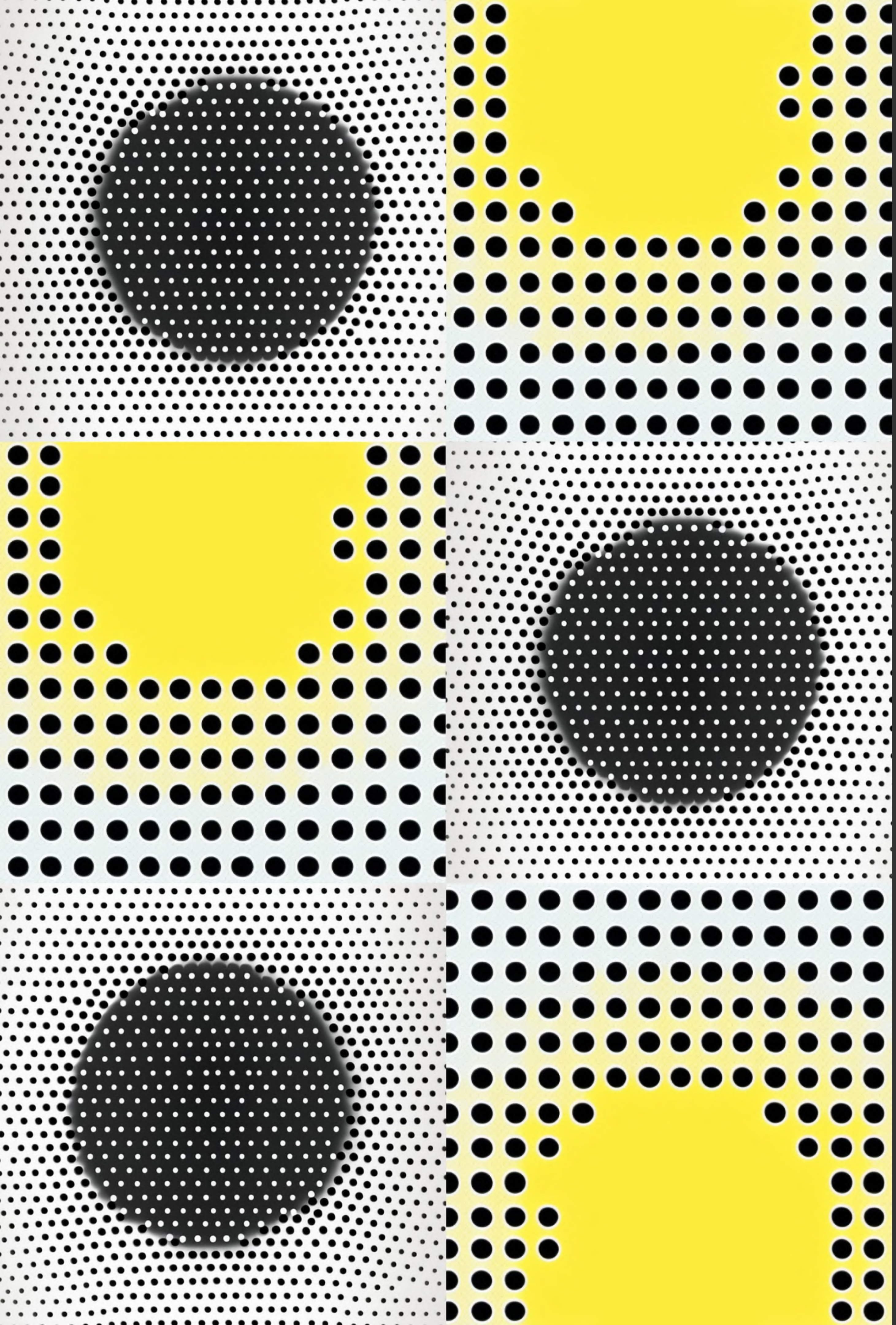

Water
& Music

Starter Pack:
An Introduction to Music Streaming Platform Models

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Who is this by?

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Who is this for?

Anyone interested in getting a better grasp on streaming economics and operations — especially:

- **Artists and their teams** seeking to understand the basics of streaming platform operations and payout models, to better **calibrate strategies and maximize financial sustainability**.
- **Builders** looking to **develop products in or adjacent to streaming** who require a foundational understanding of music streaming operations.

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Setting the Stage

Mo' Money Mo' Problems

Streaming is one of the music industry's most critical and contentious topics.

The format generated **$17.5 billion** worldwide in 2022, encompassing **67% of global recorded-music revenue.**

Since its inception, Spotify has paid almost $40 billion to music rights holders, while Apple Music paid over 5 million recording artists in 2020.

Yet, in an increasingly competitive market, it's more complicated than ever for artists to make a living from streaming.

We hear consistently from artists and their teams that the basics of streaming payments are still broadly misunderstood.

Often, analyses only concern per-stream pay rates, and overlook the underlying payment mechanisms and their consequences for artists' release strategies.

We hope to address those knowledge gaps by providing a high-level overview of the streaming business and its payment models, to help artists develop better strategic and tactical approaches for navigating this complex landscape.

Catalog-Centric Platform Strategy

Understanding different streaming business strategies and their associated incentives is essential to developing a game plan as an artist.

Virtually all major streaming platforms today operate under a **catalog-centric structure**, where the primary value propositions provided to listeners are:

- **CATALOG VOLUME:** The platform aims to provide access to the most extensive song library possible.
- **DISCOVERY:** The platform offers unique tools, like proprietary recommendation algorithms, to help listeners discover new music.

Most major DSPs license catalogs from all major labels and indies, while unsigned artists get distribution access to these platforms via third-party distributors like TuneCore and CD Baby.

This **all-you-can-stream** approach optimizes for breadth of listening across platforms' sprawling catalogs, to keep listeners' attention and engagement (even if passive) and improve free and paid user retention.

For further reading on catalog access and discovery, check out Bas Grasmayer's Water & Music article, "The rise of the fan-centric music streaming service."

Consequence: Platform Power Dynamics

Tech platforms and content aggregators are intermediaries — and streaming platforms are no exception.

Under a catalog-centric model, streaming platforms are not so much music discovery engines as they are music discovery *brokers* — building their business model around a "two-sided marketplace" that extracts value from artists who are hoping to reach the right audience.

Currently, in their push for distributed engagement across a wider catalog, streaming platforms arguably form a **wedge between fans and artists**, forcing them to leave streaming platforms to engage with each other directly.

"[Platforms] own the data, social graphs, and end user relationships — all of which creators need in order to access audiences and income ... in the majority of cases, this type of capital cannot be easily ported over to external, creator-owned properties. In this way, creator labor is controlled and commoditized by platforms."

Li Jin, Co-founder, Variant Fund

Power Play: Data Use and Withholding

As an intermediary between artists and fans, streaming platforms **control key data that could benefit artists as they seek to strategically develop audiences and build sustainable careers.**

From the artist's perspective, platforms could be more forthcoming with collected data. Platforms provide artists with limited insights, including listener engagement, and maintain power by withholding information.

By siloing data, platforms **limit artists' ability to assess the fan journey across the many platforms they use to engage their audiences.**

Spotify for Artists is an excellent example. Artists can access basic stats like listener streams, follower counts, and top-line demographics. However, surface-level data is only sometimes actionable for artists looking to develop comprehensive marketing campaigns across all platforms.

"Facebook and Spotify silo their raw user data from each other and from third parties (for legal and competitive reasons), [so] ***there's no way to paint a complete picture of the fan journey*** *from the first ad impression across their engagement with the album on Spotify over time, let alone to determine how that journey looks different across various listener segments."*

Cherie Hu, Water & Music

Advertisers <> Artists

By controlling the algorithms and platforms where listeners consume music *and* the data that audience creates, **streaming platforms can monetize artists who need these platforms to reach their fans**, leveraging vast captured data by selling marketing tools and services for artists.

By controlling the playlist algorithms that significantly determine what music gets streamed (and therefore who gets paid), **platforms create the playground and charge artists to get to the top of the slide** — making them advertising-first, rather than music-first, businesses.

CASE STUDY: *Spotify's **Discovery Mode** might be the best example of a service designed for artists to pay for access to the top of the curation pile. This features lets artists take a reduced royalty rate on individual songs in exchange for having them amplified in the platform's personalized listener recommendations.*

"The days of Spotify Premium being 'ad-free' are officially behind us."

Cherie Hu, Water & Music

How Artists are Paid from Streaming

Dividing the Pie

Streaming payment models assign values to beneficiaries from the release and consumption of music.

Streaming is a zero-sum game for listeners' attention, and payment models attempt to balance competing values within this ecosystem by allocating revenue across multiple stakeholders.

Each payment model has tradeoffs; there is no perfect system.

Recent indications from major labels suggest that rethinking streaming payment models is now on the table.

For now, we'll focus on providing explanations of the two primary payment models used by major DSPs:

- **Pro-rata payments** — the most common model for DSPs, used by Spotify, Apple Music, and more.
- **User-centric payments** — the oft-proposed alternative to pro-rata. Used by SoundCloud for some artists.

It's worth noting that there are various theoretical revenue-sharing models, including systems focused on payout by types of listener engagement, that have yet to materialize.

PRO-RATA

Stream-Share or Bust

Pro-rata payment is the most common model across streaming platforms. Spotify and Apple Music use this model, along with Tidal and SoundCloud, for most artists.

The public discourse regarding music streaming payments often focuses on an average "cents per stream" number for each platform (for example, the infamous 0.003 cents per Spotify stream).

The problem is that these comparisons don’t accurately capture how streaming services calculate individual payouts, or what this means for artists.

So how do pro-rata streaming payments work?

Pro-rata models utilize **stream-share** — meaning that after the streaming service takes a cut off the top (roughly 30%), they split the net monthly revenue (ads + subscriptions) among artists and rights holders based on each track’s share of total streams.

For example, if an artist’s tracks get 10% of the total music streams on a given platform in a month, they will receive 10% of all the revenue for that month after the platform takes its fees.

PRO-RATA

Scale is Everything

Under a pro-rata model, each stream is valued equally, regardless of its source. As a result, artists are incentivized to focus on generating a large number of streams across as many listeners as possible, in order to maximize their overall stream-share.

Put differently, **pro-rata models encourage artists to focus on streaming *at scale*, as a way to maximize financial payouts and increase their chances of financial sustainability.**

This focus on scale has the added effect of influencing the strategies artists use when releasing music. For example:

- Releasing **large quantities of music as quickly as possible**, to create more opportunities to boost streams.
- Focusing resources to acquire **playlist placements** and drive streams to the broadest audience.
- Producing **shorter tracks** to encourage repeat plays.

Pro-rata systems inherently favor artists who can scale listenership, producing a long tail of artists who struggle to achieve financial sustainability. For example, in 2022, ***only 57,000 artists of the more than 9 million uploaders to Spotify (less than 1%) generated over $10,000 in recording and publishing royalties.***

USER-CENTRIC

Direct-to-Artist

The most common alternative to the pro-rata system is a **user-centric payment system**, which DSPs like SoundCloud and Deezer have implemented or explored.

Unlike with pro-rata, user-centric systems ensure that the money users pay for their streaming subscription **only goes toward the artists they listen to**.

For example, under user-centric streaming, if you paid $15/month to subscribe to a platform and only listened to one artist, your entire $15 subscription fee would go to that artist after platform fees.

In this way, user-centric models **prioritize fan engagement over scale.**

While user-centric payment systems have been debated and studied for years, they've only been tested recently (e.g. on SoundCloud). For more on user-centric models, we recommend checking out Music Ally's fantastic rundown of existing research, as well as MIDiA's research exploring the outcomes of SoundCloud's specific fan-powered model.

USER-CENTRIC

Fan-forward Incentives

User-centric payment models incentivize artists to focus on building a group of dedicated superfans, rather than aiming to maximize their overall stream total overall.

In this format, **the more artists can engage fans to listen to their music often, the more revenue they generate.**

User-centric systems incentivize artists to focus on developing a core fanbase through activities like:

- Attracting **repeat listeners**, versus just prioritizing playlist placements.
- Developing a **narrative and world** that will capture and sustain fan attention over time.
- Using channels like **mailing lists and Discord communities** to provide opportunities for direct fan engagement.

User-centric payment systems provide increased opportunities for the long tail of small and mid-tier artists to use streaming to produce revenues. For example, MIDiA's recent evaluation of Soundcloud's fan-powered royalties (FPR) model found that, under FPR, ***63% of artists with 100 to 100,000 fans earned more than they did under the pro-rata system.***

Factors Impacting Artists' Streaming Performance

Five Major Success Factors

Democratization

Decreasing tech costs and trends like AI are quickly **growing the availability of easy-to-use music creation tools**.

Oversaturation

With 100,000 new songs ingested by Spotify every day, artists are **competing with each other** for listeners' time and attention.

Catalog Music

Emerging artists are **competing directly with existing stars**, who have a firm hold on a large share of existing audiences.

Size of the Pie

Subscriber and revenue growth **cannot keep up with the rate that new music and artists are joining** streaming platforms.

Listener Behavior

Fan listening is constantly evolving, and the way platforms respond to it is likewise changing in response.

Democratization

The last decade has seen giant leaps in the availability of tools for creating and distributing music.

In particular, the recent rise of creative AI tools makes it easier for non-musicians to turn ideas into finished songs and upload them directly to streaming platforms in record time.

These changes **democratize the music creation ecosystem,** while leading to **market saturation and greater competition among artists.**

CASE STUDY: *For more on how the development of AI music technology is accelerating the trend of democratized music creation, check out our Season 3 series of reports on Creative AI.*

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Oversaturation

The music streaming ecosystem reflects an increasingly saturated environment where individual artists compete for listeners' time and attention.

The rate at which new songs are arriving is increasing nearly exponentially:

- Spotify ingests **100,000 new songs daily**.
- Apple Music recently passed the **100 million song milestone**.
- Of **196 million ISRCs** in Luminate's system at the end of 2022 (including audio and video), **46% were created since the beginning of 2020.**

The competition for listeners is only getting more fierce, creating a challenging environment for artists to earn sustainably from streaming.

The Impact of Catalog Music

Navigating the competitive streaming landscape is even more difficult for emerging artists, who compete directly against established artists who have a foothold with listeners — a.k.a. "catalog music."

Industry data confirm this uphill battle for newer artists. Luminate, for instance, reports that **catalog music claimed a whopping 72.2% of the US music consumption market in 2022**, up from 69.8% in 2021.

Read more from Tatiana Cirisano on the uneven playing field of the modern music streaming landscape.

Size of the Pie

While changes in payout models impact how the overall streaming revenue pie is split, platforms must **increase the total revenue they generate** to grow the streaming pie as a whole.

There are two means of doing this, each with their own caveats:

Increasing prices. Subscription streaming prices have stagnated for years, and only recently have Apple Music and Amazon Music increased their overall subscription prices in Western markets. While these price increases are a good sign, they ultimately represent relatively minor growth in overall revenue for these platforms, and hardly the step change required to keep up with the rising amount of uploaded music.

Adding more users. This equation is simple: More users lead to more revenue. And yet, all signs point to an uphill battle for streaming services when it comes to user growth.

Recent analysis suggests that overall, year-over-year user growth may be slowing, due to the maturation of Western markets where streaming users may be nearing a peak.

Fan Listening Behavior

A few key trends in fan listening behavior include:

Passive Listening — i.e. background listening to cater to a specific mood, time of day, or activity.

- The trend explains the massive growth of algorithmic playlists with titles like "Mood Booster," "Deep Focus," and "teen party," and the cult-like following of lofi-beats playlists on YouTube.

Social Media Discovery — i.e. fans discovering music through their social feeds (think TikTok videos scored by soon-to-be-favorite music), then moving to streaming platforms for repeat listening.

According to Luminate, **64% of Gen Z TikTok users discover new music via short-form video clips**, making it the top source for music discovery for the younger demographic.

The Segmentation Problem:
Streaming platforms ultimately put all fans in the same bucket, and charge them each the same rate. As a result, fans can't contribute to artists directly, and artists can't reward their fans for their listenership on the platform.

Key Takeaways for Artists

Key Takeaways for Artists

Reminder: The goal of this presentation is to explain the structures and incentives underlying streaming platforms to help inform and drive artist action towards more sustainable careers.

Whatever streaming platform you have a presence on as an artist — it is important to understand the **structures and incentives they create.**

To leverage the incentives that streaming platforms have established, artists should consider the following when making decisions about where to spend their time and resources:

- Platforms are intermediaries between artists and fans that are increasingly pushing artists towards paying for advertising. **Allocating spending strategically across streaming platforms** is necessary to stand out.

- **Strategies must align with the platform**. Pro-rata models push artists to allocate resources towards attaining playlists and scaled plays, while the user-centric model encourages artists to build more deeply engaged fanbases.

- The hyper-saturated media environment is the lens through which artists should consider how and where they foster their fan communities. By **understanding the different factors shaping streaming music engagement** — oversaturation, catalog music, fan listening behavior, and more — artists can better position themselves to break through to audiences and attract new fans.

APPENDIX

Water & Music's previous streaming coverage

If this high-level introduction to streaming platforms has whet your appetite for more, Water & Music has an archive of articles that go deeper on the music streaming ecosystem. Dig in and enjoy!

🔗 What "Spotify Teardown" Means For Artists, Fans and Journalists
🔗 Streaming" isn't "direct-to-fan": The problem with Spotify's new Stories for Playlists feature
🔗 The rise of the fan-centric music streaming service
🔗 Gen Z's take on the future of new music discovery
🔗 How to build a truly "fan-centric" online music experience
🔗 The direct-to-fan tech stack for artists
🔗 Is music streaming part of the "passion economy"? It's complicated
🔗 The latest music-streaming user numbers and differentiation: What you need to know
🔗 Just how difficult is it to make a sustainable living from streaming?
🔗 How Spotify's new advertising strategy impacts artists
🔗 Artist-facing music business software is far behind Silicon Valley

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