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INTELLITIX: TURNING UP THE VOLUME

Mano Majumdar wrote this case under the supervision of Julie Gosse solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

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Eric Janssen, chief revenue officer at Intellitix, reviewed the last three years of operations in preparation for a meeting with the company’s founder and chief executive officer, Serge Grimaux. Toronto-based Intellitix had started as a company supplying paperless ticketing for live music events. It had since added social media integration and contactless payments to enhance the attendee experience.

It was now January 2016, and Janssen was considering several alternatives for the future of the business: pursuing fixed venues such as amusement parks and campuses; expanding to other live entertainment events such as food festivals and conferences; or expanding the business to new geographies. Janssen knew growth was important for Intellitix and that it was his primary mandate, but he also wondered if reaching out of its core market was wise or even necessary, especially when the market was far from saturated and Intellitix had a strong, reputable brand.

THE LIVE MUSIC INDUSTRY: North America AND BEYOND

The live music industry included indoor and outdoor performances by artists—with managers, promoters, agents, music venues, and music festivals as other major stakeholders. The music industry was one of the most concentrated in Canada, with Ontario representing over 80 per cent of both recording industry expenditure and live music revenue nationwide. Remarkably, the music industry represented a larger share of employment in Toronto than it did in Austin, Texas—one of North America’s most iconic music markets.[[1]](#footnote-1)

There were 1,240 companies active in the live music industry in Ontario in 2013, supporting 10,500 full-time equivalent[[2]](#footnote-2) jobs and generating CA$1.2 billion[[3]](#footnote-3) in economic activity. Half of the impact on employment as well as the economic activity came from the direct operations of the live music industry, and the rest was attributed to the industry’s effect on tourism.[[4]](#footnote-4)

There were 558 live music festivals held in Ontario in 2013, with 15.7 million tickets sold to 13.7 million unique visitors. Of these, 38 per cent were large festivals, defined as having ten thousand or more attendees. The major expenses of a festival were programming[[5]](#footnote-5) and labour, which accounted for 56 per cent of all costs. In contrast, ticketing amounted to only 1 per cent of expenditure. Over 70 per cent of tickets sold by venues, festivals, and promoters were sold locally.

A major challenge facing the industry was matching capacity to demand. While artists and managers bemoaned the paucity of adequate venues outside the Greater Toronto Area (GTA), more venues were required in the GTA itself to meet peak demand in the summer. There was also noticeable daily volatility in demand. Almost half of all venues were less than 50 per cent full during the average weekday, with over a third less than 25 per cent full. Music festivals relied heavily on food and beverage sales to complement the contribution from ticket sales. The fixed costs of each event were significant, and so any incremental revenue from such supplementary sources had a disproportionate effect on the bottom line.

Globally, live performances were the source of nearly 13 per cent of all music revenues, growing at the rate of 3 per cent a year. Live music revenue in the United States, one of the most lucrative and best-understood markets, was projected to exceed US$10 billion for the first time in 2018. Live performances remained an important source of revenue, especially for the best-known artists. In 2016, concert tours accounted for 88 per cent of the earnings of Beyoncé Knowles-Carter, the highest paid musician in the United States that year. American consumers allocated 49 per cent of all their music spending to live music (concerts, festivals, and performances), with the rest allocated to the purchase of recorded music.

The scale of music festivals reflected their central role in the industry. The Coachella Valley Music and Arts Festival (Coachella), the largest music festival in the world, earned US$115 million in revenues from 250,000 tickets and hosted close to 100,000 visitors on each day of the festival.[[6]](#footnote-6)

Intellitix

Background and Culture

Serge Grimaux was an experienced event promoter and serial entrepreneur who had founded two companies before starting Intellitix in 2011. In 1992, Ticketpro, one of his previous companies, based in the Czech Republic, introduced the first computerized ticketing network in Central and Eastern Europe. This company was sold to Live Nation Entertainment Inc., one of the largest online resellers of concert tickets in North America. Grimaux’s nearly 40 years of experience, intimate knowledge of the music industry, and familiarity with the process of delivering a successful event made him a unique asset to Intellitix.

Eric Janssen was a graduate of the honours business administration program at Ivey Business School in London, Canada. His experience leading sales and business development at Canadian software start-ups Mobiroo and Wrapp had made him a strong candidate for a similar role at Intellitix. Grimaux brought Janssen into Intellitix as an equity partner in 2014, with the mandate to manage and increase revenues.

A substantial proportion of Intellitix employees were recruited from the live music industry and could easily relate to their customers’ pain points. These employees perceived Intellitix as a “music company” for both personal and historic reasons. Grimaux took a broader view and described Intellitix as an “innovation company” and as “the bridge between the digital community and the real-life community.”

Product

The core of Intellitix’s business was a software platform that supported entry management, cashless payments, and customized user experiences for events. This software ran on a cloth wristband containing a radio-frequency identification (RFID) chip,[[7]](#footnote-7) sourced from a manufacturing partner. The chip acted as a passport, giving attendees access to select performances or services.

The inspiration for the product came from Grimaux’s experience in 2009 as an exhibitor at the Festival d’été du Québec. The event had utilized paper wristbands of eleven different colours to discern the various rights of admission among its attendees—a system that broke down rapidly when it had to provide timely access to over a hundred thousand people for a performance held in the dark. Grimaux had realized that RFID was the ideal solution to this problem.

Another problem faced by events was the practice of attendees sharing wristbands with each other—a phenomenon known as a “passback.” Grimaux had estimated that passbacks lost events between 2 and 5 per cent of sales and that deploying more personnel to monitor lines was neither cost-efficient nor effective. The Intellitix solution eliminated passbacks, providing an immediate payback. The Intellitix system also eliminated shrinkage from counterfeit tickets, radically reduced queueing time, and generated real-time location data on attendees. The typical Intellitix engagement was a ticketed event with 10,000 or more attendees over multiple days—so this added up to a significant dollar value. Grimaux believed that this financial benefit had made Intellitix such a compelling product and led to its enthusiastic adoption.

The Intellitix wristband was also integrated with is proprietary contactless payment solution, meaning that attendees no longer had to carry cash or cards at events, which deterred crime and encouraged sales of products ranging from alcohol to souvenir shirts. Janssen considered this aspect of the service a key motivator for events, noting that on-site sales rose between 30 and 100 per cent at events where this payment solution had been implemented. On-site food and beverage prices were typically marked up aggressively and therefore were quite lucrative.

Integration with social media added another layer of utility to the wristband. For example, linking the wristband to a social media profile could give a patron access to a playlist of bands that had performed at a festival. At each performance area at the Bonnaroo Music and Arts Festival (Bonnaroo), Intellitix had set up booths where attendees could tap their wristbands to take a photo and automatically post it to their Facebook account.

Customers

Some of Intellitix’s earliest customers were also some of its best-known and most lucrative. These included Coachella, held annually outside Palm Springs, California; Bonnaroo, a four-day music festival in Manchester, Tennessee; and Tomorrowland, an electronic dance music festival held in Boom, Belgium. Intellitix had offices in Montreal, Quebec; Chatham, Ontario; and Budapest, Hungary, and would hire local representatives as necessary to support its international customer base.

TRADE CHAIN

Music festivals and other entertainment events were increasingly incorporated, particularly to limit legal liability for their investors. Intellitix directly sold its products to the events, internally known as customers. The people who attended these events were variously called participants, consumers, attendees, guests, or patrons.

Competitors

Connect&GO

Montreal-based Connect&GO (C&GO) had significant product overlap with Intellitix. It offered contactless access and payments, augmented experiences for guests, and data collection and analysis for events. Unlike Intellitix, its platform could be accessed using a variety of wearable devices, including not only wristbands but also cards, key chains, and stickers.

C&GO was also noted for creating novel ways to integrate RFID into guest experiences and for its diverse network of industry partners, including HBO, the Toronto Maple Leafs, Honda Motor Company Ltd., Rogers Telecom Inc., and PepsiCo Inc. One example that typified both aspects was Delirius, an interactive game for guests at the 2015 Just for Laughs Festival in Montreal. The game could be played over the entire sixteen-day open-air festival and offered contest prizes, keeping consumers incented and invested. Guests were able to link the wristband to a credit card and access discounted prices. The program was created in partnership with Tangerine, a financial services company, and over 350,000 wristbands were distributed for the occasion.

C&GO’s other prominent clients included C2 Montréal, an annual business conference, and the Osheaga Music and Arts Festival. Market rumour had it that C&GO was also being considered for future editions of the Montreal Grand Prix, which would further cement its reputation as the service provider of choice for notable mass attendance events.

Token Mobile Solutions Inc.

In contrast to Intellitix and Connect&GO, Token Mobile Solutions Inc. (Token) considered RFID a needlessly expensive technology and instead stored its virtual tickets directly on customers’ phones. This naturally appealed to more financially constrained ventures such as smaller music and food festivals. Toronto-based Token was active mainly in southern Ontario and counted the Toronto Craft Beer Festival and the Downtown Kitchener Ribfest and Craft Beer Show among its customers.

In addition to access and payments, Token offered events the ability to view real-time event statistics on a back-end application (app) called Gate. The company sent employees on-site to support event staff and promised to set up new vendors rapidly, going so far as to supply tablets pre-loaded with Gate.

Unlike Intellitix or C&GO, Token’s app required patrons to purchase “tokens,” which could then be spent at an event. Unused tokens could be refunded automatically or on request, or patrons could donate them to a charity of their choice. Token charged a 6.95 per cent transaction fee on purchases, and all refunds were free.

Alternatives

Option 1: Status Quo

Janssen started by establishing a baseline for the company as it stood. He believed that the company would increase revenues by 50 per cent yearly[[8]](#footnote-8) (see Exhibit 1). Intellitix had almost no competition in its early years, but its success had drawn at least two new competitors into the market since. So far, Intellitix had spent a relatively small share of revenue on advertising, but Janssen believed that protecting their market share would require tripling this amount for 2014 (see Exhibit 2). Thankfully, the lease on their current office spaces was finally ending. The company had grown into its present combination of leases with the same landlord over time, and next year it would finally be moving into a consolidated office that cost 15 per cent less than the current lease (see Exhibit 3). The two partners were excited to move to this new space, but it would not be ready until July. All other expenses would likely remain proportional to sales (see Exhibit 4).

Option 2: Fixed Venues

Expanding the business into fixed venues was another option. These included attractions such as amusement parks, museums, and zoos; temporary populations such as campsites and cruise ships; and permanent communities such as campuses and offices. Any clearly defined space that needed to control access, track participants, or accept payments was a potential customer.

Pursuing fixed venues would require some new investments on Intellitix’s part. At present, all the equipment needed was transported to the event site in large production trailers. This included servers, scanners, networking equipment, and kiosks for loading more money onto the wristbands. Much of this equipment had to be retrofitted to be safe for transport and for use in the chaotic environment of an outdoor music festival. Another challenge of festivals was the sheer number of personal devices attempting to access the Internet simultaneously, causing slower and dropped connections. Intellitix considered uninterrupted and rapid access to its servers crucial to its success, and so it operated a closed-loop network, with local servers running independently of the public network.

In contrast, an office inside a fixed venue would eliminate most of this complexity and many points of failure. Janssen estimated that the research and development costs to modify the Intellitix system to a permanent installation with almost no maintenance needs would be about $1,500,000.

Janssen knew that year-round customers would also demand dedicated year-round support and troubleshooting, which was a new capability Intellitix would need to develop. He knew of more than one enterprise software business that had acquired customers at a rapid pace and then lost them just as quickly by failing to plan for adequate post-sales support. He was determined to avoid that fate for Intellitix.

Market research indicated that customers would need close support for the first year, which could be provided by a technician paid an annual salary of $70,000 including benefits. The goal in the first year was to help the client understand the system and learn to operate it independently. From the second year onwards, the customer could be weaned off tier-one support and be transitioned into tier-two support, which was offered from a remote location and was less intensive. One tier-two technician could then support as many as ten customers.

Fixed venues were also interested in five-year contract periods. By contrast, festivals typically required annual contract renegotiations, a costly procedure that added to the volatility of Intellitix’s finances.

So far, four fixed venues had expressed interest in the Intellitix platform, and Janssen wanted to ensure this option was financially feasible under this scenario. Janssen estimated that Intellitix could charge $250,000 in annual licensing fees and a one-time fee of $500,000 for initial hardware and installation. The one-time fee had no markup built in.

The relative ease of serving fixed venues had not gone unnoticed by competitors, and this space was already dominated by established players with niche-specific knowledge. Janssen worried that Intellitix’s four potential fixed-venue customers could easily be reduced to one by the time Intellitix had its system ready to deploy, turning the promise of millions of dollars in earnings into a costly misadventure.

**Option 3: Similar Industries**

Janssen wondered if there was a compromise to be found halfway between continuing the status quo, on the one hand, and jumping to an entirely new category of clients, on the other. Live music was not the only industry attracting large crowds. Food festivals, conferences, and sporting events, including the emerging industry of e-sports, were also close analogues.

The main advantage of pursuing other industries was that it required no new investment in machinery or dedicated support. With a few modifications, Intellitix could extend its existing operations to address these markets.

The key challenge of this route was that it had taken years to build the reputation and relationships Intellitix had in the music industry, aided by Grimaux’s personal network from his previous career. If it decided to pursue this option, Intellitix would need to qualify new customers, educate them about the product, and build a presence anew in each industry. Janssen was confident that the existing sales and marketing team had the capacity to do this, but he would need to allocate additional funds for an aggressive outreach campaign.

The initial campaign, marketing materials, website, and training would require an estimated investment of $250,000. Each new customer could be expected to create an additional $75,000–$87,000 in revenue and $20,000–$23,000 in expenses.

Option 4: New Geographies

Most music festivals were held during the summer, and as a result, 80 per cent of Intellitix’s revenues were generated during the second and third quarters of the calendar year (April to September). Janssen was interested in boosting revenue during the “shoulder seasons” in the first and fourth quarters, when Intellitix continued burning $500,000 per month in fixed costs without generating sufficient revenue to cover it. This was also a drag on employee morale—a sharp contrast from the ambience of excitement and sense of mission that normally prevailed at Intellitix. Intellitix’s core markets were in Canada, the United States, and western and central Europe. The shoulder season in the northern hemisphere was during the southern hemisphere’s summer, and Australia and Brazil, with their blend of purchasing power and popularity as tourist destinations, stood out as attractive markets.

Intellitix’s first foray into one of these markets had been in Brazil, where it had started with an all-Canadian team with the intention to validate the market before making any serious investments. Intellitix’s lack of name recognition and the perception of Intellitix as a foreign company with no local ties posed several challenges. Practical difficulties such as language barriers and regulatory nuances had convinced Janssen to seek out a local partner for future projects. The most likely candidate was a São Paulo–based event management company that wanted a controlling interest in a joint venture in return for a licence on Intellitix systems. Intellitix would receive a share of the earnings but would not be able to reflect the entire revenue earned by the joint venture on its own books. Janssen knew that this was a structure Intellitix could easily deploy, but he also wondered if it might affect the company’s valuation for future investors.

Option 5: Valuation and Exit

Intellitix had not only managed to survive beyond the difficult first three years but had also generated positive income from day one and increased its revenues consistently. While both Janssen and Grimaux enjoyed the creative challenge of growing the company, they also thought that it might be wise to sell the business while the momentum was strong and competition still far from mature. Grimaux’s experience as a serial entrepreneur and Janssen’s business development experience meant that neither of them would have any difficulty finding their next project.

Valuations in the information technology sector, especially for companies like Intellitix that generated so much of their income from intellectual property, were tricky to achieve. Typically, hardware companies commanded a multiple of two to four times revenue, while software-as-a-service companies could go for five to seven times revenue. In contrast, companies in the data space could see a multiple of 10 times or more. Intellitix had started highlighting the data aspects of its business for this reason.

Conclusion

Janssen pondered his responsibility to the many stakeholders whose outcomes were tied to the success of this venture. Grimaux as well as employees, investors, and customers would be affected by Janssen’s recommendation, and every alternative had both pros and cons. Janssen’s first job after graduation had been as a lecturer at his alma mater, teaching a business course. A case competition organized as part of that course had asked students to make a complex business decision, and now he wished that he could turn his situation into that competition and see what the students would make of it.

**Exhibit 1: Intellitix Statement of Earnings (YEARS ENDING DECEMBER 31)**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2014** |
| Revenue | $6,193,190 | $4,075,680 |
| Cost of sales | 2,975,579 | 2,116,391 |
| **Gross profit** |  |  |
| Operating expenses |  |  |
| Salaries and benefits | 1,055,800 | 529,838 |
| Travel, meals, and lodging | 700,205 | 307,560 |
| Marketing and promotions | 165,750 | 122,270 |
| Rent expense | 372,590 | 153,025 |
| Equipment expense | 61,932 | 40,757 |
| Office expense | 46,050 | 26,052 |
| Other | 61,395 | 35,650 |
| **Total operating expenses** | $2,463,722 | $1,215,152 |
| Amortization | 845,535 | 730,555 |
| **Operating income** | (91,646) | 13,582 |
| Interest expense | 95,005 | 75,125 |
| Net earnings before taxes | (186,651) | (61,543) |
| Taxes\* | – | – |
| Net earnings after taxes | $(186,651) | $(61,543) |

Note: \*Under Canadian law, losses in one year could be used to offset taxes on positive income in future years, a feature known as a tax loss carry-forward. At the end of 2015, Intellitix had sufficient credits to make the next $1,400,605 in net earnings tax-free.

Source: Company documents.

**Exhibit 2: Intellitix STATEMENT OF RETAINED EARNINGS (AS OF DECEMBER 31)**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2014** |
| Starting retained earnings | $946,026 | $1,007,570 |
| Plus net earnings | (216,651) | (61,544) |
| Minus distributions | – | – |
| Ending retained earnings | $729,375 | $946,026 |

Source: Company documents.

**Exhibit 3: Intellitix BALANCE SHEET (AS OF DECEMBER 31)**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2014** |
| **ASSETS** |  |  |
| Current assets |  |  |
| Cash | $506,715 | $910,219 |
| Accounts receivable | 500,083 | 250,075 |
| Prepaid expenses | 103,960 | 61,499 |
| Total current assets | 1,110,758 | 1,221,793 |
| Fixed assets |  |  |
| Computer and electronics | 580,865 | 4,325 |
| Hardware | 1,066,945 | 1,025,438 |
| Furniture, crates, and cases | 135,858 | 153,536 |
| Leasehold improvements | 26,614 | 17,622 |
| Total fixed assets, net | 1,810,282 | 1,200,921 |
| Intangible assets |  |  |
| Intellectual property | 220,917 | 435,849 |
| Software | 948,609 | 521,587 |
| Total intangible assets | 1,169,526 | 957,436 |
| **Total assets** | **$4,090,566** | **$3,380,150** |
| **LIABILITIES** |  |  |
| Current liabilities |  |  |
| Bank indebtedness | $29,429 | $24 |
| Accounts payable | 695,069 | 407,168 |
| Due to a shareholder | 118,628 | 301,402 |
| Total current liabilities | 843,126 | 708,594 |
| Long-term liabilities |  |  |
| Long-term debt | 1,995,065 | 1,202,530 |
| Shareholder loan | 523,000 | 523,000 |
| Total long-term liabilities | 2,518,065 | 1,725,530 |
| **Total liabilities** | **3,361,191** | **2,434,124** |
| **EQUITY** |  |  |
| Retained earnings | 729,375 | 946,026 |
| **Total equity** | 729,375 | 946,026 |
| **TOTAL LIABILITIES AND EQUITY** | **$4,090,566** | **$3,380,150** |

Source: Company documents.

**Exhibit 4: Intellitix FINANCIAL RATIOS**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2014** |
| **Liquidity** |  |  |
| Current ratio | 1.32 | 1.72 |
| Acid test ratio | 1.19 | 1.64 |
| **Efficiency** |  |  |
| Age of accounts receivable | 29.5 days | 22.4 days |
| Age of payables | 83.5 days | 49.6 days |
| Age of inventory |  |  |
| **Stability** |  |  |
| Net worth to total assets | 17.8% | 28.0% |
| Interest coverage |  |  |
| **Growth** |  |  |
| Sales | 52% | 48% |
| Net income |  |  |
| Total assets | 21% | 17% |
| Equity | (23%) | 3% |

Source: Company documents.

1. “The Great Musical North,” Martin Prosperity Institute: Rotman School of Management, University of Toronto, 2009, accessed June 30, 2018, http://martinprosperity.org/images/stories/jmc/cache/mpi-The\_Great\_Musical\_North.pdf. [↑](#footnote-ref-1)
2. Full-time equivalent jobs were thirty hours of employment for one person over one week. [↑](#footnote-ref-2)
3. All currency amounts are in CA$ unless otherwise specified. [↑](#footnote-ref-3)
4. “Live Music Measures Up: An Economic Impact Analysis of Live Music in Ontario,” Music Canada, accessed June 30, 2018, https://musiccanada.com/resources/research/live-music-measures-up/. [↑](#footnote-ref-4)
5. Programming was an industry term that referred to the cost of paying artists for performances. [↑](#footnote-ref-5)
6. “Statista Dossier on Live Music,” Statista, 2018, accessed August 8, 2018, www.statista.com/study/37206/live-music-statista-dossier/. [↑](#footnote-ref-6)
7. Radio-frequency identification chips were read using radio waves. [↑](#footnote-ref-7)
8. Cost of sales was expected to continue at present levels. [↑](#footnote-ref-8)