Goldman Sachs

The Business of the Music

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The music industry, propelled by the rise in music streaming services, has seen the value of its assets skyrocket. We sat down with Goldman Sachs' Aaron Siegel to discuss how the industry is seeking to grow in the midst of a pandemic.

In early June, Goldman Sachs took Warner Music public in one of the largest US initial public offerings this year. What does that IPO say about the industry?

Aaron Siegel: There's been an enormous resurgence in the valuation of music assets. We saw strong investor interest in Warner Music's initial public offering — which priced in the upper half of the expected range and has since traded higher. Despite the COVID-19 disruption, we were able to execute the roadshow virtually and reach a strong investor base in a shorter period of time.

Warner's IPO follows a period of growing valuations in the private M&A market, including a Tencent-led consortium's investment in Universal Music and the sale of EMI Music Publishing to Sony. All three of these transactions reflected substantial growth in value for the owners of the music businesses, who, like Access Industries with Warner, had purchased or owned these businesses during a period of challenge and transition for the music industry. Access invested approximately $1 billion in equity to purchase Warner Music in 2011 (a transaction that was announced before Spotify had launched its service in the US); today, Warner Music's market capitalization is approximately $17 billion.

What has contributed to that growth?

Aaron Siegel: The Warner Music IPO echoed many of the same themes expressed during Spotify's direct listing two years ago — in particular the extraordinary value created by the collaboration of artists, music content owners and the music streaming services. The industry has undergone a complete renaissance.

When I started covering the business 17 years ago, the music industry was in the midst of online piracy challenges and collapsing CD sales. It was depressing at times for the music companies – particularly when they were forced to cut costs to try and preserve profitability. The paid streaming model brought the business back to health again. The industry in the early 2000s was massively shrinking. Today, it's seeing sustained long-term growth. Warner Music's recent listing is a testament to the industry's strength.

What accounts for the popularity behind the streaming model and how will the industry expand from here?

Aaron Siegel: The value proposition for consumers is extraordinary which has driven widespread adoption around the world. It's consumer friendly, with applications that get delivered to consumers when they want, while the research and development invested in the digital platforms creates personalized recommendations and strong playlists. Consumers typically pay a small monthly cost for "all-you-can-access" music. Since many of these services offer a free tier to allow consumers to try out the service, the conversion rates to becoming paid subscriptions are very high. The flexibility of an on-demand service has only reinforced the value of these streaming services during this period of dramatic change for everyone's work, commutes and living schedules.

There is still meaningful headroom for continued growth in paid subscriptions as consumers continue to adopt music streaming around the world – in both developed markets and emerging markets. And there are also promising signs for growth in pricing for the music industry. In some markets that were early adopters, such as Sweden, Spotify has begun to experiment with higher pricing, while Amazon Music is offering a higher pricing tier for a higher level of audio. The industry is primed for overall growth as well as the potential for higher pricing over time.

How have changes in consumer behavior affected the music industry?

Aaron Siegel: The consumer is absorbing more audio content than before partly because of the popularity of AirPods and wireless earbuds, as well as the proliferation of smart speakers and devices in homes, many of which are typically used to play music. Both trends are broadening the consumption of music as well as the type of music that gets played. For example, parents who set up a smart speaker in their child's bedrooms are more likely to stream child-focused songs, which opens up new catalogs of music. People are interacting with music more and in different ways through the proliferation of audio devices across our lives. And every year there are new services that incorporate and license music, like Peloton for example, that deepen consumer engagement with music and broaden the industry's revenue base.