

# How this karaoke company survived the digital darlings and made lots of money

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For a while, it looked like the beat wouldn't go on for the Singing Machine Co. The largest manufacturer of home karaoke machines in North America, founded in 1982, was being crowded out of retail store shelves by newer, cooler products such as portable DVD machines, MP3 players, digital picture frames and GPS tracking devices.

At the same time, the karaoke industry was reeling from piracy lawsuits from record labels, who claimed hardware manufacturers were infringing on their copyrighted music. Video games such as "Guitar Hero" and "Rock Band" surged in popularity, making karaoke seem dated.

In 2008, the Singing Machine, headquartered in Fort Lauderdale, lost \$3 million and the former management bailed. Its 100,000 square-foot warehouse in Ontario, Calif., was crowded with overstock and the 50-person staff was battered by layoffs. The end seemed assured.

But today, the Singing Machine is humming a much happier tune. The publicly held company reported net sales of \$48.9 million for the March 31, 2016, fiscal year end period - an increase of 24 percent over 2015 of \$39.3 million. Gross profits increased by \$3.6 million to \$11.9 million, with a profit margin of 24.4 percent (up from 3.3 percent the year before.) Inventory decreased by 50 percent to \$3.7 million.

Overall, the company reported net income of \$1.7 million - a massive leap from \$0.2 million the year before. And its uptick has continued: For

the third quarter, which ended June 30, the company saw a 40 percent increase in net sales over the same period in 2015. The microcap stock, which was valued at 19 cents last September, has doubled in value over the past year, currently trading at just over 40 cents on the OTC market.

In an era where the digital landscape continues to dictate how people consume their news and entertainment, and cellphones and tablets have started to make even desktop computers obsolete, Singing Machine reversed its fortunes by focusing on what consumers really want: Fun. Instead of sleek but plain surfaces and few buttons, the company started adding lights, colors and disco balls to their karaoke machines.

"We're doing the opposite of what the trend in technology is," says Gary Atkinson, CEO of Singing Machine, who joined the company in 2008 as general counsel. "We're pushing bigger speakers, bigger boxes, bigger lights. That stuff is what is really driving sales."

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The company's first retooled machine was the SML385 ("I wish we had named it a little better," Atkinson says), an inviting contraption of swirling colors with a top-loading compact-disc mechanism and a wired microphone. An output jack connects to the TV, so the consumer can read the lyrics as he sings along. Sold for \$70, the unit remains of the company's most popular seven years after its 2008 launch. In 2015, it was Singing Machine's No. 1 seller, moving 250,000 units.

But Singing Machine has also kept up with the times. The company's website breaks down its karaoke products into three categories: The Classic Series, or analog machines that use traditional CD technology; the Download Series, which use an 8-gigabyte USB flash drive to download songs from the company's online store and outputs high-definition graphics via HDMI; and the Streaming Series, an elegant 2.1

channel Bluetooth speaker with a remote control that doubles as a microphone. (The unit also streams HD karaoke videos on-demand to the TV via a Wi-Fi connection.)

The cosmetic changes had an immediate effect on sales, says Bernardo Melo, vice president of global sales and marketing for Singing Machine.

"You have to keep in mind how much kids love opening a big box at Christmas," he says. "They love seeing a big karaoke machine rather than a smaller item you can hold in your hand. We've stuck with that and continued to add lights and color. It really resonates with the consumers." Other companies, like Samsung and Sony, are following their lead.

Big-box retailers such as Wal-Mart, Toys R Us, Target and Best Buy have also embraced Singing Machine's happier, buzzier machines. Seventy-three percent of 2015 company sales came from brick-and-mortar retail stores, and 77 percent of sales went to their five largest customers: Toys R Us, Wal-Mart, Costco, Sam's Club and Target.

According to a study by the market research group NPD, Singing Machine ranked third in 2015 in the U.S. youth electronic entertainment retail field, which grew to a total of \$62 million in 2015 - a 4 percent growth over 2014. Singing Machine's biggest competitor was VTech Corp., a phone and electronic toys manufacturer that makes the Kidizoom Smart Watch and Kidizoom Action Cam for children.

"If you walk into a Toys R Us store, you'll not only see an endcap of Singing Machine products but you also have lit units and tablets with a live demo so customers can see the machine in action," says Steven Bielan, the president of Trend Marketing, a manufacturers' agency that represents Singing Machine to retailers in the Northeast U.S. "They've done a very good job of merchandising their product line and adding technology. They've been the innovators in the (home karaoke market).

They've made it a much more appealing product. Other people in this space tend to follow what they're doing."

By focusing on the youth market, Singing Machine has carved out a space for itself in the karaoke consumer arena, competing against companies such as the toymaker GPX and the electronics manufacturer Audiovox. Peter Chirino, owner and founder of the Miami-based Karaoke Lovers Records company, says VocoPro, Audio2000 and RSQ Audio are the leading brands among hardcore karaoke hobbyists.

But Chirino says Singing Machine's products are so popular that he continues to stock CD+G karaoke discs, which many Singing Machine models use, because the demand remains high.

Singing Machine also is benefiting from a cultural resurgence of karaoke, which is popping up everywhere from "The Late Late Show with James Corden"'s celebrity-driven Carpool Karaoke segments to the USA Network's "Mr. Robot" cyberspace-thriller series. The Tel Aviv-based PlugIN, a company that operates five upscale karaoke venues throughout Israel, is branching into the U.S. with a new 11,000-square-foot space at a Fort Lauderdale-area casino scheduled to open early 2017. The company's \$2.5 million investment in the luxurious suite of 18 private karaoke rooms with gourmet food and full bar is a testament to karaoke's lasting popularity.

"Over the years, the karaoke trend has become a widespread and popular form of entertainment for young adults," says Ally Golan, vice president of U.S. marketing for PlugIN. "However, karaoke's cultural integration and appeal has been limited in the West due to its low-end reputation.

"Karaoke bars are often associated with grimy, crowded bar scenes, where patrons sing and dance in public in typically embarrassing scenarios. PlugIN is redefining that experience, and we chose the

(Florida) location because the vibrant culture and diverse demographics of South Florida would be a perfect match for us."

Atkinson says the social aspect of karaoke is part of what has helped Singing Machine thrive alongside the digital revolution that has impacted every conceivable aspect of the entertainment industry.

"We get asked that by investors all the time: Is this new video game or app going to kill your business?" he says. "But to us, the essence of what a real karaoke experience is you have the microphone, the amplified sound so you can hear your voice through the speakers, all these different echo controls, having an audience listening to your performance. You can't do that on a tablet or phone."

The home-karaoke party isn't exclusively a U.S. phenomenon. Part of Singing Machine's growth has been taking place in the United Kingdom, where the company is aggressively marketing its products via the London-based PDT company, a vendor that specializes in music instruments and accessories throughout Europe.

"Sales of Singing Machine in Europe have grown over the past five years since we started distributing for them by an average of 70 percent per year," says David Holder, managing director of PDT. "They have gone from being a small percentage of our overall music business to becoming a multimillion dollar business, with a heavy concentration on the fourth quarter as they make such great Christmas presents.

"Until recently, karaoke was perceived as a bit of a joke in the U.K., but with parents looking for creative outlets for kids who are addicted to iPhones and iPads, singing is now encouraged as a form of expression and creativity that is 'real' rather than virtual," he said.

Holder says adults have started buying Singing Machine's higher-end

products in large numbers and expects the company's karaoke sales in 2016 to double last year's totals.

In the past, says Singing Machine's Melo, the company would have licensed its products to other companies to sell under their own brand names.

"Someone in Italy would buy one of our products but it was called Canta Tu (You Sing) and they wouldn't know it was a Singing Machine product," he says. "Our competitors have even bought the keywords 'singing machine' to use on their websites, because now you have consumers searching for 'singing machine' instead of 'karaoke.'"

Singing Machine's products are manufactured in Shenzhen, China, and stored at the warehouse in California. The company does its own shipping-on-demand, which allows retailers to avoid the inventory pressure of keeping the machines in stock.

To maximize revenue, Singing Machine has also gotten into the digital realm. Working in conjunction with Stingray Digital Media Group, a Montreal-based multiplatform music service provider, Singing Machine operates its own download store. Its current catalog lists 14,000 fully licensed songs, from Disney to country to hip-hop, intended to feed the machines it sells. The company has also started selling accessories such as microphones.

"Before, we'd sell the machine and that was the last we saw of that customer," Atkinson says. "Now we sell that same machine and open a new revenue stream where the customer comes back to us to purchase songs and accessories. We're still getting a 20-25 percent margin off the original sale, but now we're seeing revenue streams of 30-40 dollars per customer who are buying songs.

"There are always new songs coming out and there's always a new hit people want to sing. And everything falls under the Singing Machine label, so it's a great way of engaging with the brand and creating customer loyalty."

Melo says the average buyer of a Singing Machine product is "a 38 to 50-something year-old mom who is buying it for the home or for their teenage daughter or son. Then it's the grandparents and then the father. As you get into higher price points, you get guys like us who like to sing and entertain." The more expensive machines are bought by a more balanced demo.

With its growing success comes an appetite for expanding the market even more, he said. "We still have some opportunities with Best Buy that we're exploring. Kohl's is a company we want to get back as well. And this year we're launching another line of machines that will allow us to market to toy buyers and people buying Apple products in the electronics department at the same store.

"Our ideal lifecycle is you get one of these machines when you're 3 or 4, then you get another one when you're 11 or 12, and then when you grow up you buy one of the higher-end machines. We want to make people karaoke fans for life."

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## THE SINGING MACHINE CO.

What it is: Manufacturer of consumer karaoke machines, founded in 1982.

Locations: Fort Lauderdale, Fla. (corporate headquarters); Ontario, Calif. (warehouse/storage); Shenzhen, China (manufacturing)

Full-time employees: 40

CEO: Gary Atkinson

Net sales: \$48.6 million in 2016 (fiscal year ending March 31); \$39.3 million in 2015; \$31.3 million in 2014

Gross profit: \$11.9 million in 2016; \$8.3 million in 2015; \$7.1 million in 2014

Net income: \$1.7 million in 2016; \$200,000 in 2015

Income from operations: \$1.9 million in 2016; \$568,612 in 2015; \$278,965 in 2014

Ownership: Publicly held [company](#) with \$15.6 million market value trading on the OTCXQ market for over-the-counter stocks under the symbol SMDM.

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