



Apple Inc.

The world's most valuable company has perfected the luxury tech business model

MarketLine Case Study

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1. Overview

1.1. Catalyst

In April 2020, Apple became the first company in the world to reach a \$2tn market cap. Apple's 'luxury tech' business model has been as important to its success as its innovation with groundbreaking products like the iPhone and iPad, and has competitors playing catch-up with their own premium devices that put factors like style, user experience and exclusivity on a par with technical performance. As the technical prowess of Apple's products becomes increasingly less important than the power of its brand, with competitors offering the same technology at lower cost, the future of the model is uncertain. However, Apple is sure to continue relying on its service ecosystem – the key to its marketing strategy – for future profitability.

1.2. Summary

The key to understanding the luxury tech business model in its current form and the foundations of Apple's supremacy in the field lies in the company's game-changing products and services. Looking at how important each of these offerings has been to the company's present success shows how important new innovations will be for its future.

Personal devices have been the biggest drivers of Apple's success with personal-use consumers. In effectively inventing new product categories where it can set consumers' expectations from the beginning, the company has been able to make it extremely difficult for others to seriously compete with its personal devices in desirability terms.

The iPhone was the most powerful of these, presenting a way of integrating a tech product into a marketable lifestyle, and offered a design that was unique among its competitors. The iPhone's unrivalled functionality created exclusivity that made a real difference to customers whose lifestyles increasingly revolved around the internet, digital media and social networks.

The reason for this is the iPhone's ability to push consumers' price-points up whilst retaining and even gaining a huge market share, by marketing its way into aspirational lifestyles. The marketing tour-de-force which began in 2007 has been a defining feature of the successful luxury tech model which competitors are only just trying to emulate with their own products.

However, Apple's competitors in the computer and smartphone market have begun to graduate from mimicking its business model with cheaper devices to seriously rivalling it. Apple's response to these rival offerings has kept it on top, but in the case of Microsoft the threat is ambiguous, and its full impact on the company's market share remains to be seen.

Whilst Apple remains out in front, the kinds of technological innovation which the company got ahead of over the last decade are likely to place less emphasis on devices and more on services in the future. Apple is in a uniquely strong position to lead the emerging IoT theme thanks to its closed ecosystem of products. However, the very utility of closed ecosystems to consumers will make its competitors more determined than ever to copy the luxury tech business model.

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2. In Luxury Tech Apple has pioneered a powerful business model

In April 2020, Apple became the first company in the world to reach a \$2tn market cap. Since its inception the company has been selling its high-end, 'luxury' personal computers, and since the iPod was released in 2001 it has pushed the price-bracket for numerous other electronic devices as well. Apple's 'luxury tech' (LTech) business model has been as important to its success as its innovation with groundbreaking products like the iPhone and iPad, and has competitors playing catch-up with their own premium devices that put factors like style, user experience and exclusivity on a par with technical performance. Microsoft and Google in particular have begun to run marketing campaigns in a similar vain to Apple's, placing their LTech products at the center of aspirational lifestyles.

As the technical prowess of Apple's products becomes increasingly less important than the power of its brand, with competitors offering the same technology at lower cost, the future of the LTech model is uncertain. However, Apple is sure to continue relying on its service ecosystem – the key to its marketing strategy – for future profitability.

2.1. Apple has diversified its LTech model into numerous product and service categories

Apple's history can be approached from many angles, and is often seen in terms of the departure, return and legacy of former CEO Steve Jobs. However, the key to understanding the LTech business model in its current form and the foundations of Apple's supremacy in the field lies in its game-changing products and services. Looking at how important each of these offerings has been to the company's present success shows how important new innovations will be for its future.

2.1.1. Rivals are only just catching up to Apple's landmark iMacs and Macbooks

Apple's history can be approached from many angles, and is often seen in terms of the departure, return and legacy of former CEO Steve Jobs. However, the key to understanding the LTech business model in its current form and the foundations of Apple's supremacy in the field lies in its game-changing products and services. Looking at how important each of these offerings has been to the company's present success shows how important new innovations will be for its future.

The company's foray into tech offerings that can be considered 'luxury', putting aesthetics and desirability on a par with or above technical performance, arguably began with the introduction of the iMac computer in 1998. The iMac had a brightly-colored, compact design which at the time was likened to art, and elevated the model of most tech companies above functionality. The key to Apple's new model was its target audience, which outside of the education and publishing sectors notably included private consumers, seeking computers for home use.

Since the original iMac, Apple computers have been through numerous iterations, of which its laptops have become most prominent. These iterations have consistently heightened the benchmark for aesthetic appeal with increasingly compact designs and more expensive materials. Whilst maintaining market-leading performance benchmarks for its professional users – located mainly in creative industries – the company has centered many of its product updates on improving ergonomics and the user experience. These improvements may not be strictly functional, but they work to keep Apple's strong base of personal consumers intrigued and satisfied.

Whilst rivals in the personal computing sphere like Lenovo, HP and Dell have largely continued to pursue a lower-margin model, competing to maximize sales rather than driving up their price-points, Microsoft has begun directly competing with Apple's premium consumer laptops. Nonetheless, the fact that it took until 2015 for Microsoft to release the Surface tablet, making way for a full range of tablets and laptops with an emphasis on aesthetics and build-quality, is testament to the difficulty Apple's rivals have had in matching its LTech model.

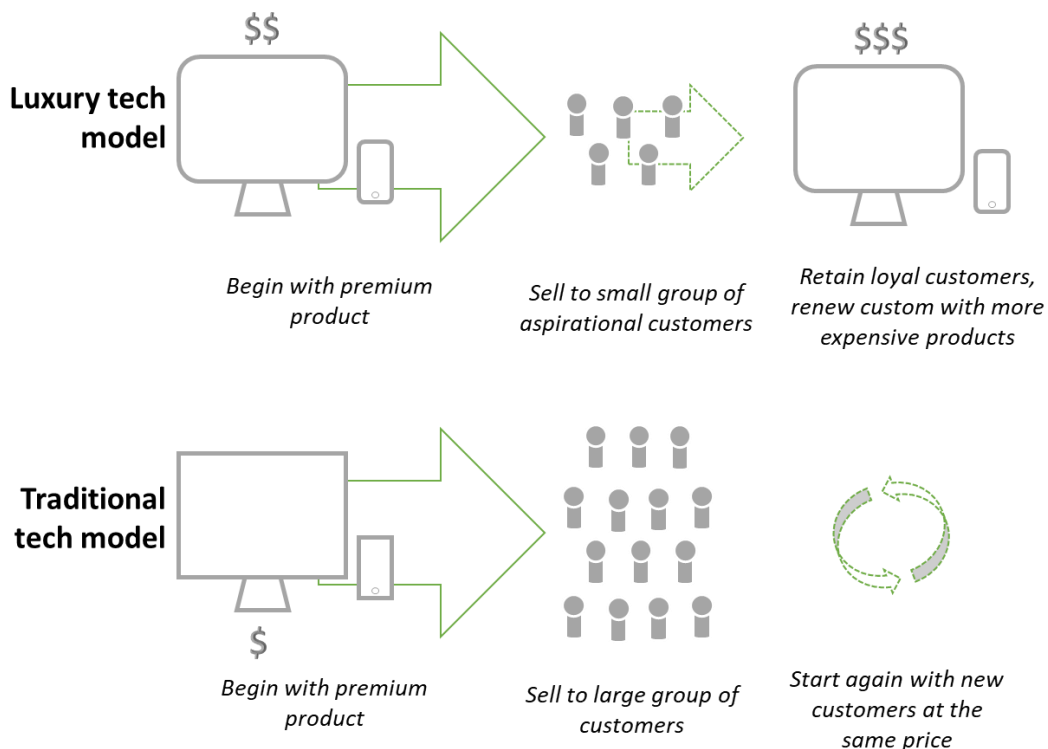
2.1.2. The iPod was Apple's first inimitable device innovation

Contributing significantly more revenue to Apple's LTech model, personal devices besides laptops have arguably been the biggest drivers of its success with personal-use consumers. In effectively inventing new product categories where it can set consumers' expectations from the beginning, the company has been able to make it extremely difficult for others to seriously compete with its personal devices in desirability terms. However, this strategy may not be replicable indefinitely, as the nature of technical innovation moves away from devices.

In 2001, following the release of the iTunes store for converting hard-copy music to MP3 format, Apple introduced the iPod, which represented its first foray outside of the personal computing market. As well as making Apple into a media company – by 2006 more than a billion songs and videos had been sold through iTunes – the iPod range became the first example of a strategy essential to the LTech model.

Because of its immediate market lead over other MP3 players with unmatched storage and a typically ground breaking design, Apple was able to use the iPod to lock in and retain the consumers for whom the product was becoming a lifestyle essential. Having done so, it began to continually upgrade the model with new designs and user-experience features, from belt-clips to touchscreens. This strategy of continual low-risk upgrades, or 'retain-and-renew' (RaR), is now a hallmark of Apple's business model, and makes it almost impossible for less profitable companies to keep pace.

Figure 1: The LTech business model versus a traditional consumer tech model.



Source: MarketLine

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2.1.3. The iPhone combined Apple's luxury offering with genuinely unmatched functionality

The first iPhone, released in 2007, may have been Apple's defining technical innovation, but it was still every bit a high-end product of the LTech model. Like the iPod, it represented a way of integrating a tech product into a marketable lifestyle, and offered a design that was unique among its competitors. The iPhone's unrivalled functionality created exclusivity that made a real difference to customers whose lifestyles increasingly revolved around the internet, digital media and social networks. Most smartphones had until 2007 been based on the Blackberry, with a half-screen, half-keyboard layout, but the iPhone went for a more colorful, tactile touchscreen that brought with it iOS, the now-bestselling mobile operating system focused explicitly on the ease and enjoyment of the user experience.

Just as importantly, though, the iPhone immediately picked up the RaR strategy deployed with the iPod. Relying on the loyalty of existing customers, Apple has been engineering more expensive iterations of the iPhone every year since its first release, increasing the level of exclusivity with each price-hike. This essential element of the LTech model has continued to differentiate Apple from sales-focused competitors, whilst actually beating them at the sales game as well for most of the iPhone's history.

Along with the unprecedentedly high frequency of iPhone iterations came another exclusivity factor that reinforced Apple's ability to renew the consumers it retains – updates to software as well as hardware. As cyclical improvements on the basic hardware of the iPhone become more difficult to sustain, and because the software is an essential differentiator for the device, new packaging for the iPhone offering has increasingly been realized with the operating system (OS). Numerous updates to the iPhone's OS have made older models obsolete more quickly, in turn heightening the vitality and desirability of the latest models and renewing loyal customers at a higher rate than ever.

2.1.4. The iPad brought the luxury offering to a far wider consumer base

Having created a luxury computer with the later iterations of the MacBook, and created an endlessly marketable tech-driven lifestyle offering with the iPhone, Apple introduced the iPad in 2010. With its first tablet device Apple created another category that competitors have since been striving to fill with their own offerings, and another product through which to deploy its RaR strategy.

In many ways, though, the iPad was the purest example of the LTech model, offering very little new functionality against the iPhone and MacBook and instead repackaging these into a design that reoriented the user experience. The value of the iPad has been to bring Apple's unique aesthetic and exclusivity to more consumers, targeting leisure-time as its chief use case. It has also given the company another way to bring those consumers into its ecosystem of digital media services.

2.1.5. Apple's ecosystem of services is also part of its RaR success

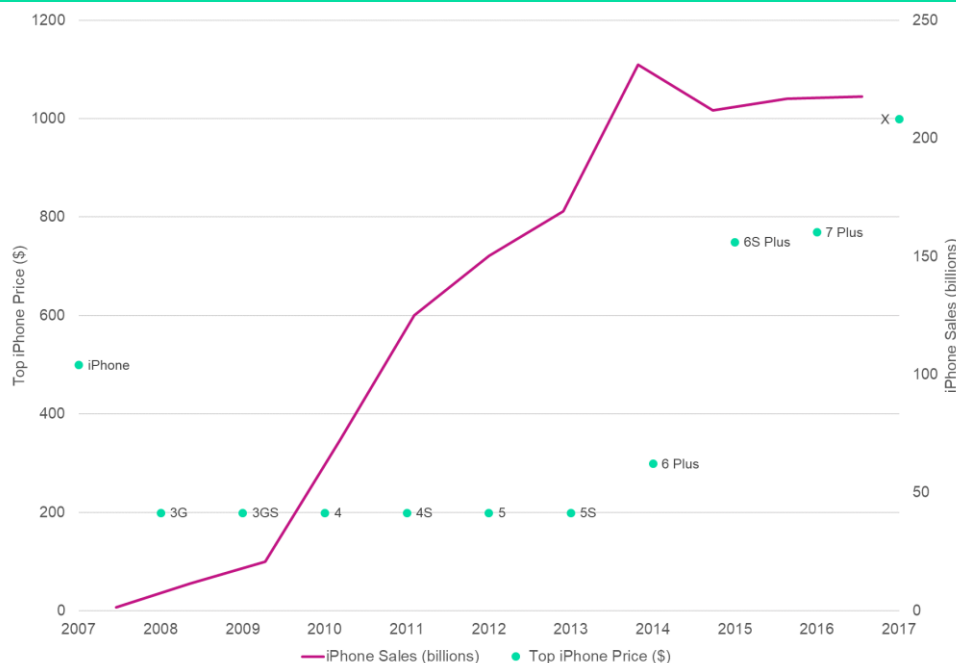
Since Apple released its first computer, the deliberate lack of interoperability between its products and those of other brands has been a defining feature of its premium business model, and has shaped the exclusivity of its brand. The first Mac OS could only be run on Apple machines, setting a precedent for all Apple services, and another example which competitors would eventually follow.

Shortly after the release of the iPad, in 2011 Apple unveiled its iCloud suite, a cloud storage service which updates applications, documents, photographs and other content between a user's Apple devices. Whilst not being an obvious characteristic of the original LTech model, iCloud has in fact helped to strengthen that model by perpetuating the exclusivity of Apple's user experience. The more information which users store to iCloud, which can only be accessed through Apple devices or in a limited way on a browser, the more reliant they are on MacBooks, iPhones and iPads. This in turn serves the RaR strategy which underpins the LTech model, enabling Apple to leverage the dependence of its loyal customer base for the introduction of new luxury products with bigger price tags and guaranteed margins.

3. The iPhone has made the LTech model more lucrative than ever

Apple was already one of the most profitable companies in the world before the release of the first iPhone, but that device has been indispensable in its ascendance to a \$2tn market cap in 2020. The reason for this is the iPhone's ability to push consumers' price-points up whilst retaining and even gaining a huge market share, by marketing its way into aspirational lifestyles. The marketing tour-de-force which began in 2007 has been a defining feature of the successful LTech model which competitors are only just trying to emulate with their own products.

Figure 2: iPhone sales (billions) and the peak iPhone price in each year (2007–2017).



Source: Apple, MarketLine Analysis

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3.1. The iPhone outprices rival smartphones and moves consumer price-points to meet it

As shown in Figure 2, the sales of the iPhone showed particularly strong growth from the release of the iPhone 4 model, and began to slow slightly over the next few years. Apple stopped segmenting its published sales figures by product-type in 2018, but the figures up to that point show that when iPhone sales dropped in 2014 and 2017, a more expensive model brought sales back up in each case. The iPhone models shown in the chart are the most expensive of the models released in each respective year. From 2013 onwards Apple released two new models each time, one of which was slightly higher-spec and came with a higher price-tag. Since 2016, there have been three new models released in each iteration, to keep Apple products attainable for a broader range of consumers. However, the more expensive variations have shown that Apple can trade on the exclusivity of a higher price-point to maximize the potential of its RaR strategy.

It appears that Apple has pushed the profitability of the LTech model to new heights mainly on the strength of the iPhone. Suffice it to say that the iPhone has been the company's best-selling product for most of the 2010s, with a 62% share of revenues in 2018, and that more expensive models have generally coincided with profit growth. In 2015, for example, whilst sales went down as the newest iPhone pushed the top-band price further than ever, the company's net income increased by 35%, reaching an all-time high. This may have had something to do with the new Apple Watch, but the wearables segment made up less than 10% of sales in that year, and the iPhone is likely to have been the primary driver of income.

Reliance on the iPhone could be seen as a weakness for Apple, especially smartphone penetration in its key markets matures. Emerging markets are more difficult for Apple to get into without undermining its LT model, as those markets are usually marked by lower consumer spending power, despite rapid growth in uptake of smartphones. For this reason the company will come to rely increasingly on the services segment for sustained profitability (see Section 4). However, the success of the iPhone over the last decade has demonstrated the power of the LT model for driving income with exclusivity and a determined RaR strategy.

3.2. As competitors threaten to catch up with cheaper LTech products, Apple still remains dominant

Apple's competitors in the computer and smartphone market have arguably begun to graduate from mimicking its LTech model with cheaper devices to seriously rivaling its products. Samsung, its longest-standing competitor in the latter market, has changed tack cautiously towards premium products whilst maintaining an extensive range of cheaper models. However, Microsoft has entered the premium computing sphere with some success, having not been a major player in any hardware segments prior to 2015. Apple's response to rival luxury tech offerings in both these segments has kept it on top, but in the case of Microsoft the threat is ambiguous, and its full impact on the company's market share remains to be seen.

3.2.1. Samsung luxury tech lacks the ecosystem which underpins Apple's LTech model

Whilst there are various emerging competitors to the iPhone in 2020, including a range of devices from Huawei that are becoming increasingly popular outside of Asia-Pacific, these usually remain committed to undercutting Apple on price. For Samsung, a host of more affordable products was joined by the Galaxy Note smartphone in 2011, a year after the iPad massively had expanded the screen size that consumers could expect from a mobile device.

The Galaxy Note has not only kept pace with the iPhone's pricing – the highest-spec model in October 2020 retailing off-contract for \$1430 – but have also deployed user experience features as their key differentiators. The Note originally came with a bigger screen than any iPhone, boldly blurring the line between Apple's smartphone and tablet offerings. Users can interact with the screen with a stylus that comes as standard, something which has always been an extra even on the iPad. Samsung also innovated with a borderless, 'wrap-around' screen, which has now been all-but imitated by Apple.

In 2020, following an earlier unsuccessful launch, Samsung followed up with another innovation that has received critical praise, if not quite converting many consumers. The Galaxy Fold makes another bold stride away from the iPhone's design to tempt customers with individuality, introducing a pioneering foldable screen.

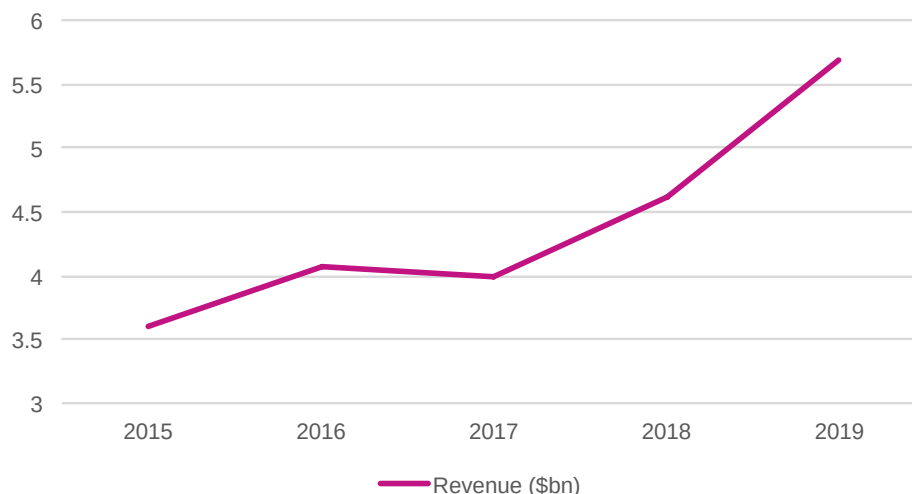
Samsung now has two products which cater, in theory, to the luxury tech consumer and match or almost match Apple's high-end pricing, but the profitability of Samsung's smartphones remains far behind. The reason for this is the lack of a closed ecosystem of services accessible only on Samsung devices. Instead Samsung has largely relied on Google's Android operating system (OS), with the small exception of its own Tizen OS, available on a limited range of devices. The competitive disadvantage is that almost all other smartphone manufacturers besides Apple also run the Android OS, preventing Samsung from retaining loyal customers who might happily renew their custom when it releases more expensive but less innovative models. That disadvantage keeps Samsung from fully deploying the LTech business model.

3.2.2. Microsoft's Surface products are quickly making ground despite their open ecosystem

Like Samsung's smartphones, Microsoft's bids to match Apple's LTech model in the computing market have featured closer pricing structures and novel features to enhance the user experience. Crucially, they have also placed significant emphasis on lifestyle and enjoyment in their marketing, in a way that is directly comparable with Apple's marketing.

The Surface was launched in 2015, aiming to play Apple at its own game by 'creating a new category'. This new category was a hybrid tablet that could replace a laptop for many users, repackaging features for leisure-time consumers as Apple had done with the iPad whilst also meeting more practical requirements. From the Surface there has since proliferated a diverse range of luxury tech products which notionally compete with Apple's tablet, laptop and desktop offerings. Special user experience features which differentiate the products from Apple's include fabric-lined keyboards and a new biometric function – authentication using facial recognition – that has since been taken up by newer iterations the iPhone.

Figure 3: Surface revenues 2015–2019 (\$bn).



Source: Microsoft, MarketLine Analysis

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The growth in revenue which the Surface range delivers for Microsoft can be largely attributable to its early-stage strategy, which aims to balance the LTech model with winning new users. Iterations of Surface products, particularly the Surface Laptop 3 and Surface Book in 2020, have indicated that Microsoft is yet to implement a RaR strategy like Apple, with few software or hardware updates to render the older models obsolete. It will certainly take a while for the Surface range to amass a base of loyal customers comparable to Apple's, but if and when it does there will be little stopping it from fully realizing the LTech model with a strategy that is closer to RaR. The only thing, in fact, will be a closed ecosystem.

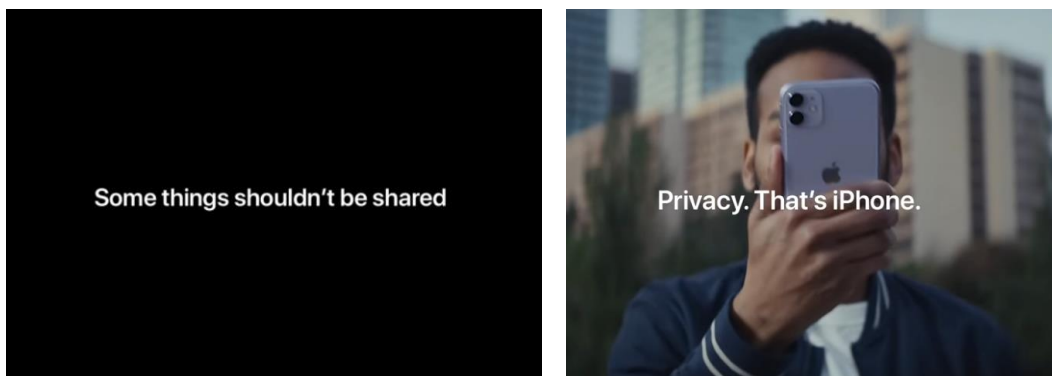
As with Samsung's reliance on Android, Microsoft's use of its own trademark Windows OS, which is installed on most non-Apple computers, could prevent it from leveraging any customer loyalty to that OS. Windows is and will almost certainly remain a more lucrative product for Microsoft (it represented 16.2% of total revenues in 2019, versus 4.5% for Surface products). The company cannot afford to pull back on the inclusivity of its OS just to heighten the exclusivity of its new, less lucrative hardware. It remains to be seen whether it will find an alternative solution, but for now Microsoft is still just shy of realizing the LTech model's potential in the way that Apple has.

3.3. Apple's vulnerability to LTech rivals is reflected in its defensive restructuring of product ranges

Developments in Apple's product range in 2020 have signaled a slightly defensive rearrangement of its product and pricing structures, which will likely be apt to deal with the rival moves on its LTech model outlined above. In April 2020, as COVID-19 and its impending financial implications loomed for many consumers, the company reintroduced an 'affordable' iPhone SE model, the first since September 2018, when the original SE was discontinued. This move was indicative of a marked reduction in the minimum price customers are required to pay for a new iPhone; the peak-price iPhone X, also discontinued in 2018, has not since been matched by a base model. Any iPhone models since the iPhone X which have passed the deal-breaking \$1k mark have instead been marketed as more exclusive versions of concurrent base models.

Beyond the iPhone, competition from Microsoft's Surface range appears also to have turned Apple's hyper-premium implementation of the LTech model down a notch, whilst maintaining some exclusivity over Microsoft with its pricing. The iPad Pro base model released in March 2020 had a higher starting price than its Surface tablet equivalent, despite having a smaller screen. Apple has again reliably leveraged its loyal customer base to charge more a product that was targeted primarily at pre-existing Apple users who could act as early adopters. Additionally, with the iPad range now fleshed out into three distinct models, Apple can continue to draw a broader range of consumers into its ecosystem with more mid-price products, and in doing so maintain the premium appeal of its MacBook laptops, which in 2020 still start at \$999.

Figure 4: Apple's privacy-focused marketing campaign.



Source: Apple

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3.4. Apple's continued dominance is a combination of range-restructuring and the power and resilience of its brand

As well as restructuring its products in order to maintain exclusivity with lower average pricing, Apple has responded to the LTech maneuvering of its rivals with a new emphasis in its marketing messages. These messages will help to convert some users for the first time, but will more importantly bolster the resilience of its loyal pre-existing customers with another reason to pay more for premium Apple products.

The new marketing message in 2020 is simple: Apple values privacy more than its competitors. This plays on consumer fears over Big Tech's trustworthiness and transparency, which have grown ever more intense since Facebook's Cambridge Analytica scandal in 2018, and plays to an inherent strength of the closed ecosystem which underpins Apple's LTech model.

As opposed to Microsoft with its widely-used OS, and especially opposed to Google with its ad-based business model, Apple can boast a 'closed loop' of devices and services with low security risks and no monetization of users' personal data. This messaging is of course partly necessary to distance Apple from a media storm that threatens to envelope it along with its competitors, but it is also a cunning promotion of luxury tech. Pay more for aesthetic appeal, exclusivity and an enjoyable user experience, and pay more to be part of a closed loop.

4. The future of the LTech model is in diversification and the IoT

Whilst Apple remains out in front, the kinds of technological innovation which the company got ahead of over the last decade are likely to place less emphasis on devices and more on services. Apple is in a uniquely strong position to lead the emerging IoT theme thanks to its closed ecosystem of products. However, the very utility of closed ecosystems to consumers will make its competitors more determined than ever to copy the LTech business model.

4.1. IoT will be the next testing ground for the LTech model

The IoT is already a predominant theme in technological innovation, and the advent of 5G connectivity is expected to massively speed up its development. An increasing number of devices and services are expected to be accessible and controllable through personal devices, particularly smartphones and to a lesser extent wearables. This is certainly good news for Apple's RaR strategy, as the need for interoperability and a consumer preference for simplicity will likely lead its present and potential customers to invest wholesale in one company's products and OS or another's. This of course represents a challenge for the LT model as well, as the 'luxury' of connectivity and slick devices becomes more commoditized and its competitor's eye up consumers with lower price-points.

4.2. Wearables and healthtech are the future of Apple's IoT

Apple's most recent entry into a new device category occurred with the Apple Watch in 2015, signaling a clear move in the direction of the wearables market. This is one market – unlike high-end personal computers, large-capacity MP3 players, smartphones and tablets – where Apple was not a leading innovator, but rather an imitator of other companies' partially-successful products. The Apple Watch came at a time of peak market penetration growth for the Apple ecosystem, giving retained customers a way to invest more in the brand and inviting new ones in with a novel offering. More importantly, though, the Apple Watch has given the company an early lead in another emerging technology theme, healthtech, which will play to its strengths as a tech company marketing itself holistically as part of the consumer's lifestyle.

Healthtech is an important feature of the IoT landscape, with huge potential for selling connected products than can monitor and manage health indicators. Even greater investment in this theme from companies like Amazon and Google has hinted at significant opportunities for private healthcare companies to market medical devices and treatments through these networks of products. Wearables like the Apple Watch are therefore going to be a major area of growth for Apple as it seeks to push its LTech model into new markets and find new ways of renewing interest from its retained customers.

5. Appendix

5.1. Abbreviations and acronyms

LTech – Luxury Tech

RaR – Retain-and-renew

OS – Operating system

5.2. Sources

Company financial statements

MarketLine Companies Database

5.3. Further reading

Consumer Technology Solutions: Smart products and services present some key opportunities

Smartphone Companies: COVID-19 creating difficulties but the fight is not over yet

Amazon & Big Tech: Subcommittee hearings only a warm up before EU's upcoming report

6. Ask the analyst

We hope that the data and analysis in this case study will help you make informed and imaginative business decisions. If you have any questions or further requirements, MarketLine's research team may be able to help you. The MarketLine Research team can be contacted at ReachUs@MarketLine.com.

7. About MarketLine

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