that Daniel writes for you can click the link below in the show notes. That's all we've got time for today.

Danny, thank you so much as always for hanging out.

Daniel Konstantinovic:

Yeah, thanks for having me.

Marcus Johnson:

And thank you to-

Daniel Konstantinovic:

Oh.

Marcus Johnson:

Sorry, go on.

Daniel Konstantinovic:

Just I was going to say I was prepared this time to respond to what you're saying unlike in the opening.

Marcus Johnson:

Well you wandered off.

Thanks to Victoria who edits the show, James who copyedits it, and Stuart who runs the team.

Thanks to everyone for listening in. We'll see you tomorrow hopefully for the Behind the Numbers Weekly Listen. That's an eMarketer podcast made possible by InMobi.