HARVARD | BUSINESS | SCHOOL

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Hallstead Jewelers

What have we done? Daddy would know what to do, but I don't. I really thought growing this business would be an easy thing for us, but now I am not so sure. All of the work that we did in 2005 was supposed to set us up for new success, profits, and a bright future. But now, we are showing losses on both the historical investment and on our modernization and expansion.

Gretchen Reeves was talking in early February 2007 with her sister and partner Michaela Hurd after receiving preliminary income statements for Halstead Jewelers for fiscal year 2006 which had ended January 31, 2007 (See **Exhibit 1**). In a new building, just renovated in 2005, with 50% more space and selling staff than ever before, the business had experienced a loss almost double the income of the last "normal" year, 2004. To Gretchen, this did not bode well for the future.

The sisters' grandfather established Hallstead Jewelers 83 years earlier in the largest city in the tri-state region. For more than 50 years, until his death, he had nurtured and grown the original store from a start up to one of the largest jewelry and gift stores in the United States. Four departments sold almost everything that customers expected in a jewelry and gift store: fine jewelry and gems, watches, tabletop gifts (china and flatware), and artistic gifts. Customers came from throughout the region to buy from extensive collections in each department. Any gift from Hallstead's had an extra cache attached to it. It was presumed to be the best.

When Grandfather died, the store was left to his only son, who had literally grown up in the store to become his father's partner in the business. That son was the father of both Gretchen and Michaela. Another child, their brother James, had shunned the business to study medicine and surgery. The girls, however, followed in their father's footsteps and grew up in the store, learning the business. At the death of their father in 2002, the three children inherited the business as equal partners, and by agreement with James, Gretchen and Michaela took over the management of the business and store.

At the time of the sisters' assumption of the ownership and management of the store, it was still operating in the original store location on Lake Avenue and Second Avenue. In the late 1930's, Lake Avenue became the most important retail location in the city. The store was improved and provided elegant space for the display and sale of their products. It was a destination-shopping place. The store was remodeled and redecorated again after the founder died, but the location and space remained the same until 2004.

Professor William J. Bruns prepared this case. HBS cases are developed solely as the basis for class discussion. The company mentioned in the case is fictional. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

In the meantime, the principal retail shopping areas shifted two blocks west to Washington Street. Stores were larger there and could accommodate department stores and larger specialty retailers. But reputation and selection still brought customers to Lake Avenue for the selections at Hallstead's. Shopping centers were developed in suburban locations, but Hallstead Jewelers stayed put. The sisters' father saw the changes in the retail landscape, but he took no action because of them. Hallstead's was a one-store seller at its original location, in many ways an anachronism.

By the time the sisters assumed management, there were signs that it might be time for changes. Sales had been stagnant since 1999 or so, and profits were slipping. One of the sisters' first ideas was to look for another or several locations. A consultant said that they needed more space and a fresh store look. Expansion was impossible without moving, and although a move might entail some risk, he recommended that they look toward a larger location on Washington Street. They made some changes in product offerings that offered more sales potential at the cost of minor reductions in margins.

In 2004 a large toy seller with more space abandoned the corner of Washington Street and Second Avenue. The sisters wasted no time in signing a new five-year lease and starting extensive and expensive renovations. Since the new store was only two blocks from the original location, Gretchen and Michaela were confident that their loyal customers would find and follow them. Renovations and moving took most of 2005, and they started 2006 in the new store. They laughed about 2005 being a "lost" and "loss" year, but they were sure 2006 would bring a new day to Hallstead's.

The retail jewelry business was changing. Tiffany & Company, a business with an origin much like Hallstead Jewelers, had grown into an international powerhouse. With their "blue boxes" they had become the largest diamond seller in the United States. At the same time, a start- up internet seller named Blue Nile, founded in the infancy of the World Wide Web a decade earlier was the second largest diamond seller in the United States. The sisters had not had time to think about what those trends meant for Hallstead's.

But as fiscal 2006 ended and the preliminary income statement was in, both Gretchen and Michaela knew something more had to be done. They wanted to figure out what had happened between 2004 and 2006, and they wanted to explore ideas about changes in strategy that would return the business to profitability and a brighter future. Their accountant suggested that the move to a new location had changed the economics of their business somewhat, and that further changes in promotion might be in order. Increasing advertising might bring in more customers, or changing pricing formulas to fend off new internet jewelry competitors might be considered. The sisters put together some questions that they asked the accountant to analyze for them using some additional operating statistics that they had at hand (**Exhibit 2**).

Questions:

1. How has the breakeven point in number of sales tickets (number of customer orders written) and breakeven in sales dollars changed from 2003, to 2004, and to 2006? How has the margin of safety changed? What caused the changes?

2. One idea that the consultant had was to reduce prices to bring in more customers. If average prices were reduced ten percent (10%), and the number of sales tickets (unit sales) increased to 7,500, would the company's income be increased? With prices reduced, what would be the new breakeven point in sales tickets and sales dollars?

3. Another idea that Gretchen had was to eliminate sales commissions. Hallstead's was the only jewelry store in the city that paid sales commissions, and although both Grandfather and Father had insisted that commissions were one of the reasons for their success, Gretchen had her doubts? How would the elimination of sales commissions affect the breakeven volume?
4. Michaela felt that a bigger store could benefit from greater advertising and suggested that they increase advertising by $200,000. How would this affect the breakeven point? Would you recommend that the sisters try this?
5. How much would the average sales ticket have to increase to breakeven if the fixed cost remained the same in 2007 as it was in 2006?
6. What do you recommend that the managers at Hallstead Jewelers do?

Exhibit 1 Hallstead Jewelers; Income Statements for Years Ended January 31 (thousands of dollars)

	2003	2004	2006
Sales	$8,583	$8,102	$10,711
Cost of goods sold	4,326	4,132	5,570
Gross margin	$4,257	$3,970	$ 5,141
Expenses			
Selling expense			
Salaries	2,021	2,081	3,215
Commissions	429	405	536
Advertising	254	250	257
Administrative expenses	418	425	435
Rent	420	420	840
Depreciation	84	84	142
Miscellaneous expenses	53	93	122
Total expenses	$3,679	$3,758	$ 5,547
Net income	$ 578	$ 212	$ (406)

Source: Casewriter

Exhibit 2 Hallstead Jewelers Operating Statistics

	2003	2004	2006
Sales space (square feet)	10,230	10,230	15,280
Sales per square foot	$ 839	$ 792	$ 701
Sales tickets	5,341	5,316	6,897
Average sales ticket	$ 1,607	$ 1,524	$ 1,553

Source: Casewriter