EDITORIAL

DO CO-OP PROGRAMS DECREASE RETAIL PROFITABILITY?

DEALING WITH COMPARATIVELY limited promotional budgets and a narrowly focused group of customers, manufacturers of music and sound products have long relied on co-op advertising programs to build brand awareness and spur sales. Co-op programs vary from company to company, but typically the manufacturers offer retailers either additional discounts or cash payments to be applied to support brand and marketing building promotion. Co-op programs are viewed as the ultimate "win-win" situation, which helps explain their longevity. In theory, manufacturers get a higher profile among buyers, retailers get extra bucks to help boost their advertising, and everybody goes home happy. In practice, however, traditional co-op programs are generating a growing number of complaints.

The following common example helps explain why. Manufacturer "X" offers a group of catalog operators and other large retailers a hefty extra discount to advertise its line of products. With this backing, these dealers then advertise brand "X" products at near loss-leader pricing, driving market prices down across the country. Rather than work at such narrow margins, hundreds of other dealers then lessen their commitment to, or abandon altogether, brand "X" to concentrate on more profitable product offerings.

Everyone loves low prices, so it's hard to make a case against them; however, do manufacturers really advance the standing of their product lines or expand the market by underwriting rock-bottom-price advertising? Dealers doing the advertising contend that these ads build store traffic and generate sales; however, does this represent "plus" business or merely business taken from other retailers? No one knows for sure, but one thing we do know is that loss-leader pricing has the less beneficial effect of prompting scores of dealers to abandon product lines, reducing vital representation in the field. Just consider the fact that in numerous markets of over 100,000 residents certain hi-tech product lines simply can't be found in any local store. Manufacturers need to do a hard cost-benefit analysis of co-op as it's now practiced. Is the prospect of thinning the ranks of dealers and diminishing the level of local representation sufficiently offset by the extra business generated by a dozen or so dealers' aggressive discounting? We tend to think not, largely because music products are not that price-sensitive. As computer prices have declined dramatically over the past decade, unit sales have increased exponentially. By contrast, microprocessor-based synthesizers have seen comparable price reductions, yet sales volumes have actually decreased. Price reductions in just about every segment of the music products industry have had a similar nominal effect. To someone who can't play or isn't interested in playing, an instrument or a sound system at 90% off retail is still probably not worth it.

Setting pricing levels is the prerogative of every retailer, and the market justifiably rewards the most efficient. What's more, it's only logical for manufacturers to provide retailers with incentives to promote, and for retailers to seize every pricing advantage they can. Having said this, we still have a hard time understanding why so many manufacturer co-op programs succeed only in lowering street prices.

For a more enlightened approach to joint retail/supplier promotional efforts, the rest of the industry would do well to study the percussion business. Drum makers have channeled co-op dollars into underwriting artist clinics and other proven business-building "events" rather than just blow-out advertising. This is perhaps one reason why percussion products will be one of the strongest performing segments in the industry in 1997.

Brian T. Majeski
Editor