

AUDIO ADVICE: FROM RETAIL TO E-TAIL

Michael A. Stanko wrote this case solely to provide material for class discussion. The author does not intend to illustrate either effective or ineffective handling of a managerial situation. The author may have disguised certain names and other identifying information to protect confidentiality.

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On a Friday afternoon in January 2016, Jonathan Stephens took a break from the tedious task of entering product information into his Amazon.com seller account. His tranquility was short lived; his thoughts were drawn to upcoming deadlines and the branding decision that he and his colleagues at Audio Advice faced as they planned their e-commerce site. Stephens knew he needed to devote some time to thinking about branding, but it was getting late and he had to stop at the FedEx store to send a carton of unexpectedly fast-selling headphones to Amazon before heading home for the weekend.

While managing an online retailer was a dream come true for Stephens, it was hard to feel self-indulgent as he hauled the cardboard box out of his car's trunk. Standing in line, he had a rare few moments to ponder his time at Audio Advice and think about the next steps he and his colleagues needed to take.

Audio Advice was a brick-and-mortar retailer that Stephens was trying to treat as a start-up; his challenge was to take this long established retailer online as soon as possible. During his short time at Audio Advice, they had already experienced some success online as an Amazon Marketplace seller, but Stephens and the rest of Audio Advice's management had a bigger vision for online retailing. Their ambitious e-commerce plans called for site development to begin in February, with a goal of launching on June 1, 2016, but many important questions still remained unanswered.

BRIEF HISTORY OF AUDIO ADVICE

Leon Shaw put his passions for technology, music, and delighting customers to use in founding Audio Advice in Raleigh, North Carolina in 1978 (see Exhibit 1). The original showroom focused on high-end audio equipment, representing several upscale brands. Some brands, such as Denon, Mirage, and Conrad-Johnson, were still relevant almost 40 years later. In its early years, Audio Advice sold plenty of record players while they were still a mainstream technology. In the past decade, they also played a role in the "vinyl revival" as a growing number of enthusiasts discovered (or rediscovered) the joys of vinyl records.

While vinyl had come, gone, and come again, Audio Advice had also introduced customers to emerging audio technologies such as compact discs (first commercialized in 1982), MP3 players (first

commercialized in 1997), and home surround sound systems. At Audio Advice's showroom, customers could experience a US\$100,000¹ home theatre or select from several loudspeakers priced at over \$10,000. Of course, there were also more modestly priced offerings available, such as headphones starting at \$100.

Through the years, Shaw had consistently been active in industry associations, such as the Home Technology Specialists of America. This helped to ensure that Audio Advice stayed informed of technological developments and competitive activities.

In 2007, Scott Newnam invested in Audio Advice and took the role of president and chief executive officer. (Shaw remained very active within Audio Advice as chair of the board of directors.) Prior to this, Newnam had founded a media technology company while an MBA student at Harvard Business School. When that company was acquired, Newnam returned to his home state of North Carolina and invested in Audio Advice. He was looking for a more balanced life in this new role, but had ambitions for Audio Advice, believing it could reach a larger audience.

Soon after Newnam became involved in Audio Advice, they opened a second showroom in Charlotte. This was the first step in growing Audio Advice's reach. The second store continued Audio Advice's history of steady revenue growth. Both stores proved to be reasonably recession-proof, even through the great recession of the late 2000s. By 2015, Audio Advice's annual in-store revenues surpassed \$10 million. Despite this growth, it gnawed at Newnam that Audio Advice's reach was still limited to the two largest cities in North Carolina, the ninth largest U.S. state by population. Industry wide, sales had shown steady growth over the previous four years after recovering from a significant drop during the recession (see Exhibit 2).

In terms of culture, one constant at Audio Advice was a strong emphasis on delighting customers. Newnam put it this way:

From the day I got here, everyone at Audio Advice had a passion for audio and electronics, but I think the key thing to understand in thinking about why we do things the way we do is that everybody in the company loves the smile on a customer's face. When we interview prospective employees, we are looking to see them derive enjoyment from the happiness of customers. *That* is what's required to make sure [employees will] go above and beyond.

This culture had led to numerous awards from local and national publications, including being named *This Week in Consumer Electronics (TWICE)* magazine's Best Audio Video Specialty Retailer in the United States.

Over the previous five years, Newnam had gotten to know Stephens, a graduate of North Carolina State University's MBA program with experience managing online sales of technology products. In October 2015—as conversations within Audio Advice about selling online became serious—Newnam hired Stephens as general manager for online sales.

Audio Advice's management felt sure that there was room for profitable growth through online selling, but they were also certain that there would be concerns from all corners of the organization. Audio Advice's organization was dominated by sales staff who were pragmatically oriented toward the customers walking through the doors of their retail locations. While the sales staff were not closely involved in the early discussions regarding online strategy, Shaw and Newnam were aware that these employees would be sensitive about funnelling marketing efforts to online, rather than in-store sales, especially because the sales

¹ All currency amounts are shown in U.S. dollars unless otherwise specified.

staff earned commissions on their in-store sales. Some believed that online selling could benefit the sales staff with online orders leading to phone calls and store visits to discuss upgrades, but it was clear these issues needed to be thought through. For instance, what would happen when technical support was needed for an online sale? The sales staff typically supported their own customers as part of the sales process, but they clearly wouldn't love the idea of supporting customers who had bypassed sales staff by buying online.

Audio Advice had long had a website and had used email marketing to promote its products and in-store events; however, audioadvice.com had been exclusively focused on directing potential customers to the two store locations. There was some sentiment that a tool that had been previously used to the benefit of sales staff might end up competing with these same people.

THE CHANGING AUDIO RETAIL LANDSCAPE

The higher performance (and often higher priced) portion of the audio equipment business was often referred to as the "audiophile" segment. Components such as turntables, home theatre receivers, headphones, speakers, and subwoofers were typically sold individually to consumers who thought of themselves as audio enthusiasts, and enjoyed the process of experiencing and learning about new products and technology. Audio Advice targeted these audiophiles, engaging their desire for high performance products and their interest in learning about emerging technologies.

Many of the brands Audio Advice sold in their stores had traditionally prohibited online selling. Indeed, many audiophile components were only sold in specialty audio stores (such as Audio Advice), in which customers could try the products for themselves. This was part of a long-held, but changing, industry practice known as channel protection: to build strong partnerships with traditional audio retailers, manufacturers severely restricted (or eliminated) online selling and sales through other types of retailers, such as big-box electronics stores. The retailers rewarded the manufacturers for this exclusivity by stocking and promoting brands that couldn't be found in other channels. However, this practice was shifting as consumers showed increasing interest in buying more products online. A few years ago, customers would never have thought to shop for diamonds or mortgages online, but both of these were now big businesses.

Audiophile brands generally offered a great deal of pricing protection to their retailers through minimum advertised price (MAP) agreements, meaning that prices in the audiophile segment were typically consistent across retailers with very little discounting. In the recession of the late 2000s, some traditional audiophile brands, facing slumping sales, widened their distribution to big-box outlets and/or online retailers. They sometimes sold at prices below those offered by specialty audio stores, leaving some uncertainty in audio retailers' relationships with manufacturers.

As in other areas of retail, audiophile customers began taking advantage of high-touch channels to see and hear products, then purchased from lower priced sources online. This "showrooming" trend was a major concern. While some traditional audiophile brands (e.g., Sennheiser, KEF, Audio-Technica, Klipsch, and Denon) were selling more product through online retailers, other brands (e.g., Linn, Mark Levinson, and Classé) remained devoted to distributing through specialty audio retailers. Still other audiophile brands had taken halfway approaches, distributing some products through online channels and big-box stores while attempting to keep distribution of their highest performance products exclusive to specialty retailers. Some large retailers stretched to take advantage of this approach; for example, Best Buy created Magnolia sections in some stores to carry "premium" audio components, some of which were drawn from traditional audiophile brands. As of 2016, approximately eight per cent of audio equipment sales took place online, though this percentage was expected to nearly double in the next five years (see Exhibit 3).