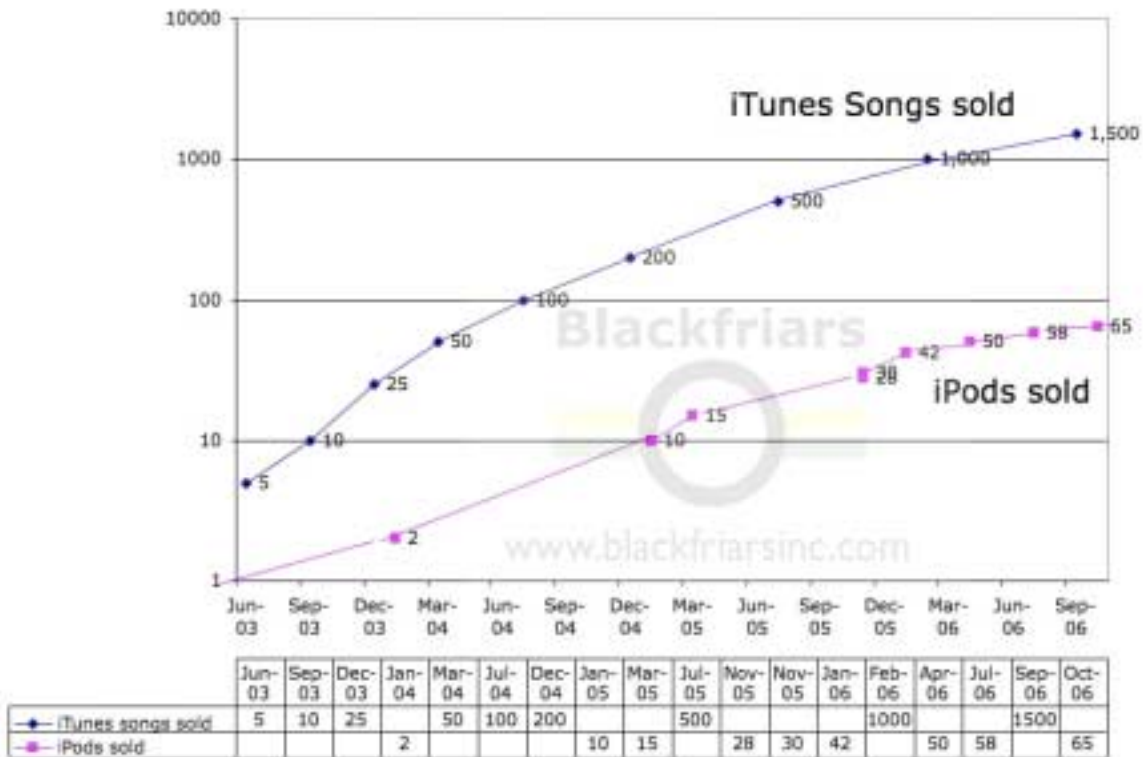




Tuesday, December 12, 2006

Do the math: iTunes sales aren't collapsing



Graph of three years of iTunes and iPods sales.

I always enjoy Forrester's Josh Bernoff's writing and analysis, but we often don't see the same data the same ways. So when I read yesterday's New York Times quick article claiming that iPods aren't driving iTunes sales, I decided that they must have misquoted him. When I saw today's article in The Register claiming that iTunes sales are collapsing, I decided there was enough silliness being repeated over and over that I had to run some numbers myself.

The data point in question in the New York Times is from this quote:

Although both [iTunes and iPod sales] are successful, the relationship may not have worked out exactly as expected. At any given point, the cumulative number of songs sold by the iTunes store has generally been about 20 times the cumulative number of iPods sold, according to Forrester Research, the technology consulting firm. That ratio has recently crept up to roughly 22 to 1, as 1.5 billion songs have been sold. The figures were compiled from public statements by Apple.

The numbers suggest that iPods are not driving iTunes sales as much as early supporters may have expected.

The graph above looks at cumulative iPod and iTunes sales **on a logarithmic scale**. Now to review a little high school math (yes, high school was a long time ago here as well), when you plot things on a logarithmic scale, exponential growth shows up as a straight line. A gradually tailing off curve generally still implies substantial growth -- iTunes sold a billion songs just in the past 12 months. So the first takeaway from the above curves should be that both the iTunes and iPod sales are growing dramatically.

Secondly, let's look at the ratio between songs and iPods. In December 2003, iTunes had sold about 25 million songs for 2 million iPods, or a ratio of about 12.5 to 1. Today, that number is more like 23. So songs per iPod have actually grown over three years, and that's why the curves are getting farther apart. Further, some of those iPods sold now are not operational (although my December 2001 first generation iPod is doing fine, not everyone is so careful or lucky), and some iPods go to repeat buyers. So the actual ratio of songs to iPods is actually higher than this graph would indicate.

The bottom line: anyone who claims iPod sales are collapsing can't do basic math. The rate of song purchases is going to change month-to-month, and Forrester's data shows that. But the iTunes Store is the fourth largest online retailer of any type and is selling almost three million songs a day. And of course, none of that counts revenues from TV shows or movies either, each of which amount to millions of dollars of revenue per year. If that's a collapse, I don't know what these authors consider success.

Full disclosure: I do own a small number of Apple shares.

Update: I have seen a few postings referencing this article saying that Josh and I are looking at the same data. We are not; he has access to some proprietary Forrester data that I don't have access to. And the numbers he has cited are averages from a sample of about 2,000 US credit card records (which, by the way, ignores all the European and Asian iTunes stores), which may or may not be representative of the entire population of iTunes music buyers. My interpretation of his data is that the second derivative of revenue may have changed in the last few months, but as the data clearly shows, that is very very far from iTunes sales collapsing. It simply means that its growth has slowed somewhat. Nonetheless, given that Apple took nearly three years to hit a billion songs sold, and the fact that it sold a billion just in the last twelve months, iTunes music sales remain quite healthy and producing revenues of more than one billion US dollars a year.

Update 2: That little discontinuity in the graph above at December 2005 is because

Apple sold 14 million iPods last Christmas, up substantially from its average quarter of only 4-8. This Christmas, I'm predicting Apple will sell 20 million (and Apple always beats my projections). **Periods of disproportionate iPod sales drive down the ratio of songs to iPods.** Further, Josh's analysis does note that iPod gifts and gift card usage are not included in his count. Guess when those items are used most often. That's right, around now, not during the first nine months of the year.

The bottom line: iTunes is doing just fine.