Hormon Acoustics New Business Model.

Hormon is a small company located in Madrid, Spain. The company designs, manufactures and markets high quality speakers for music systems. The company is the result of the ongoing efforts of Jose Urrialde, a young entrepreneur.

Mr. Urrialde had founded a professional sound company, mainly installing high quality public address and music systems. Mr. Urrialde realized that there was a demand from recording professionals for a high quality no-non-sense speaker system that sounded great when listened from a few meters distance.

In his free time he started designing speaker systems in the mid 90s. Urrialde is in unheard mixture of sound expert and common sense designer. In the area of high quality speakers there is a lot of hype, and people are willing to pay lots of money for speakers, based solely on intuitive and musical considerations, sometimes inaudible by the not so discriminating listener. Jose strove from the very beginning to achieve a natural sound, without incurring in the outrageous expenses involved in producing high-end speakers.

**The product**

Normally a speaker system has three (or more) basic components.

The first is the speaker(s) itself. This is the sound producing transducer, a combination of a strong magnet, a moving coil and a cone of some lighter material. The signal from the amplifier is fed to the coil, that moves inside the magnetic field created by the magnet, driving along the cone. In turn the cone moves (pushes) the surrounding air, creating pressure zones that produce sound waves. Speaker design and manufacturing is a delicate and technical operation, that is normally in the hands of specialized companies. A limited number of companies supply most of the speakers used in commercial speaker systems. Typically, a speaker system mounts a number of basic speakers. The most common number is two. One of them (smaller and lighter, perhaps 2 inches in diameter) takes care of reproducing the higher frequencies, the shrill portion of music, and the other (bigger and heavier) takes care of the bass portion. As the bass portion carries most of the energy, extra-care must be taken to ensure that bass frequencies do not reach the tweeter, whose light structure could be easily damaged by them.

The second major component of a speaker is the filter. The filter actually performs the electronic separation of the high and bass frequencies, and feeds them to each one of the (two) main speakers.

Finally the speakers should be mounted into a box. The box is critical for the end quality of the music. The reason is simple, yet elusive. When moving, the cone creates pressure while it is advancing and depression when receding. But when the front of the cone advances, the rear recedes. Therefore, in open air, the air would flow from the front of the cone to the rear, instead of propagating the vibrations to the room, where listeners normally reside. The front panel of a speaker box is critical for any design, since it radiates some of the vibrations generated by the speaker itself. As
vibrations propagate from the moving cone to its surroundings, the box contributes to the sound by providing some “coloration” to it.

One of Urrialde’s contributions was the realization that the most suitable material for building the front of the box was concrete. Thus after several years of experimentation, Urrialde put together a speaker system using a box, whose front was made up of reinforced concrete. Urrialde also designed an adapted filter, so that the speaker system was very “natural sounding”, a property that highly appreciated in recording studios. The resulting speaker had a great quality, especially when listened from a close range, 2-3 meters, typically working distances found in small recording studios, growing rapidly in Spain in the late 90s. The speakers were priced at 240 Euros a piece, and normally two were required for a stereo application.

The speaker was well received by the recording studios. Almost 100 systems were sold in the first few months, mainly in this market segment where Urrialde was well known. But the studio market was relatively small, and soon it became apparent that speaker sales were not going to boom. The bigger market was in home music systems, but this was a very difficult market to crack. Urrialde thought that the Logistics and Distribution System (the supply chain) design and operation was a major blocking factor in reaching the domestic user.

**Home-music distribution system.**

The home music market is divided in three main segments. The mass-market producers of medium quality sound systems compose the largest segment. Companies such as Sony, Pioneer, JVC, and so on, manufacture and distribute large numbers of fair to good sound systems, including both the electronics and the speakers. Prices for those systems are in 1,000-2,000 Euro range. According to Jose, the speakers are the weakest link in these kind of sound systems. The electronics are capable of supplying greater sound, yet normally hindered by poor speaker systems.

The second segment is the traditional hi-fi market. This is made up by smaller, mainly European, manufacturing companies, that sell components or even complete systems through representatives in the country and dealers of hi-fi equipment. This segment started years ago distributing Sony’s and Pioneers, and migrated to this kind of equipment as the higher quality systems became more popular and cheaper. As a result, this segment is outrageously competitive. According to Urrialde, many so-called experts try to create opinion among buyers that are not discriminating enough to judge for themselves. Trapped among the mass distributors and the high-end specialists, this segment in Spain is increasingly chaotic and lacking prestige. Systems in this range may cost anything from 2,000 to 4,000 Euro. Stores in this range look like small-speakers-and-systems warehouses. Typically they have a single listening room, where everything is displayed and may be listened to.

Finally the upper end is represented by a number of importers distributing through a few high-end stores that sell few units at a high price. Catering to a discriminating audience, they feature lavishly furnished rooms where the customer can listen to competing systems at his/hers heart content before buying. A system in this range starts at perhaps 5,000 Euro and from here upwards, the sky being the limit.
Urrialde knew his product was unprepared to compete in the high-end segment. His speaker system was in the price range of the household hi-fi systems, but had distinctive competitive advantages that made it a very special bargain. He felt that, if his speaker were to be successful, the customers had to perceive these subtle differences. The high end was the only segment where this was done by the stores, never so in the hi-fi market. He wanted to avoid being entrapped in the traditional hi-fi market where the distinctive features of his speaker could be lost amongst many lower quality competitors.

The pressures of its main company, and the impasse created by those considerations had an impact on Hormon. Manufacturing, that had been done by Urrialde and a colleague on an ad hoc basis, was stopped and the concrete speakers nearly forgotten.

In 1997 Urrialde was busy concentrating on his main business. From time to time a customer would appear asking for a “one of those wonderful concrete speakers”. He was told that a speaker would be shipped to him as soon as production restarted. However, Urrialde was puzzled by the need to design a new approach to distribution for his product.

**Come 2000**

Around mid 2000 and by pure chance, Urrialde came in contact with a previous customer, Maria Dry, that wanted to buy a new pair of Hormon Speakers. When told about the situation, the prospective customer reacted by proposing a joint venture. Urrialde would design and sell speakers. Maria, an experienced business consultant, would analyze the situation and propose and help implement new ways of reaching the end customer.

Towards the end of 2000, Maria presented her approach to Mr. Urrialde. A new company was created, where in addition to Jose and Maria, two new members contributed with capital. The company started operations early in 2001. It had two employees, plus the involvement of the founding partners. The machines, jigs and fixtures used in the previous production were contributed to the new company by Jose. He also assumed the role of product designer and implementor. The speaker was slightly redesigned.

Jose had always wanted to build a solid wooden box for the speaker system. Now he redesigned the box to used solid pinewood instead of the more traditional plywood. Even if the orthodox method to speaker design recommends plywood, as a softer material, and therefore providing less color to the sound, Jose felt that natural wood would contribute to the unique performance of his own concrete front speakers. The result was exactly as Jose expected. The sound was rounder and sharper with the new design.

Production began immediately. A Danish company, specialized in basic speakers, was chosen to be the supplier for this type of apparati. They insisted on a minimum purchase quantity, in order to be able to provide a reasonable good price. Negotiations with the Danish company had begun, and a deal was coming at the time of writing.
this case. Supply time for the basic speakers was one month, plus shipping time from Denmark.

Maria's plan called for the speakers to be targeted as replacement speakers for medium sound systems. Many people were able to afford a pair of Hormon speakers (now to be sold at roughly 600 Euro). The speakers provided a quantum leap in their system response. But people would buy, he thought, only after living the experience themselves, that is by listening to their own system with the new Hormon speakers. Not by listening to promises of dealers, all too often overblown. Experience showed that the resulting increase in sound quality was in many cases literally spectacular. Replacing the cheap speakers in a conventional system by Hormon ones, indeed provided a dramatic change in performance. Experiments were conducted with a number of friends. None of the people that had their original speakers replaced by Hormons in their home music system, wanted to return the Hormons. All of them asked to buy the systems, after being blazed by the spectacular change in quality that result from the switch.

Maria's plan tried to exploit this fact by using a mixed approach, which almost completely skipped the traditional Supply Chain in the sector. The idea was to sell speakers in an “Avon” or “Tupperware” manner. A number of people were offered the possibility of being appointed Hormon PSR (Professional Sound Representative). A PSR was a person with a feeling for music and sound, not necessarily a technical expert, with enough knowledge to be able to advise the prospective customer on the best use of Hormon Speakers.

A PSR was offered a 30% commission on the speaker price. In exchange he/she would demonstrate the speakers to his friends, at their own homes and with their music systems. He would help in installing the speakers for their listening evaluation. If after the experience, the customer decided to buy, and this was expected to be the case in a high percentage of situations, the PSR would prepare and install with the customer his new speakers. PSR’s were supposed to be part time people, students, retired persons, and in general people that wanted some extra income resulting from practicing their main hobby, music listening.

To back up the network of PSR's, a single store was appointed as a demonstration center in each geographic area. A demonstration center was paid 5% of the sales in its whole area, in exchange for keeping a display area and a listening room for Hormon speakers, well separated from all other competitors. The store took care of after sales customer service. The PSR network was rather volatile and there was a need for a professional anchoring point for the customer that had any complaints or demands for information.

An Internet channel complemented the system. A web site was created containing technically light information on speakers. It included everything an amateur, but connoisseur, would need to know about speakers and Hormon speakers in particular. Many web contents were strictly sales talk. Hormon's web was designed to give the customer all of the details that normally were not given through the traditional hi-fi channel.
Also, a customer could buy a pair of Hormon speakers on the web, and pay by using his credit card. The frequency of this event would probably be low, since the web was mainly designed as a PSR support tool.

In any case, transportation costs were charged to the customer and speakers were send by a logistics system assuring 15-30 day delivery lag anywhere in the world, and 7-15 days anywhere in Europe. A number of depots were to be created, as sales picked up in the main markets. But since Hormon was essentially a monoproduct company, this was not considered a serious drawback.

**The situation in 2001**

By the beginning of 2001 sales were beginning to increase. A first training course for PSRs was offered, with 15 people attending. The web site was completed and operational by the end of January. A store was appointed as the demonstration center for the Madrid area. Insuring the adequate supply of high quality speakers from Denmark was not going to be easy, since the Danish company insisted on a firm contract for a high number of speakers. Urrialde wanted a high level of flexibility at the initial stages of the new business, an in particular to be able to adjust its production capacity to market evolution. The Danish company expressed interest in putting together a program of joint development. Hormon considered it was too early for any agreement.

The distribution system (the SC) was rather surprised by the Hormon initiatives. It was a disruption of the traditional way of reaching the customer in the sector. Bypassing the stores, allowed Hormon to convey its distinctive message to the customer. But what would be the reaction of the stores, should the demand for Hormon speakers rise quickly? Although Hormon was going for the highterto little explored replacement market, the traditional products could feel the breath of Hormon on their backs, if, and that was a big if, the company sales picked up as expected.