SPOTIFY TECHNOLOGY S.A. [1]

1. HISTORY OF THE COMPANY

Spotify company was founded in 2006 by two entrepreneurs, Daniel Ek and Martin Lorentzon, in Stockhold (Sweden).

Apart from developing the application, the first 2 years of the company were entirely dedicated to overcome one of its main challenges: obtaining the *intellectual licenses* required to stream music. These licenses are very difficult to obtain, as each country has its own systems and processes for agreeing on the terms for broadcasting. That's why, initially, they focused on Europe and decided not to expand in the United States, which they would do 3 years later.

A beta version of Spotify was launched in 2007, and it included the possibility of sharing playlists regarding users, leading to a viral growth. The final application was launched on October 7th, 2008 in Sweden, Norway, Denmark, UK and Spain. At the beginning, only two types of subscriptions were available: free (with ads and limited listenings for every song) and premium (ad-free, offline and unlimited). A few months later, the company launched the Spotify app for Android and iOS, leading to a significant increase in the amount of both premium and overall members.

On May 2010, Spotify announced two more types of accounts: Spotify Unlimited and Spotify Open, and on September it was announced as a Technology Pioneer for 2011 by the World Economic Forum (WEF). Starting 2011, the company achieved 1 million premium subscribers that was doubled by September that same year thanks to the partnership attained with Facebook, which created a viral network effect, gaining advantage over their competitors. They decided to significantly reduce the amount of hours that free and open Spotify subscribers could listen to music (10 hours per month) and limited the amount of plays per track to five. However, Premium and Unlimited users were not affected by this change, nor new users for the first six months.

[1] Case written by Juan Barenys, Mireia Falgueras, Maria García, Amadeu Roigé and Claudia Tarradellas, with the supervision of Professor Oriol Amat, UPF Barcelona School of Management, 2016.

A new application update was released on April 2013, adding new features like synchronized lyrics, music reviews, messages between users and browse, allowing the members to find playlists and charts created by others using filters such as genre, activity or mood. By winter of that same year, the application had more than 24 million active members and had registered over 4,5 billion hours streamed. From 2014 to 2016 Spotify entered into partnership with several companies like Uber, PlayStation and Starbucks, and also launched new features like a family plan subscription and improvements in the application like video and podcast playlists. They also launched a new feature that detected at what pace runners were going, and suggested tracks that matches its tempo.

One of the main challenges Spotify faces is its losses. Since the creation of the company in 2006, they have reported negative profits for the shareholders -this year, losses hit $194M. This is due mainly to the high costs they pay to record labels for the licenses of music. However, the company has been one of the most successful technological start-ups in recent years, as their revenues topped $2bn this year and have raised several rounds of capital -the last one, in June 2015, raised $526 million.

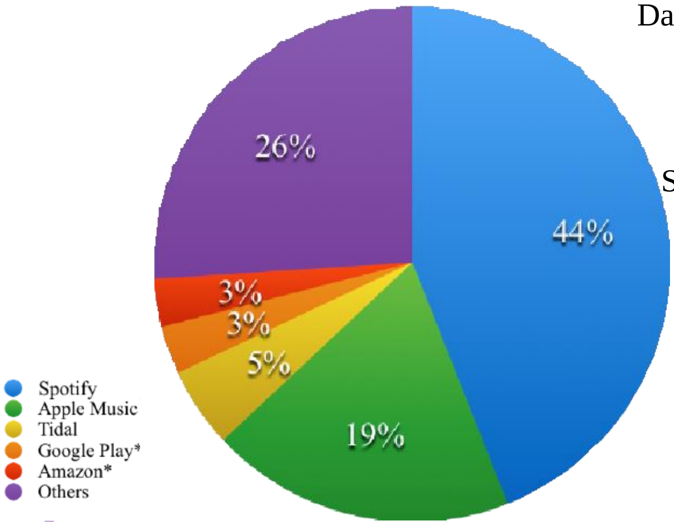
Another controversial aspect in the recent history of the company was the announcement made by some artists like Taylor Swift or Adele that refused to stream their music on Spotify: they complained that Spotify pays very little money for the licenses of music, and that this is very harmful for the music industry, specially for those artists at the beginning of their careers. However, the company claims in its website that they have paid until now 5 billion dollars to the artists and right-holders of the music.

2. INDUSTRY & COMPETITORS

The music streaming service industry is quite new: it arose in the late 2000s. However, the worldwide music streaming market is growing unexpectedly, with the major label companies collectively reporting an increase on streaming revenues of 52% in the second quarter of 2016 compared to the same period the previous year. Furthermore, according to IFPI, total streaming revenues growth ratio on 2015 was of 44% increase.

On the other hand, Spotify is located within another more general industry: the music industry, which in turn has recently faced one big challenge, the end of piracy. Illegal downloads have been a major threat for record labels and artists: between 1999 to 2009, total music sales decreased by more than 50%. So the music industry, which had been historically very powerful some decades ago, has lost now more than half of its customers because of piracy.

However, it’s seems that there’s still a little bit of hope for the music industry: the rapid decline in sales has begun to be compensated with the rise of streaming services such as Spotify, Apple Music, or Pandora in the United States. In 2015, revenue from streaming services accounted for 20% of all music industry revenue, and that is a quite impressive fact for an industry that didn’t even exist a decade ago. Furthermore, recent studies have shown that on-demand music streamers are 90% more likely to spend money on music and 50% more likely to spend money on event tickets.



Data from the market share of the streaming music industry shows that there are currently 5 main companies competing in the worldwide market: Spotify, Apple Music, Tidal, Google Play Music and Amazon Music, the graph on the left represent the market share of each of them. The 26% remaining percentage stands for other companies which offer similar but not exactly the same service or which service is limited to a number of countries, including YouTube, Pandora, Rhapsody, Deezer, rdio…

Apple Music has become one of the greatest growths in this field, with 11 million subscribers reached since its launchment in June 2015. But, has Spotify suffered from the emergence of this new competitor? It seems not: Spotify reached 40 million Premium users by the end of 2015 and $5 billion paid to artists and right-holders. In other words, despite the appearance of this new competitor, 2016 is being the best year in the history of Spotify.

Finally, the most important latest updates in the industry are related with the *going beyond music* features. It has become clear that users demand new and more personal ways to enjoy the music they like, they don’t have enough with listening to their music and playlists. That’s why all these 5 main competitors have recently launched new features that offer to the user the possibility to discover music by creating custom playlists, browsing music by generes or mood, launching their self radio stations… All these companies offer a combination between personal music collections and the streaming catalog being or not subscribed.

Regarding the product, the table below shows the different services that the main competitors of Spotify offer and at what price[2].

	Spotify	**Apple Music**	**Amazon Music**	**Tidal**	**Google Play Music**
Monthly fee	9,99 $	9,99 $	9,99 $	9,99 $/19,99 $ for Hi-Fi	9,99 $
Free option?	Yes, with ads	No	No	No	Yes, but limited
Free Trial Period	30 days	3 months	30 days	30 days	30 days
Music Library Size	More than 30 million	30 million	10 million	25 million	30 million
Maximum bitrate	320Kbps	256Kbps	256Kbps	256Kbps/1.411Kbps	320Kbps
Family sharing?	$5 per additional user	$14,99 up to 6 users	No	$4,99 / $9,99	No
Offline listening	Mobile and desktop	Mobile only	Mobile and desktop	Mobile only	Mobile only
Radio Stations	Yes	Yes	Yes	No	Yes
Podcasts	Yes	No	No	No	Yes
Music videos	Yes	Yes	No	Yes	No

Note that nearly all competitors offer almost the same exact service at the same exact price, there are only few differences in the quality of audio or the availability of podcasts and music videos.

That's why we can't conclude that Spotify's main source of differentiation has been the *going beyond music* philosophy, because their main competitors also offer the browsing and discovering features previously mentioned. For instance, they all use big data to track the musical tastes of every user and creates custom playlists based on the music they like.

The key question we should ask ourselves is: how did Spotify compete in a saturated market, with lots of companies offering exactly the same service at the same price?

3. PRESENT SITUATION OF THE COMPANY

Spotify is the worldwide leader application in music streaming, with more than 100 million users from all over the world and 35 million songs on its catalog.

[2] Percentage of market share for Google Play Music and Amazon Music Unlimited is based on estimations, as any of the two companies reveal the actual number of users they have.

Users can dive into Spotify using one of the two listening plans: Spotify Free or Spotify Premium. The free version serves audio and banner ads, manage your digital music files, and connect with others using the built-in social networking features. The $9.99-per-month Spotify Premium lets you hear select albums before they're released, play songs on demand, and cache songs for offline playback on your computer, phone, or other devices. It also increases audio quality. Spotify's revamped Family Plan now grants six people individual premium accounts. This new, lower-cost Spotify Family Plan directly competes with Apple Music and Google Play's month family plans.

You can access Spotify on a PC in two ways: by accessing the Web player or downloading the desktop app. The Spotify listening experience is similar regardless of how you access the service, but downloading the desktop client nets additional benefits. With the Spotify desktop app, you can view lyrics and add MP3 files to your music catalog. You cannot do either when using the browser- based Spotify. Besides the desktop client, there are Spotify apps available for Android, iOS, and Windows Phone.

From the human resources prospective, workers have many incentives. Spotify says that stronger salaries are required to be competitive and innovative. According to Spotify’s annual report, the average employee, from the more unqualified workers up to Daniel Ek (CEO), earns an average salary of €151,180. That means the average employee compensation has ballooned by 152%, despite losses.

From the progress prospective, one of Spotify’s operating principles is the idea of giving the consumer the most choice possible. No two people are like and not everyone will have the same needs and Spotify aims to give their customers choices. This is why Spotify as multi-levels of membership options and is available on a very of different platforms. It is also why Spotify now offers three levels of sound quality for mobile users.

The simple model is also a key success factor as the actual lack of sophisticated functionality has actually proven to be an asset: the app is very easy to use and anybody could learn how to use it within minutes.

One of Spotify’s biggest strengths is the fact that its platform allows access to a very large selection of music. Spotify comfortably uses cross-platform compatibility; it can be used on any online devise without having to convert data to a new format. That’s one of the main sources of advantage when compared to piracy. It is true that piracy is free, but the access to music is much more easier when using Spotify than downloading media files which have to be converted and exported on easy device that the user wants to listen in.

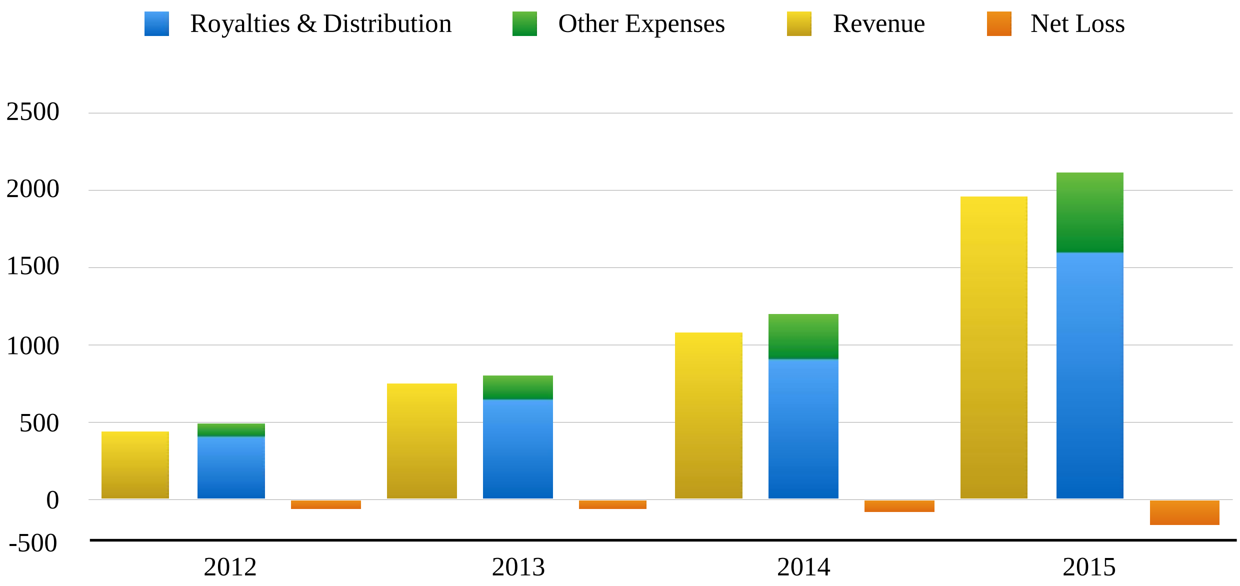
Spotify is a social music platform. It has strategically made connections with other services, such as Facebook. This provides its users with a sense of identity when creating playlists and sharing them with their friends, recommending songs and ergo, advertising Spotify’s brand.

From the clients perspective, Spotify built a large group a loyal brand advocates within it's first few years - which is almost unheard of in most industries (Skype being a exception). This undeniably contributed to their growth and success in subsequent years.

4. MAIN PROBLEMS AND CHALLENGES THE COMPANY IS FACING NOW

Despite its huge success, Spotify has also some weaknesses, especially regarding finance and their competitors.

- Cost of royalties: The royalties that Spotify pays out each month represent 70% of its total monthly revenue, and as software does not make enough money through advertisements or monthly fees this makes the company incur into losses. Spotify has paid to right holders $1billion since 2008, in 2011 the company faced net losses of €45,4 million and €58,7million in 2012. This means that the business remains heavily lossmaking. This lack of profitability is the reason why Spotify has received so many criticism, leaving investors and those within the industry concerned for its overall sustainability. Investors may not expect Spotify to be making a profit yet, but with no existing business in hardware or advertising that can generate enough profits, the company's future depends on figuring out how to manage its royalty commitments, running costs and investment in new features and countries and how to get more paying subscribers.


Royalties & Distribution
Other Expenses
Revenue
Net Loss
2500
2000
1500
1000
500
0
-500
2012
2013
2014
2015

- Piracy: Piracy is free, quick and it has a larger catalogue of music. Although piracy of music is illegal, Spotify has no choice but to compete with this, while earning money to pay out to its clients and remain a legal business, which is a difficult challenge to overcome. However, the challenge to completely eliminate piracy is becoming more of a reality as consumers are turning to free music platforms, like Spotify.
- Not having a large group behind to assume losses: despite having more users than Apple Music, Spotify doesn't have a determinant that Apple Music does: a large group behind. As it has been previously stated, music streaming companies usually have a large amount of expenses due to high costs of royalties and licenses, and not having a large group behind to assume losses may represent the difference between surviving or not surviving for the company in the long-run.
- Controversial issues with artists and rights-holders: As it has been said in the History of the Company section, Spotify has had some public controversies with well-known artists like Adele and Taylor Swift who refused to stream their music in Spotify because they complained that the company pays very few amount of money for the rights of the music.

Nowadays, Spotify is leading the music streaming service industry and has established a steady market niche for itself. Their app is available in 57 countries world-wide, but it still has lot of opportunities to grow, as the industry continues growing very fast. It has just started to expand in 2013, and it plans to continue growing in its current market this year, so we will surely see improvements in the company in the future.

5. QUESTIONS TO ADRESS:

1. What are the main qualitative strenghts and weaknesses of the company?
2. Is Spotify financially solid enough from the point of view of liquidity, debt, profit…?
3. Is the model subscription offered by Spotify sustainable? Should they reduce expenses?
4. Construct a Cause & Effect Diagram
5. Make recommendations to the company

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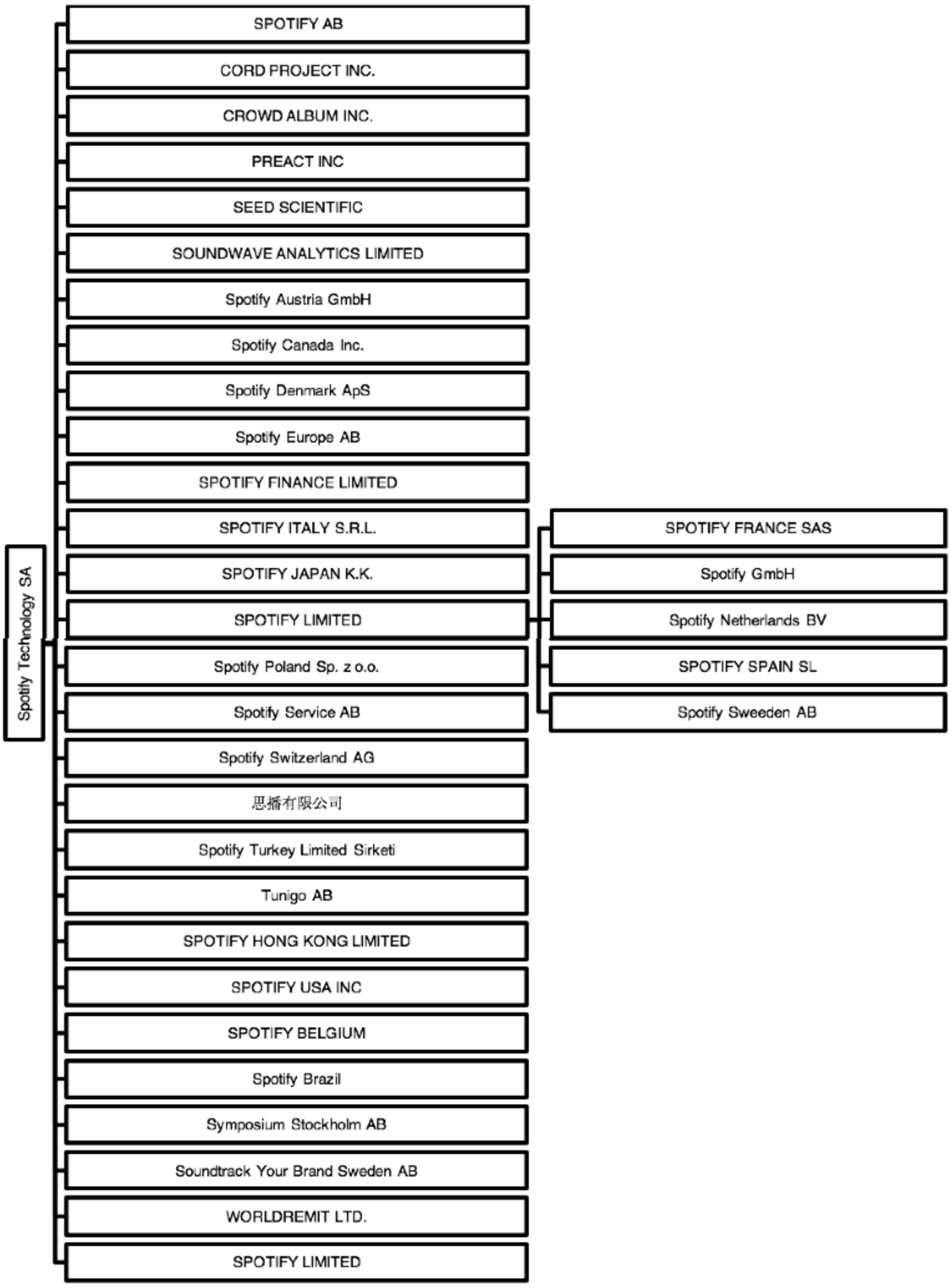
7. SOME PREVIOUS NOTES ON THE DATA AND SOURCES ANALYZED:

1. The company that we have chosen to analyze has been Spotify Technology SA, which has its headquarters and fiscal and tax residence on Luxembourg. The decision to choose Spotify Technology SA was motivated by the fact that it actually stands for the GUO (Global Ultimate Owner) or Highest Parent Company of the Group. Furthermore, the reported Balance Sheet and Profit & Loss Account has been classified as consolidated by the main auditor, Ernst & Young Luxembourg SA, which is also a commissioner in the Board of Directors.
2. Any space left in blank in the financial report is because there is no available information or because the company doesn't report any information about that specific value.
3. The cluster of companies with we have chosen to compare for the average ratios and values are the ones in *Programación, consultoría y otras actividades relacionadas con la informática* in the ACCID report (CNAE 62)


Spotify Technology SA
SPOTIFY AB
CORD PROJECT INC.
CROWD ALBUM INC.
PREACT INC
SEED SCIENTIFIC
SOUNDWAVE ANALYTICS LIMITED
Spotify Austria GmbH
Spotify Canada Inc.
Spotify Denmark ApS
Spotify Europe AB
SPOTIFY FINANCE LIMITED
SPOTIFY ITALY S.R.L.
SPOTIFY JAPAN K.K.
SPOTIFY LIMITED
Spotify Poland Sp. z o.o.
Spotify Service AB
Spotify Switzerland AG
思播有限公司
Spotify Turkey Limited Sirketi
Tunigo AB
SPOTIFY HONG KONG LIMITED
SPOTIFY USA INC
SPOTIFY BELGIUM
Spotify Brazil
Symposium Stockholm AB
Soundtrack Your Brand Sweden AB
WORLDREMIT LTD.
SPOTIFY LIMITED
SPOTIFY FRANCE SAS
Spotify GmbH
Spotify Netherlands BV
SPOTIFY SPAIN SL
Spotify Sweeden AB

	Average sector	Average sector with profits	2014	%	2013	%	2012	%	2011	%
Non-current assets	**41,71%**	**39,09%**	**109.239**	**23,12%**	**45.970**	**12,31%**	**27.695**	**10,32%**	**11.102**	**6,82%**
Intangible assets			58.259	12,33%	6.591	1,77%	7.471	2,78%	4.014	2,47%
Tangible Fixed assets			50.710	10,73%	38.941	10,43%	15.055	5,61%	7.088	4,35%
Other non-current assets			0	0,00%	438	0,12%	5.169	1,93%	0	0,00%
Current Assets	**58,29%**	**60,91%**	**363.279**	**76,88%**	**327.412**	**87,69%**	**240.667**	**89,68%**	**151.698**	**93,18%**
Inventory			0	0,00%	0	0,00%	0	0,00%	0	0,00%
Debtors			57.869	12,25%	36.777	9,85%	28.051	10,45%	24.388	14,98%
- Cash and cash equivalents			206.492	*	217.968	*	167.471	*	104.271	*
Other curent assets			305.407	64,63%	290.635	77,84%	212.616	79,23%	127.311	78,20%
Total Assets	**100,00%**	**100,00%**	**472.515**	**100,00%**	**373.382**	**100,00%**	**268.362**	**100,00%**	**162.800**	**100,00%**
Net Equity	**29,07%**	**35,88%**	**69.964**	**14,81%**	**101.546**	**27,20%**	**103.240**	**38,47%**	**68.526**	**42,09%**
Capital			405.145	85,74%	293.600	78,63%	77	0,03%	73	0,04%
Other shareholders funds			-336.181	-71,15%	-192.054	-51,44%	103.163	38,44%	68.453	42,05%
Non-current Liabilities	**22,00%**	**15,13%**	**20.382**	**4,31%**	**4.566**	**1,22%**	**85.563**	**31,88%**	**42.003**	**25,80%**
Long term debt	5,91%	2,35%	2.577	0,55%	0	0,00%	0	0,00%	0	0,00%
Other long term liabilities	16,09%	12,78%	17.805	3,77%	4.566	1,22%	85.563	31,88%	42.003	25,80%
- Long term provisions			17.805	*	4.566	*	85.563	*	42.003	*
Current Liabilities	**48,93%**	**48,98%**	**382.169**	**80,88%**	**267.270**	**71,58%**	**79.559**	**29,65%**	**52.271**	**32,11%**
Short term loans	2,23%	2,40%	1.705	0,36%	0	0%	0	0%	0	0%
Creditors	10,27%	10,05%	78.328	16,58%	71.594	19,17%	35.129	13,09%	24.780	15,22%
Other current liabilities	36,43%	36,54%	302.136	63,94%	195.676	52,41%	44.430	16,56%	27.492	16,89%
Total Equity and Liabilities	**100,00%**	**100,00%**	**472.515**	**100,00%**	**373.382**	**100,00%**	**268.362**	**100,00%**	**162.800**	**100,00%**

Spotify Technology SA
1610 Luxembourg
Latest Account Date: 31/12/2014
Case written by: J. Barenys, M. Falgueras, M. García, A. Roigé, C. Tarradellas

MAIN RATIOS	Average sector	Average sector with profits	2014	2013	2012	2011
DEBT AND CAPITALIZATION						
Debt = Liability / Assets	0,71	0,64	0,85	0,73	0,62	0,58
Debt Quality = Current Liabilities / Total Liabilities	0,69	0,76	0,95	0,98	0,48	0,55
Financial Expenses = Financial Expenses / Sales			0,02	0,00	0,06	0,19
LIQUIDITY						
Liquidity = Current Assets / Current Liabilities	1,19	1,24	0,95	1,23	3,03	2,90
Treasury = Debtors + Cash / Current Liabilities	1,15	1,22	0,69	0,95	2,46	2,46
Acid Test = Cash / Current Liabilities	0,43	0,55	0,54	0,82	2,10	1,99
Working Capital (real) (euros)			-18890,0(	60142,00	161108,0	) 99427,00
ASSETS MANAGEMENT						
Non-current assets turnover	2,63	3,35	9,90	16,25	2,60	0,72
Current assets turnover = Sales / Current aassets	1,89	2,15	2,98	2,28	0,30	0,05
SALES			1081726,	746858,0	71919,00	8025,00
Sales growth = Last year's sales / Previous year sales			1,45	10,38	8,96	
PROFITABILITY, SELF-FINANCING AND GROWTH						
Return on assets = EBIT / Assets	0,01	0,07	-0,35	-0,24	-0,20	-0,27
Return on equity = Net Income / Equity	-0,01	0,15	0,00	0,00	-0,57	-0,28
Cash flow / Sales	0,03	0,08	0,02	0,01	-0,69	-5,13
Cash flow / Assets	0,03	0,10	0,04	0,02	-0,19	-0,25

Ratios

	ROE =	EBIT/Sales	Sales /Assets	(Assets/ Equity) x (EBT/EBIT)	Net Profit/EBT
2014	0,00	-0,15	2,29	6,49	0,00
2013	0,00	-0,12	2,00	2,17	0,00
2012	-0,57	-0,74	0,27	2,88	1,00
2011	-0,66	-5,38	0,05	2,45	1,02

Breakdown of Profitability

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	2014	2013	2012	2011
A) CASH FLOWS FROM OPERATING ACTIVITIES				
1) EBT	-158.579	-53.817	-56.744	-44.524
2) Adjustments	**63500**	**50739**	**12847**	**5947**
(+/-) Depreciation	18.987	9.152	8.792	4.224
(-) Financial income	25.512,00	39.449,00	88,00	172,00
(+) Financial expenses	19.001,00	2.138,00	3.967,00	1.551,00
3) Cange in current capital	**443.611,24**	**594.682,00**	**280.239,00**	**181.669,00**
(+/-) Inventory	0	0	0	0
(+/-) Debtors and other accounts receivable	57.869,00	36.777,00	28.051,00	24.388,00
(+/-)Other current assets	305.407,00	290.635,00	212.616,00	127.311,00
(+/-) Creditors and other accounts payable	80033	71594	35129	2478
(+/-) Other current liabilities	302,236	195.676	4443	27492
4) Other cash flows from operating activities	**-18563**	**-2138**		
(-) Interest Payment	18563	2138	N/A	N/A
(-) Income tax payment / (+)Income tax revenue	3678	2078	1918	899
5) Cash flows from operating activities (1+2+3+4)	**329.969**	**589.466**	**236.342**	**143.092**
B) CASH FLOW FROM FINANCING ACTIVITIES				
9) Financial income (+)	25.512,00	39.449,00	-88,00	172,00
10) Financial expenses (-)	19.001,00	2.138,00	3.967,00	1.551,00
11) Financial Result	6.511,000	3.736,000	-3.837,000	-1.379,000
C) INCREASE / DECREASE IN CASH AND CASH EQUIVALENTS (5+8+12)	**336.480**	**593.202**	**232.505**	**141.713**
Cash and cash equivalents at the beginning of the year	217968	167471	104271	-
Cash and cash equivalents at the end of the year	-	217968	167471	104271

Cash Flow Statement

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	Average sector	Average sector with profits	2014	%	2013	%	2012	%	2011	%
Earnings	**100,00%**	**100,00%**	**1.081.720**	**100,00%**	**746.858**	**100,00%**	**71.919**	**100,00%**	**8.025**	**100,00%**
Sales			1.081.720	100,00%	746.858	100,00%	n.a.		n.a.	
Cost of Goods Sold	27,82%	27,12%	876.089	80,99%	614.523	82,28%	n.a.		n.a.	
GROSS MARGIN	**72,18%**	**72,88%**	**205.631**	**19,01%**	**132.335**	**17,72%**	**n.a.**		**n.a.**	
Other Expenses	28,53%	27,06%	370.721	34,27%	223.513	29,93%	n.a.		n.a.	
EBIT	**0,70%**	**5,03%**	**-165.090**	**-15,26%**	**-91.178**	**-12,21%**	**-52.865**	**-73,51%**	**-43.144**	**-537,64%**
Financial Income	1,18%	1,06%	25.512	2,36%	39.499	5,29%	88	0,12%	172	2,14%
Financial Expenses	2,05%	0,71%	19.001	1,76%	2.138	0,29%	3.967	5,52%	1.551	19,33%
Deppreciation and gains of financial diposals			6.511	0,60%	37.361	5,00%	-3.879	-5,39%	-1.379	-17,19%
EBT	**-0,17%**	**5,39%**	**-158.579**	**-14,66%**	**-53.817**	**-7,21%**	**-56.744**	**-78,90%**	**-44.524**	**-554,83%**
Taxes			3.678	0,34%	2.078	0,28%	1.918	2,67%	899	11,21%
Ordinary activities result			-162.257	-15,00%	-55.895	-7,48%	-58.662	-81,57%	-45.423	-566,04%
Total results	**-0,39%**	**4,21%**	**0**	**0,00%**	**0**	**0,00%**	**-58.662**	**-81,57%**	**-45.423**	**-566,04%**

Profit & Loss Account

1. **Identify main qualitative strenghts, weaknesses, opportunities and treaths (SWOP)**

	Strenghts	**Weaknesses**
Who	Founded by an enterepreneur Startup way of doing —-motivated employees (high salaries, high flexibility on schedules, bonus for extra goals…)	
What	First company in offering the service Spotify is world-wide leader (44% of international market share) Access to large music library (more than 35 million songs) Online music streaming industry (emerging and high-growth market)	High degree of competition Potentially saturated market — All companies offer very similar services with the same prices
How	Startup approach to growth — constant improvement and innovation is the only way to success Excellent customer experience Customizable service (set according to personal preferences) Offers unlimited Free Subscription	Extra-high quality of sound not offered (other competitors do) No synergies with personal library of music Free subscription forces the user to listen to ads

Opportunities	**Threats**
Consolidation as a market world-wide leader International expansion opportunities (emerging markets) Gain bargaining power among righ-holders Sinergies with other applications	Although they have very high revenues, they have been reporting losses since the creation of the company Appearance of new competitors with a more solid financial situation (Apple Music) Piracy (opportunity cost of not paying the monthly subscription to the service)

2. Identify main financial strengths and weaknesses

	Strenghts	Weaknesses
Liquidity		- Current ratio: 0.95 - Quick ratio: 0.69 - Negative Working Capital
Debts		- Debt ratio: 0,85 - Quality of debt ratio: 0,95
Asset Management	- Fixed-asset turnover: high - Current-asset turnover: high and increasing	- Fixed-asset turnover: decreasing
Sales	- High increase in sales	
Expenses	- Financial Expenses (0,02)	- Extremenly high costs of goods sold
Profit		- 0 Profits
Return		- ROE = 0 - ROA = -0.35
Self-financing		- No possibility of self-financing
Growth	- High growth in sales	- Very weak financial position

1. Liquidity

- Average liquidity ratios for profitable companies within the sector were 1.24 for the current ratio; 1.22 for the quick ratio; and 0.55 for the acid test. And Spotify's ratios in 2014 were 0.95, 0.69 and 0.54 respectively.
- Even though the acid test result matches the average of the sector, the current and quick ratios are significantly below the average of the sector. This in fact suggests that the company will struggle to meet their current obligations as their fall due: current liabilities are bigger than current assets and cash & debtors only represent 69% of current liabilities.
- There is a big gap between working capital needed (132.844) and actual working capital (-18.890). There is definitely a liquidity problem. (Check Part 3: Topics Specially Relevant for the Company — Working Capital)
- Z score: Performing the Z score we obtain a negative value, that menas that the company is in risk of default.

Z score	-1,6	+ 6,1 * (E/A)	+ 6,5(NP/A)	+ 4,8(NP/Eq)
-0,746	-1,6	0,854	0	0

Z Score: Amat, Anton and Manini, 2016

2. Debt

- The average sector debt ratio and debt quality ratio in profitable companies were 0.64 and 0.76 respectively. In 2014, Spotify registered 0.85 debt ratio, which is approximately 25% above its industry average. Moreover, the quality of debt ratio was 0.95, also above the industry's average. Financial expenses, however, represented 2% over total sales, which is a common percentage for most companies.
- The company's deb ratios are above the industry ratios, which implies that there is an excess of debt in the company and that the debt quality is not very good, as current liabilities -liabilities that have to be paid in a year or less- represent 95% of total liabilities.

3. Asset Management

- The fixed-asset turnover ratio since 2011 until 2014 were 0.72; 2.59; 16.24; 9.90. The highest growth period was in 2013, with a 625% increase relative to the 2012 period. However, from 2013 to 2014 it has suffered a 60% decrease, which suggests that assets management was worsen during the period.
- The current-asset turnover ratio since 2011 until 2014 were 0.05 ; 0.29 ; 2.28 ; 2.97 respectively.

  Together with the fixed-asset turnover ratio, the company had highly improved their asset management during the 2012-2013 attaining a 760% increase. However, differently from the fixed-assets management, it kept improving, but at a slower pace.

4. Sales

- Spotify's sales have always raised every year: the sales growth ratio has always been positive and quite high, so sales are a financial strength for Spotify.
- However, we can observe that this increase has been reduced in the last years, going from an enlargement of 1038% in 2011 to a 145% in 2014. This is due to the fact that Spotify is a technological start-up which operates in a very new sector, the online music streaming sector, that experienced a high growth in the very first years of the 2010's decade but that it reached a more stable growth in recent years, so it was almost impossible to maintain such a high level of growth every year.

5. Expenses

We will distinguish between the different types of expenses in the income statement.

- First of all, the cost of goods sold, which represent an 80%-81% of sales while in the average of the industry it is just a 27%. This means that the company uses 80% of its revenue just for paying the costs related to production and marketing.

- Secondly, Financial Expenses. Although in the last year it has increased a bit (1.47% points higher), it has suffered a continuous reduction, from the 19.33% in 2011, reaching a mark of 1,76% in 2014. This decrease has allowed them to allocate in a quite good position below the average of the sector (2.05%), but they still haven't reached the levels of those companies having profits (0.71%).

6. Profit

- Since it was born, Spotify has never reported positive profits. We can observe that until 2012, the firm has had huge losses, and that in years 2013 and 2014 it hasn't experienced profits nor losses.

7.Return

Given that the company hasn't had profits in the last two years, the return generated by equity or assets is very small or even negative.

- Return on Assets (EBIT/Assets) is -0.35. The negative value of ROA is due to the fact that Earnings Before Taxes are negative.
- Return on Equity (Net Profit / Equity) takes a value of 0 as there are no profits.

If we look at the Parés breakdown of profitability, we can check that:

- EBIT over Sales, which informs about the margin (how much the firm has spent before paying interests and taxes) takes a negative value (-0,15), so spendings are higher than earnings at this stage of the Income Statement.
- Sales over Assets, which informs about the efficiency of assets, takes a very high value (2.29). That is because technological firms usually generates lotes of sales with a few amount of assets.
- Assets over Equity x EBT over EBIT, which relates the level of debt with the interest costs, takes a very high value (6.49).
- Net Profit/EBT, which informs about the impact of taxes on business ROE takes a 0 value, as profits are 0.

8. Self-financing

Spotify doesn't report any information on the dividends the company distributes. However, we have some data that makes us think there is no reinvestment on the profit the company generates.

- Net Profits have been 0 the last two years -the company has not generated any profit- so none profit can be reinvested on the company
- Equity has been decreasing overtime (from 42% in 2011 to 15% in 2014), probably to compensate for consecutive losses.

9. Growth

Although the growth of sales are very high, the company is in a very weak financial position

- On the one hand, we could classify Spotify as a high-growth company in terms of sales, because sales growth has been than 100% in all years (the company doubles the previous year sales).
- On the other hand, ROE and ROA are negative or 0, there is a high level of debt and there are no profits, so the company is in a very weak financial position.

3. ANALYZE TOPIC SPECIALLY RELEVANT FOR THE COMPANY

3.1 Working Capital Analysis

	2014	Average Sector	Ac. Sect. with Profits
Working Capital (CA - CL)	-18,890	1,273,738	880,916
Working Capital Nedded*	132,844		
Working Capital Surplus	-151,734		

*To perform the calculations of the minimum cash required, we consider 10% of the sum of creditors and other current liabilities

There is a big gap between the Working Capital Needed and the actual working capital of the company. Therefore, we can confirm what it was previously stated in the Liquidity Analysis, that the company has strong liquidity problems and that may have difficulties facing

3.2 Breakdown of revenues and customers: premium and free customers

As it has been explained in the first part, Spotify offers nowadays two different types of subscriptions: premium subscription and free subscription. Given that the firm is having strong losses, we should consider if offering these 2 subscription options is convenient or not for the company.

We will first analyze the percentage of users of Spotify who use a free and a premium account. By 2014 there were 50,000,000 total users of Spotify: 37,5000,000 free users (75%) and 12,500,000 premium subscribers (25%).

Total revenues in 2014 were 1,081,720€: 978,565€ (90,46%) came from the monthly payment of premium subscribers and 98,823€ (9,54%) came from companies who paid for the ads free users listened.

In other words, 90% of the revenues of Spotify come from the 25% of , while the remaining 10% of the revenues come from the 75% of users. And this gap is increasing by 2015: free users are growing much more faster than premium subscribers do. Spotify should reconsider their model of subscription, as it can been proved that it is highly unsustainable.

	November 2014	%
Total Users	50,000,000	100%
- Premium Subscription	12,500,000	25%
- Free Subscription	37,500,000	75%
Total Revenues	1,081,720	100%
- Premium Subscription	978,565	90,46%
- Free Subscription (Ads)	98,823	9,54%

Figure A
Total Revenue
(2014)

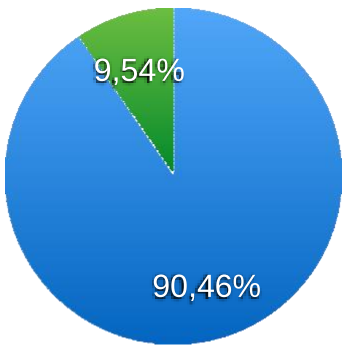
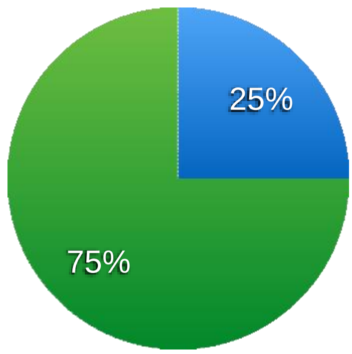
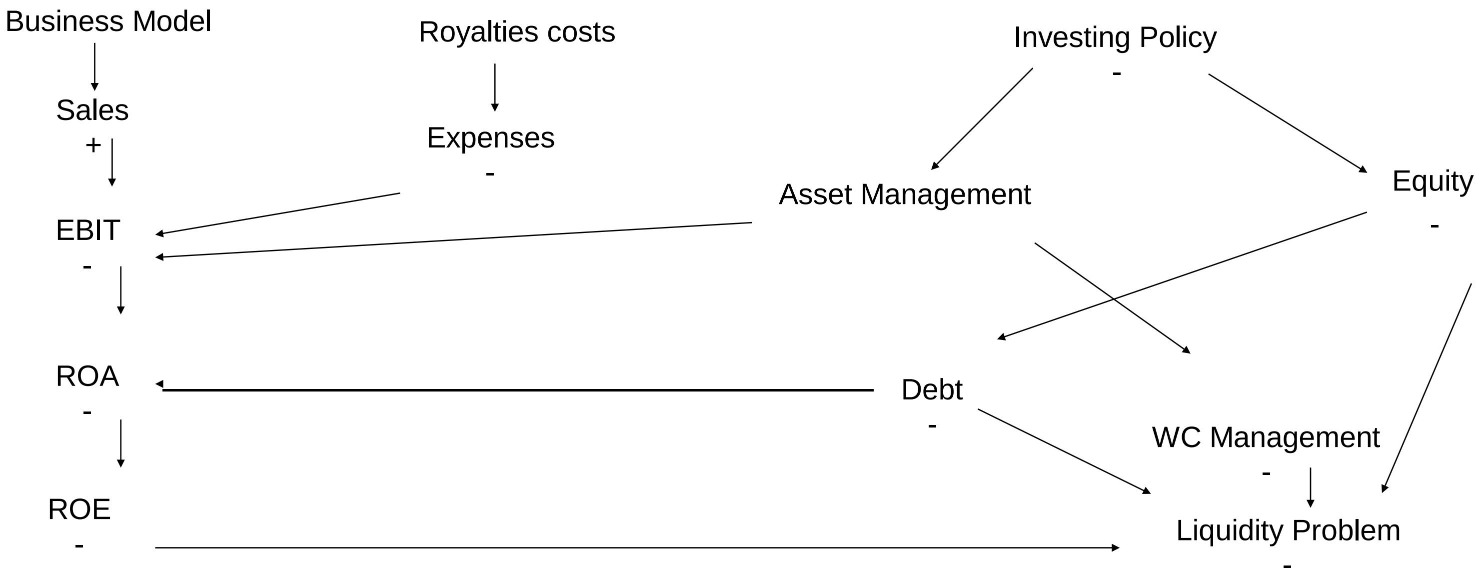


Figure B
Total Users
(2014)



Premium
Free Subscription (Ads)

4. Cause & Effect Diagram



5. Recommendations

Summing up the Cause & Effect Diagram above, we could say:

- There is a very good Business Model (world-wide leader, high-demand sector…) that produce very high sales (increasing more every year).
- However, there are high royalties costs which need to be covered, harming the EBIT, the Net Profit, and also the ROA and ROE.
- A very bad investing policy with low Equity and very high short-term debt, which makes the company face high liquidity problems.

That's why, our recommendations to the company would be:

1. Reach a new agreement with right-holders and discographies in order to reduce royalties and therefore reduce expenses by 19%.
2. Transform 30% of short-term debt into long-term debt.
3. Increase Equity by 10%

5.1 Reduce expenses

	Last Income Statement	**Impact of Measures**	**Income Statement After Measures**
Expenses	876,089 €	(-19%) = -166,456 €	709,633 €
Gross Margin	205,631 €		372,087 €
EBIT	-165,090 €		1,366 €
Net Profit	0		166,456 €

We previously stated that the enormous cost of royalties is the main threat for the company. Therefore, by reaching an agreement with the right-holders and reducing cost of goods sold, all values in the Income Statement Increase, ending up with a higher EBIT and Net Profit.

5.2. Convert short-term debt into long-term debt & Increase in Equity

	Last Balance Sheet	Impact of Measures	Balance Sheet After Measures
Increasing Equity by 10%	Equity = 69,964€	Equity +10% = +6,996€	76,960 €
Transform 30% s.t. debt into l.t. debt	Short-term debt = 382,169€ Long-term debt = 20,382€	↓ 30% s.t = -114,650€ to l.t = +114,650€	S.T. debt =267,519€ L.T. debt = +135,032€
Capital Structure	Equity = 0,14 Liabilities = 0,86		Equity = 0,17 Liabilities = 0,83

By doing a debt swap, we achieve a lower level of short term debt which reduces risk of having liquidity problems. By increasing equity, we achieve a better capital structure (less percentage of debt) but it is still insufficient.

5.3. Impact of measures on values

	Before Measures	Measure	Impact of Measures
Liquidity (CA/CL)	0,95	↓short-term debt	1,35
Working Capital	-18,890 €	↓short-term debt	95,760 €
Quick Ratio	1,15		
ROA	-0,35	↓Expenses	0,02
ROE	0	↓Expenses ↑Equity	2,16

There is also positive impact on some values that were previously problematic:

- When transforming short-term debt into long-term debt, liquidity ratio improves a lot as well as working capital, which is now positive. Quick ratio also increases as a result of a decrease in short-term debt.
- By reducing expenses, we achieve a higher ROA, as EBIT increases. ROE also increases as a result of an increase in Net Profit.

6. Balanced Score Card