

Jones • Blair Company

In early January 2000, Alexander Barrett, President of Jones•Blair Company, slumped back in his chair as his senior management executives filed out of the conference room. "Another meeting and still no resolution," he thought. After two lengthy meetings, the executive group still had not decided where and how to deploy corporate marketing efforts among the various architectural paint coatings markets served by the company in the southwestern United States. He asked his secretary to schedule another meeting for next week.

■ THE U.S. PAINT INDUSTRY

The U.S. paint industry is divided into three broad segments: (1) architectural coatings, (2) original equipment manufacturing (OEM) coatings, and (3) special-purpose coatings. Architectural coatings consist of general-purpose paints, varnishes, and lacquers used on residential, commercial, and institutional structures, sold through wholesalers and retailers, and purchased by do-it-yourself consumers, painting contractors, and professional painters. Architectural coatings are commonly called *shelf goods* and account for 43 percent total industry dollar sales. OEM coatings are formulated to industrial buyer specifications and are applied to original equipment during manufacturing. These coatings are used for durable goods such as automobiles, trucks, transportation equipment, appliances, furniture and fixtures, metal containers and building products, and industrial machinery and equipment. OEM coatings represent 35 percent of total industry dollar sales. Special-purpose coatings are formulated for special applications or environmental conditions, such as extreme temperatures, exposure to chemicals, or corrosive conditions. These coatings are used for automotive and machinery refinishing, industrial construction and maintenance (including factories, equipment, utilities, and railroads), bridges, marine applications (ship and offshore facilities such as oil rigs), highway and traffic markings, aerosol and metallic paints, and roof paints. Special-purpose coatings account for 22 percent of total industry dollar sales.

The U.S. paint industry is generally considered to be a maturing industry. Industry sales in 1999 were estimated to be slightly over \$13 billion. Average annual dollar sales growth was forecasted to approximate the general rate of inflation through 2000.

Outlook for Architectural Paint Coatings and Sundries

Industry sources estimated U.S. sales of architectural paint coatings and sundries (brushes, rollers, paint removers and thinners, etc.) to be \$10 billion-plus in 1999.

The cooperation of Jones•Blair Company in the preparation of this case is gratefully acknowledged. This case was prepared by Professor Roger A. Kerin, Edwin L. Cox School of Business, Southern Methodist University, as a basis for class discussion and is not designed to illustrate effective or ineffective handling of an administrative situation. Certain names and selected market and sales data have been disguised and are not useful for research purposes. Copyright © 2000 by Roger A. Kerin. No part of this case may be reproduced without written permission of the copyright holder.

Architectural coatings are considered to be a mature market with long-term sales growth projected in the range of 1 to 2 percent per year. Demand for architectural coatings and sundries reflect the level of house redecorating, maintenance, and repair, as well as sales of existing homes, and to a lesser extent new home, commercial, and industrial construction. Industry sources also noted that the demand for architectural coatings and sundries is affected by two other factors. First, the architectural coating segment faced competition from alternative materials, such as aluminum and vinyl siding, interior wall coverings, and wood paneling. Second, paint companies had developed higher-quality products that reduced the amount of paint necessary per application and the frequency of repainting. Counteracting these factors, industry observers foresaw increasing demand for paint sundries due to a trend toward do-it-yourself painting by household consumers.

U.S. paint manufacturers are under growing pressure to reduce emissions of volatile organic compounds (VOCs) from paints and to limit the consumption of solvents. The Environmental Protection Agency (EPA) has proposed a three-step plan for the reduction of VOCs in architectural and industrial maintenance coatings. The first phase of the plan, which took effect in 1996, required a 25 percent reduction in VOC content from the base year of 1990. VOCs must be reduced by 35 percent (from the 1990 base year) in 2000 and 45 percent in the third phase in 2003. Compliance with EPA regulations has further eroded historically low profit margins in the paint industry.

Consolidation and Competition in the Architectural Coatings Segment

Slow sales growth, the necessity for ongoing research and development, and recent compliance with governmental regulations have fueled merger and acquisition activity in the U.S. paint industry since 1990. Companies seeking growth and a higher sales base to support increasing costs are making acquisitions. Companies that were unwilling or unable to make capital and research and development (R&D) commitments necessary to remain competitive sold their paint businesses. Industry sources estimate that the number of paint companies is currently 600, or about 40 percent fewer companies than in 1975. The number of paint companies is presently declining at a rate of 2 to 3 percent per year. Merger activity generally involved the purchase of small companies by larger firms to boost their specific market or geographic presence. Still, because of readily available technology and difference in paint formulations associated with regional climatic needs, a small number of regional paint manufacturers, such as Jones•Blair Company, have competed successfully against paint manufacturers that distribute their products nationally.

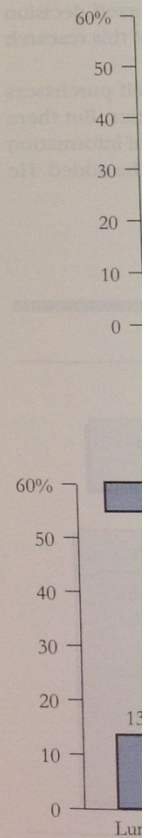
Major producers of paint for the architectural coatings segment include Sherwin-Williams, Benjamin Moore, the Glidden unit of Imperial Chemicals, PPG Industries, Valspar Corporation, Grow Group, and Pratt & Lambert. These producers account for upwards of 60 percent of sales in the architectural coatings segment. They market paint under their own brand names and for retailers under private, controlled, or store brand names. For example, Sherwin-Williams markets the Sherwin-Williams brand and produces paint for Sears.

About 50 percent of architectural coatings are sold under private, controlled, or store brands. Sears, Kmart, Wal-Mart, and Home Depot are major marketers of these brands. In addition, hardware store groups such as True Value and Ace Hardware market their own paint brands.

Specialty paint stores, lumberyards, and independent hardware stores that sell architectural paint and paint sundries have been able to compete in the paint business despite the presence of mass merchandisers (such as Sears) and home improvement centers (such as Lowe's and Home Depot). Industry sources estimate that specialty paint stores account for about 36 percent of paint and sundry sales; hardware and

EXHIBIT

Store Patrona



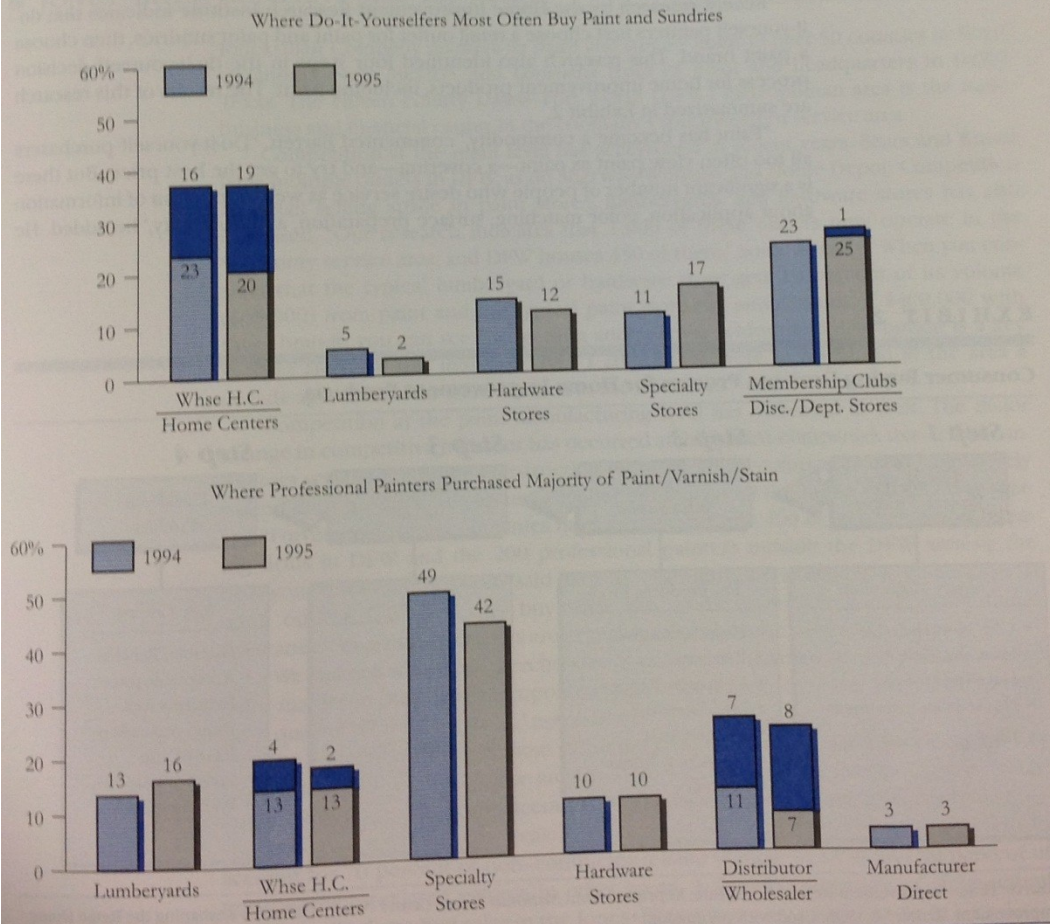
Source: Home Improvement

lumberyards account for 14 percent. Furthermore, specialty paint and hardware stores and lumberyards in nonmetropolitan areas have outdistanced mass merchandisers and home improvement centers as sources for paint and paint sundries. This is largely attributable to a lack of home improvement centers and mass-merchandise distribution in these areas and paint store, hardware, and lumberyard customer relations and service. However, Wal-Mart has been an effective competitor in many non-metropolitan areas.

Exhibit 1 shows store patronage by do-it-yourself painters and professional painters. As indicated, home centers (including wholesale home centers) and mass merchandisers (including membership clubs such as Sam's) represent the two most frequently patronized categories of retailers shopped by do-it-yourself painters for paint and sundry

EXHIBIT 1

Store Patronage by Type of Buyer: Do-It-Yourselfer and Professional Painter



Source: Home Improvement Research Institute. Reprinted from *National Home Center News*, "10 Forces Reshaping the Retail Home Improvement Market," © 1996. Used with permission.

items. Specialty paint stores and lumberyards were the most frequently patronized retail stores by professional painters for paint products and sundry items.

Architectural Coatings Purchase Behavior

Approximately 50 percent of architectural coatings dollar sales are accounted for by do-it-yourself painters. Professional painter purchases account for 25 percent of dollar sales. The remainder of architectural coatings dollar sales result from government, export, and contractor sales.

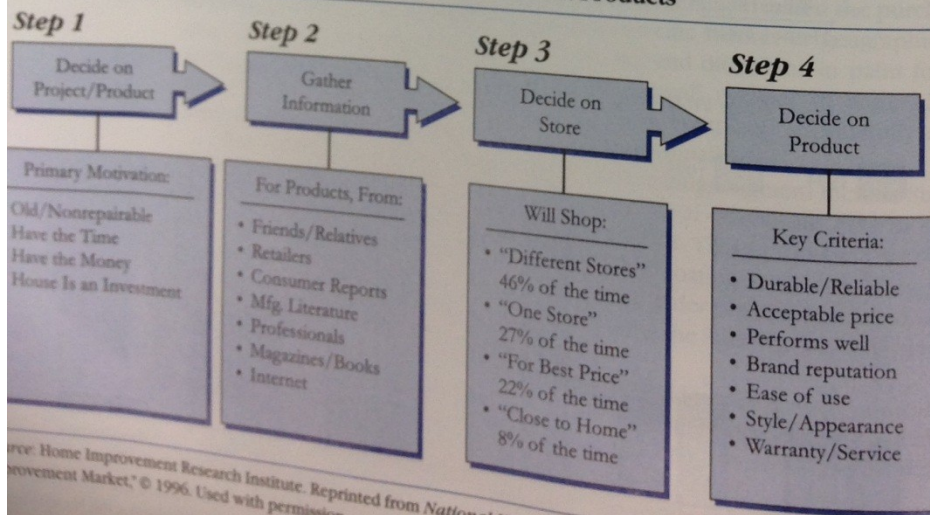
Almost 60 percent of annual architectural coatings sales are for interior paints. Exterior paint represents 38 percent of sales. Lacquers and all other applications make up the balance of sales. Slightly less than one in four households purchase interior house paint in any given year. The percentage of households purchasing exterior house paint is considerably less than that for interior paint. The popularity of do-it-yourself painting, particularly for interior applications, has increased the paint and sundry item product line carried by retail outlets. Paint industry consumer research indicates that the average dollar paint purchase per purchase occasion is about \$74.00. The average dollar sundry purchase per purchase occasion is about \$12.00.

Recent research by the Home Improvement Research Institute indicates that do-it-yourself painters first choose a retail outlet for paint and paint sundries, then choose a paint brand. This research also identified four steps in the do-it-yourself decision process for home improvement products, including paint. The results of this research are summarized in Exhibit 2.

"Paint has become a commodity," commented Barrett. "Do-it-yourself purchasers all too often view paint as paint—a covering—and try to get the best price. But there is a significant number of people who desire service as well in the form of information about application, color matching, surface preparation, and durability," he added. He

EXHIBIT 2

Consumer Buying Decision Process for Home Improvement Products



Source: Home Improvement Research Institute. Reprinted from *National Home Center News*, "10 Forces Reshaping the Retail Home Improvement Market," © 1996. Used with permission.

conceded that "once paint is on the wall, you can't initially tell the difference between premium-priced and competitively priced paint."

"There is a difference between painting contractors and professional painters, however," he continued. "Pot and brush guys [professional painters] do seek out quality products, since their reputation is on the line and maintenance firms don't want to have to paint an office each time a mark appears on a wall. They want paint that is durable, washable, and will cover in a single coat. They also look to retailers who will go the extra mile to give them service. Many request and get credit from stores. They appreciate being able to get to stores early in the morning to pick up paint and supplies. They deal with stores that can mix large quantities of custom colors and expect to work with knowledgeable store employees who can give them what they want. It is not surprising to me that paint stores remain the preferred outlet for paint and sundries for professional painters. Contractors simply want a coating in many instances and strive for the lowest price, particularly on big jobs."

■ JONES • BLAIR COMPANY SERVICE AREA

Jones•Blair Company markets its paint and sundry items in over 50 counties in Texas, Oklahoma, New Mexico, and Louisiana from its plant and headquarters in Dallas, Texas. The eleven county Dallas-Fort Worth (DFW) metropolitan area is the major business and financial center in the company's southwestern service area.

Competition at the retail level has accelerated in recent years. Sears and Kmart have multiple outlets in DFW, as do Sherwin-Williams and Home Depot. Competition for retail selling space in paint stores, lumberyards, and hardware stores has also increased. "Our research indicates that 1,000 of these outlets now operate in the 50-county service area, and DFW houses 450 of them," noted Barrett. "When you consider that the typical lumberyard or hardware store gets 10 percent of its volume (\$65,000) from paint and the typical paint store has annual sales of \$400,000 with three brands, you can see that getting and keeping widespread distribution is a key success factor in this industry. Over 1,200 outlets were in operation in the area a decade ago; about 600 were situated in the DFW area."

Competition at the paint manufacturing level has increased as well. The major change in competitive behavior has occurred among paint companies that sell to contractors serving the home construction industry. These companies have aggressively priced their products to capture a higher percentage of the home construction market. "Fortunately, these companies have not pursued the 400 or so professional painting firms in DFW and the 200 professional painters outside the DFW area or the do-it-yourselfer market as yet," said Barrett. "They have not been able to gain access to retail outlets, but they may buy their way in through free goods, promotional allowances, or whatever means are available to them in the future."

"We believe that mass merchandisers control 50 percent of the do-it-yourselfer paint market in the DFW metropolitan area. Price seems to be the attraction, but we can't quarrel with their quality," noted Barrett.

The estimated dollar volume of architectural paint and allied products sold in Jones•Blair's 50-county service area in 1999 was \$80 million (excluding contractor sales). DFW was estimated to account for 60 percent of this figure, with the remaining volume being sold in other areas. Do-it-yourself household buyers were believed to account for 70 percent of non-contractor-related volume in DFW and 90 percent of non-contractor-related volume in other areas. A five-year summary of architectural paint and allied product sales in the Jones•Blair service area is shown in Exhibit 3.

EXHIBIT 3

Architectural Paint and Sundry Sales Volume, Excluding Contractor Sales (in Millions of Dollars)

Year	Total Dollar Sales	DFW Area Sales	Non-DFW Area Sales
1995	\$75.7	\$50.9	\$24.8
1996	76.4	50.8	25.6
1997	77.6	50.5	27.1
1998	78.4	50.7	27.7
1999	80.0	48.0	32.0

■ JONES•BLAIR COMPANY

Jones•Blair Company is a privately held corporation that produces and markets architectural paint under the Jones•Blair brand name. In addition to producing a full line of architectural coatings, the company sells paint sundries (brushes, rollers, thinners, etc.) under the Jones•Blair name, even though these items are not manufactured by the company. The company also operates a very large OEM coatings division, which sells its products throughout the U.S. and worldwide.

Company architectural paint and allied products sales volume in 1999 was \$12 million, and net profit before taxes was \$1,140,000. Dollar sales had increased at an average annual rate of 4 percent per year over the past decade. Paint gallonage, however, had remained stable over the past five years. "We have been very successful in maintaining our margins even with increased research and development, material and labor costs, but I'm afraid we're approaching the threshold on our prices," Barrett said. "We are now the highest-priced paint in our service area." In 1999, paint cost-of-goods sold, including freight expenses, was 60 percent of net sales.

Distribution

The company distributes its products through 200 independent paint stores, lumberyards, and hardware outlets. Forty percent of its outlets are located in the 11-county DFW area. The remaining outlets are situated in the other 39 counties in the service area. Jones•Blair sales are distributed evenly between DFW and non-DFW accounts. Exhibit 4 shows the account and sales volume distribution by size of dollar purchase per year.

Retail outlets outside the DFW area with paint and sundry purchases exceeding \$50,000 annually carry only the Jones•Blair product line. However, except for 14 outlets in DFW (those with purchases greater than \$50,000 annually), which carry the Jones•Blair line exclusively, DFW retailers carry two or three lines, with Jones•Blair's line being premium priced. "Our experience to date shows that in our DFW outlets, the effect of multiple lines has been to cause a decline in gallonage volume. The non-DFW outlets, by comparison, have grown in gallonage volume. When you combine the two, you have stable gallonage volume," remarked Barrett.

Promotional Efforts for Architectural Coating Sales

Jones•Blair employs eight sales representatives. They are responsible for monitoring inventories of Jones•Blair paint and sundry items in each retail outlet, as well as for order

EXHIBIT 4

Account and Sales Volume Percentage Distribution by Dollar Purchase per Year

<i>Dollar Purchase Year</i>	<i>Retail Accounts</i>			<i>Dollar Sales Volume</i>		
	<i>DFW</i>	<i>Non-DFW</i>	<i>Total</i>	<i>DFW</i>	<i>Non-DFW</i>	<i>Total</i>
\$50,000+	7%	10%	17%	28%	28%	56%
\$25,000–\$50,000	14	20	34	13	13	26
Less than \$25,000	19	30	49	9	9	18
Total	40%	60%	100%	50%	50%	100%

taking, assisting in store display, and coordinating cooperative advertising programs. A recent survey of Jones•Blair paint dealers indicated that the sales representatives were well liked, helpful, professional, and knowledgeable about paint. Commenting on the survey findings, Barrett said, "Our reps are on a first-name basis with their customers. It is common for our reps to discuss business and family over coffee during a sales call, and some of our people even 'mind the store' when the proprietor has to run an errand or two." Sales representatives are paid a salary and a 1 percent commission on sales.

The company spends approximately 3 percent of net sales on advertising and sales promotion efforts. Approximately 55 percent of advertising and sales promotion dollars are allocated to cooperative advertising programs with retail accounts. The cooperative program, whereby Jones•Blair pays a portion of an account's media costs based on the dollar amount of paint purchased from Jones•Blair, applies to newspaper advertising and seasonal catalogs distributed in a retailer's immediate trade area. Exhibit 5 on page 106 shows an example of a Jones•Blair Company cooperative print advertisement. The remainder of the advertising and sales promotion budget is spent on in-store displays, corporate brand advertising, outdoor signs, regional magazines, premiums, and advertising production costs.

I PLANNING MEETING

Senior management executives of Jones•Blair Company assembled again to consider the question of where and how to deploy corporate marketing efforts among the various architectural paint coatings markets served by the company. Barrett opened the meeting with a statement that it was absolutely necessary to resolve this question at the meeting in order for the tactical plan to be developed. The peak painting season was soon approaching and decisions had to be made.

Vice President of Advertising: Alex, I still believe that we must direct our efforts toward bolstering our presence in the DFW do-it-yourselfer market. I just received the results of our DFW consumer advertising awareness study. As you can see [Exhibit 6, page 107], awareness is related to paint purchase behavior. Industry research on paint purchase behavior indicates that a large number of do-it-yourselfers choose a store before selecting a brand. However, a brand name is also important to consumers because they do think about paint they have seen advertised when choosing a brand. This becomes very important in those stores carrying multiple brands. It seems to me that we need an awareness level of at least 30 percent among do-it-yourselfers to materially affect our sales.

EXHIBIT 5

Jones • Blair Company Print Advertisement

SPRING Paint Sale

PRINT IT RIGHT
Paint
JONES-BLAIR
SINCE 1928

LIMITED TIME ONLY!

\$00.00
A GALLON

POLYFLEX EXTERIOR FLAT

- Mildew Resistant
- Resists Peeling, Flaking & Blistering
- Thousands of Colors

20

SATIN \$00.00 • SEMI-GLOSS \$00.00

MORE GREAT PAINTS ALSO ON SALE!

Wash & Wear
INTERIOR LATEX WALL PAINT
\$00.00 A GALLON
WASH & WEAR INTERIOR FLAT

- One Coat Coverage
- Spatter Resistant
- Pleasant Fragrance
- Thousands of Colors
- Easy Soap & Water Clean-up

SATIN \$00.00 • SEMI-GLOSS \$00.00

Jones-Blair
10 YEAR WARRANTY
SUPERIOR INTERIOR SEMI-GLOSS
\$00.00 A GALLON
SEMIGLOSS DECORATOR INTERIOR SEMI-GLOSS

- Scrubbable
- Spot Resistant
- Thousands of Colors
- Easy Soap & Water Clean-up

FLAT \$00.00 • SATIN \$00.00

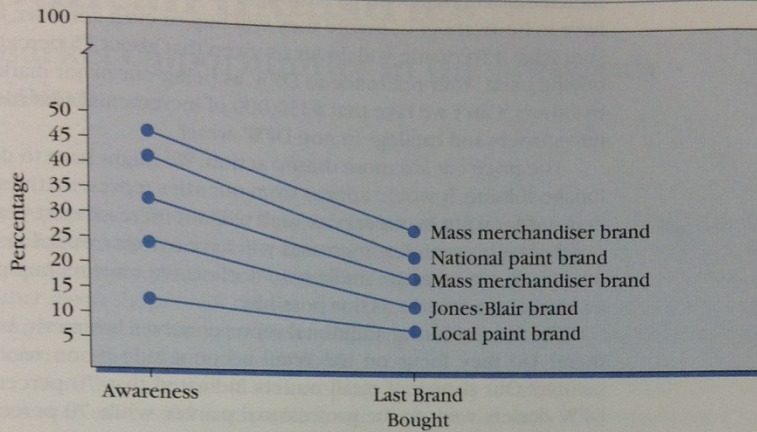
(DEALER IMPRINT)

Preliminary talks with our ad agency indicate that an increase of \$350,000 in corporate brand advertising beyond what we are now spending, with an emphasis on television, will be necessary to achieve this awareness level. Furthermore, this television coverage will reach non-DFW consumers in some 15 counties as well.

Vice President of Operations: I don't agree. Advertising is not the way to go, and reference to the DFW area alone is too narrow a focus. We have to be competitive in the do-it-yourselfer paint market, period. Our shopper research program indicated that

EXHIBIT 6

Percentage of DFW Population That Was Aware of Paint Brands and Purchased Paint in the Last 12 Months



Awareness Question: "What brands come to mind when you think of paint?"

Last Brand Bought: "What paint brand did you purchase the last time you bought paint?"

Note: Sample size was $N = 400$. Percentages are subject to a 5 percent sampling error.

dealers will quickly back off from our brand when the customer appears price-sensitive. We must cut our price by 20 percent on all paint products to achieve parity with national paint brands. Look here. In today's newspaper, we advertise a price-off special on our exterior paint, and our price is still noticeably higher than a mass merchandiser's everyday price. With both ads on the same page, a customer would have to be an idiot to patronize one of our dealers.

Vice President of Sales: Forget the DFW market. We ought to be putting our effort into non-DFW areas, where half of our sales and most of our dealers exist right now. I hate to admit it, but our sales representatives could be more aggressive. We have only added five new accounts in the last five years; our account penetration in non-DFW areas is only 16 percent. I'm partially at fault, but I'm ready to act. We should add one additional sales representative whose sole responsibility is to develop new retail account leads and presentations or call on professional painters to solicit their business through our dealers. I've figured the direct cost to keep one rep in the field at \$60,000 per year, excluding commission.

Vice President of Finance: Everyone is proposing a change in our orientation. Let me be the devil's advocate and favor pursuing our current approach. We now sell to both the homeowner and the professional painter in DFW and non-DFW markets through our dealers. We have been and will continue to be profitable by judiciously guarding our margins and controlling costs. Our contribution margin is 35 percent. Everyone suggests that increasing our costs will somehow result in greater sales volume. Let me remind you, Alex, we have said that it is our policy to recoup noncapital expenditures within a one-year time horizon. If we increase our advertising by an incremental amount of \$350,000, then we had better see the incremental sales volume as well. The same goes for additional sales representatives and, I might add, any across-the-board cut in prices.

Mr. Barrett: We keep going over the same ground. All of you have valid arguments, but we must prioritize. Let's think about what's best for all of us.

Increased advertising seems reasonable, since national paint firms and mass merchandisers outspend us tenfold in absolute terms. You are right in saying people have to be aware of us before they will buy, or even consider, Jones•Blair. But I am not sure what advertising will do for us given that about 75 percent of the audience is not buying paint. Your reference to DFW as being our major market has been questioned by others. Can't we take that \$350,000 of incremental advertising and apply it toward newspapers and catalogs in non-DFW areas?

The price cut is a more drastic action. We might have to do it just to keep our gallonage volume. It would appear from our sales representatives' forecast that gallonage demand for paint in our service area will not increase next year and we can't increase our prices this year. Any increases will have to come out of a competitor's hide. Moreover, since our costs are unlikely to decline, we must recoup gross profit dollars from an increase in volume. Is this possible?

The idea of hiring additional representatives has merit, but what do we do with them? Do they focus on the retail account side or on recruiting the professional painter? Our survey of retail outlets indicated that 70 percent of sales through our DFW dealers went to the professional painter, while 70 percent of our sales through our non-DFW outlets went to do-it-yourselfers. Our contractor sales in DFW and other areas are minimal. We would need a 40 percent price cut to attract contractors, not to mention the increased costs, expertise, and headaches of competitive bidding for large jobs.

Now that I've had my say, let's think about your proposals again. We're not leaving until we agree on a course of action.