Case Analysis 6: Sonance at the Turning Point

MKT 487

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Situation Analysis:

Sonance is a company created by two friends in 1982, in San Juan Capristo, California. Their names are Scott Struthers and Geoff Spencer. They returned back to help with some important decision concerning their company. They hired a new CEO name Shawn Sugarman and a new Chief Sales Officer named Ari Supran. Sonance is known for their built in-wall high quality speakers. They were the first to move them off the wall and floor and into the wall. When the company was first created a pair of speakers cost about $75 to manufacture. They sold them to dealers for $195. The dealers then turned and sold them for $550. After a copyright legal issue with SpeakerCraft in 1999, that Sonance did not win because of bad legal advice, and competition in the industry. Sonance found a way to manufacture for just $50 per pair. Then sold to dealers for $140, and they sold it for $400. In 2004 Sonance introduced the iPort, which was a device that could connect an iPod directly. It had a listed price of $598 and was sold exclusively through custom installation dealers. The dealers paid Sonance $300 per unit. Sugerman and Supran met with the iPort design team. They found a way to sell it commercially and for only $125. Sonance estimated that about 2,500 houses were falling into the luxury designer home category and they made up about 25% of that market.

Problem/Decision Statement:

- The audio segment of the consumer electronics industry totaled about $5.6 billion in factory sales and has been on the verge of decline for years. Industry observers believe that is due to:
    - Lack of product innovation
    - Difficulty conveying product features to consumers in most retail settings
    - Greater interest in video-related categories

- Sonance was hit with a decline in sales from $53 million in 2003 to just above $47 million in 2004, due to the following:
    - Sonance was dropped by half of its high-end installers
    - Lowe's decided to exit from the in-wall speaker category

- Sonance has problems with its current target market which is both the mass market consumer and new production home developers.
    - Mass Market Consumer
        - Distributed to customers through its largest retail accounts Best Buy and Lowe's, which Lowe's exited
        - Buyers consider price and sound quality very significant in the following product categories:

            - Home theater in a box (HTIB)
            - A/V reciever (AVR)
            - A/V receiver plus speakers
        - The vast majority of the home audio sales totaled $9 billion in 2004; however, Sonance's prices are well above average
        - Retail customers tend to install the products themselves, affecting potential for profit from installation services
    - New production home developers
        - Production housing segment was growing the fastest in the Sonance portfolio
        - Homeowners wanted advanced sound systems
        - Both sales to custom installers or production builders took some time to translate contracts into dollars
- Competition is intense in consumer electronics
    - Some of Sonance's competitors are larger with more diversified revenue bases, significant research, and development budgets
    - Nortex's acquisitions of three competitors intensified price competition
    - Competition (SpeakerCraft) could offer higher margins and cheaper installations than Sonance

Sonance is facing many issues that are jeopardizing the company's survival. Because the consumer electronics industry is changing continuously, the company must consider many alternatives to solve these problems. Sonance must consider either rebuilding its relationship with high-end dealers, or expanding its product line with a cautious price range to compete effectively with competitors. This decision will ensure Sonance's sustainability, profitability, and potential for future growth.

Identification of Alternatives:

<u>Pursue iPort Strategy:</u>
Sonance is trying to expand their market share in the expanding retail consumer marketplace. One way of achieving this is by allocating its resources toward the development of the new iPort system. With iPods and MP3s becoming extremely popular, introducing a product that will allow the consumer to easily connect their MP3 player to their home sound system could increase sales dramatically. Sonance could partner with Target and align with their increased consumer electronics with an emphasis on style strategy. The iPort R&D team guarantees that if fully funded, the iPort could be ready to go into production by September 2006, in time for the CEDIA EXPO.

Pursue Architectural Series Strategy:

Sonance has recently begun to lose its foothold in the custom housing market. One way of returning to their core customers is by introducing a new Architectural Series of speaker systems. These speakers are the first truly flush-mount trimless speakers that have completely eliminated sightlines. This could re-introduce them to the very high-end consumer market that is willing to spend a massive amount of money to have the highest quality speakers. The extremely high gross profit margins offered to the dealers (75%) would entice custom home entertainment dealers across the country to carry the Sonance brand.

Criteria for Evaluation of Options:

What should we consider before pursuing Option 1: Pursue iPort Strategy?

- Which segment of our target markets would be best served by this strategy: mass market consumers or new production home developers?
    - Mass market
    - Home developers may lose some money

- Since it is likely that one market will be served more efficiently, does this result in the company neglecting the other market?
    - No, expanding on it

- If fully funded, the iPort can be launched into production in time for the CEDIA EXPO. We must consider a) can this be fully funded, and b) if it cannot be fully funded and production cannot start in time for the CEDIA EXPO, how impactful is that? When would we launch the product?
    - The iPort R&D group promised that if the venture was fully funded, it would be ready to launch by September 2006. This would be just in time for the CEDIA EXPO.

- As iPods continue to develop, does the product have to change along with those developments? If so, what effect does this have on production and marketing strategy?
    - I believe the iPort will have to continue to innovate with the market as Apple continues to innovate. If apple introduces new iPod models which have different size ports, Sonance can create adapters to make the existing products work properly. In the future, Sonance can look to expand into the bluetooth music department in order to connect music wirelessly.

What should we consider before pursuing Option 2: Pursue Architectural Series Strategy?

- Which segment of our target markets would be best served by this strategy: mass market consumers or new production home developers?
    - Home developers

- Since it is likely that one market will be served more efficiently, does this result in the company neglecting the other market?
    - No, Sonance will continue in its existing market.

- Is it wise to pursue a high-end product after Sonance has been dropped by over half of its high-end installers, and the company is also seen by consumers as being as expensive brand?
    - It is wise to create an innovative architectural strategy. This will attract people who are particular about their interior.

- Is the market for this type of high-end product large enough to sustain the cost involved with pursuing this strategy? Are there enough customers in the target market who would be willing to purchase this product, and will those customers continue to buy for a long period of time?

Option Analysis:

<u>Option 1: Pursue iPort Strategy</u>

- Both segments of the target market can be served using this strategy by marketing the lower end products to the mass market, and the higher end to new production home developers.
- We should not neglect a certain market, but rather see how we can more efficiently serve that market.
- Make a huge push to get the iPort fully funded in time for the CEDIA EXPO, if not, it could be detrimental to the company and leave them in the past.
- Continue to innovate the iPort as Apple continues to innovate. Without continued innovation, the iPort could quickly become obsolete.

<u>Option 2: Pursue Architectural Series Strategy</u>

- Home developers would be our target markets for this option.
- Do not ignore the mass market, just focus more resources to the home developers.

- An architectural series approach will attract more of the higher end customers because they are particular about the interior of their homes.
- There may not be a big enough market for this option. Also, once homeowners buy, they may not buy again for years, or maybe ever again depending on if they move or not.

Recommendations:

We recommend Sonance sells the iPort, an in-wall docking station for the apple iPod, to the mass market. Sonance could introduce the iPort to the retail market through super stores, particularly Target.

Sonance introduced the iPort in 2004, but only sold through custom installation dealers. We believe Sonance should further the utilization of the iPort, by selling the iPort to the mass market through Target. It was predicted that Target was going to be making a big push into consumer electronics, which creates a great opportunity for Sonance. Partnering with Target will give Sonance the distribution channel they need, by exposing the iPort product to the mass market. Target could have pictures on the wall of the iPort feature and inform customers who buy iPods of the new iPort dock.

Additionally, iPod sells were advancing at an explosive rate. In 2004, Apple iPod accounted for half of mp3 sells. In 2005, iPod sells increased by 409%. The explosive growth of iPods paired with Target's expansion into the consumer electronic industry creates a very profitable opportunity for Sonance. It is predicted that iPod sales will continue to increase. It is also a very good time to implement the iPort strategy because the iPod R&D group guaranteed that if fully funded, the iPort could be ready to go into production by September 2006, which would be perfect timing for the holiday season and the CEDIA EXPO. Sonance could utilize the CEDIA EXPO to create brand awareness of the new feature.

Appendices

5 P's

Product: Sonance was the first company to take speakers off the walls, floors, and bookshelves and build them directly into the walls and ceilings. The company is known for their high quality speakers.

Price: When Sonance first started it was only $75 to manufacture a pair of speakers. They were sold to dealers for $195. And the dealers sold it for $550 per a pair. After a legal battle of copyrights and competition. We made it only $50 to manufacture and sold it to dealers for $140.

The iPort was listed at $598 and was sold exclusively through custom installation dealers. They paid Sonance $300 per unit. It cost on average to instal was $150. The company was sitting at $53,044,000 of sales in 2003 and dropped $5,744,000 in 2004 because Lowe's exited out of the in-wall speaker category.

Place: Sonance directly manufactures its speakers. Then they will sell the to custom installation dealers, who will go out and directly install them in for the consumer or they will get in touch with the consumer and they will go out themselves and install it.

Promotion: Some of the Consumers heard of Sonance through Lowe's and Best Buy, but a lot of them heard through custom installation dealers, who dealt with specifically in installing their items for you.

People: Sonance sold to dealers as well as three other consumer categories. The three categories are:

- Retail Consumer
    - Home theater in a box
    - A/V Receiver
    - A/V Receiver plus speakers
- The New Home Owner's
    - Sonance did not hold main market share of this category
    - Chip Brown (previous CEO) helped Sonance get into this market
- WAF (Wife's Approval Factor)
    - For men who wanted high quality sound
    - As well as not ruining the wife's interior design of the house.

SWOT Analysis

Strengths:	**Weaknesses:**
- First one's to create in-wall speakers - Introduction of the iPort - Architectural Series Speakers - Hiring new CEO and New Chief Sales Officer - Bring back the CEDIA EXPO	- Changing strategy to diversification - Losing copyright battle against SpeakerCraft - Losing leadership position in the industry

Opportunities:	**Threats:**
- Mend relationships and commit to high-end custom installers - The introduction of the Architectural Series - Focus on retail consumer markets - Full support behind the iPort redesign and marketing	- Losing more money to companies getting out of the in-wall speaker category like Lowe's did - In wall speaker audio segment trend could be ending - Company may be able to keep up continuous innovation to technology - Competitors have a competitive advantage with low prices and faster installation