Is Bigger Still Better?

For as long as we've been publishing, companies in and out of the music industry have relentlessly pushed for sales growth, reasoning that increased volume will yield economies of scale, which translate into fatter profits. It's a thesis that has been validated by history. Enormous unit production enabled Henry Ford to squeeze costs out of the Model T and deliver an affordable vehicle while simultaneously generating fat profit margins. In the same time frame, piano makers Baldwin, Kimball, and Steinway leveraged their scale to produce outsized profits. In recent years, however, new design and manufacturing technologies have significantly reduced the economic benefits of scale, with significant implications for both product selection and retail.

Over the past few decades, digital technology has revolutionized the way products are designed and built. Software-based design solutions have compressed the process, replacing laboriously hand-drawn blueprints with computer files that are more accurate and far easier to share and revise. And, thanks to the collapse in the price of computing power, boutique manufacturers now have ready access to sophisticated design systems that used to be available only to giant enterprises like Boeing or General Motors.

This technology has extended from the design studio to the factory floor. Design systems linked to computer-controlled machinery have slashed the cost of producing stuff. Instead of using hard jigs and fixtures, milled from blocks of aluminum, machines can be programed to produce the same parts. Aside from being less costly, these computer production solutions offer greater flexibility—it's easier to reprogram a machine than re-shape an aluminum production fixture—and often superior quality.

The most obvious benefit of these technologies has been major improvements in product value. Fifty years ago, the Kay Guitar Company caused an industry sensation with its Vibrato Vanguard model. Produced at a Chicago factory, the guitar carried a breakthrough price of $79.99 and was widely hailed by retailers as "the best value in the history of the guitar business." $79.99 sounds like a pretty good deal, and it was in 1965, but adjusted for inflation it translates to $590 in contemporary dollars. Considering its cheesy single pickup, flimsy tremolo unit, and marginal fret job, the Vanguard would be a tough sell today at any price. At $590, it would be a non-starter, given the quality of current products in that price range.

Less obvious is their impact on corporate structure, making it possible for smaller companies to compete in ways that were previously impossible. The rise, fall, and rebirth of Sequential Circuits provides an instructive case study. In the '70s, Sequential Circuits needed a staff of more than 300 to design and produce groundbreaking synthesizers like the Prophet 5. The company was later acquired by Yamaha and shut down. Company founder Dave Smith has since restarted operations in San Francisco. These days, however, Sequential designs sophisticated keyboards with a skeletal staff of well under 20, and farms out production to a nearby contractor. The way Smith explains it, with the internet and improved design technology, there's far less labor involved in tasks ranging from sourcing parts to designing circuitry. What used to take a team weeks to accomplish can now be done in a morning by a single person. The technology that allows Dave Smith to produce more with less has also given rise to scores of what can best be described as boutique manufacturers. Their presence is evident at every NAMM show, with upstarts displaying guitars, saxophones, effects pedals, and accessories.

The proliferation of boutique suppliers in the music industry also coincides with a buying public that is relentless in its demands for variety. Budweiser, the leading beer brand, has watched its unit volume steadily trend down due to the rise of scores of micro-brews. A frustrated Bud exec recently quipped, "We're not going to get swallowed by a whale, we're getting nibbled to death by minnows!" Big food brands including Kraft, General Mills, and Kellogg's are facing a similar challenge as consumers seek out niche brands that appear to be "less manufactured." In the music industry, more participants in a slow-growth market means intensified competition. And, for larger companies, their heft doesn't provide the same competitive advantage it once did. On the retail side the proliferation of brands also alters the competitive landscape.

An environment where customers demand choice, where larger retailers are trimming their inventory, and where the number of available brands steadily rises seems like fertile ground for niche retailing. Elsewhere in this issue, we highlight two unusual businesses exploiting these trends. Pedal Genie has taken advantage of the staggering number of available guitar effects to create a unique rental service that resembles Netflix. With software-based effects, can a streaming service be far behind? Guitar Sanctuary, with its stunning showroom outside of Dallas, specializes in the guitars that are not readily available online or in chain stores. Both businesses are outgrowths of these larger design and manufacturing trends. Expect more like them in the years to come.

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