

Libey Economic Outlook

May 2006

Donald R. Libey, Editor

Published Exclusively For Clients Of

Libey Incorporated

Consultants & Recruiters to Multichannel Direct Marketing

Cherry Hill, New Jersey Des Moines, Iowa

www.libey.com

Case Study: Don's Bait Shop 1953

Real Fundamentals for Success

Donald R. Libey

The Start-Up

My first knowledge of gross margin and net profit came on a Saturday morning, June 13, 1953 at Avon Lake, Ohio on the south shore of Lake Erie. That was the day I opened my first business: Don's Bait Shop. It was a moveable business, self-contained in a Western Auto red wagon, pulled to various lake-front locations by the proprietor, a chubby nine-and-a-half year-old kid seeking sufficient wherewithal to purchase Cokes and snacks while otherwise idling in the out-of-school summer sun.

The business had four large (two-gallon size) metal pots, liberated from my Mother's later-summer canning of tomatoes, string beans, peas and corn. One was filled with rich, dark dirt from the family garden and three with water dipped out of Lake Erie. In the dirt were dozens of giant night crawlers from the garden. In the three pots with water were assortments of dozens of small, medium and large minnows netted upstream from a creek that emptied into the lake. These were plump fingerlings that were irresistible to the Lake Erie Sheepshead and the other three- to five-pound lovelies that the fishers of Avon Lake went a mile or more by boat out into the lake to catch.

My business day—in an early pattern that would stay with me the rest of my life—began at 4 a.m. Out in the garden in moonlight, I forked up night crawlers, having

wet the ground well the evening before to draw them up to the surface. With a gross or two of worms fresh and active, I moved to the creek area about 5 a.m. and began netting and sorting minnows. By 5:30 a.m., I was enroute to my early morning selling location, the Avon Lake Boat Club where the fishermen (and they were, entirely, men) hauled their boats from the boat sheds to the water on a miniature trolley. I set up Don's Red Wagon Bait Shop on the shore at the end of the trolley tracks, ready for business by 5:45 a.m.

Night crawlers and minnows were priced at fifteen cents a dozen or two-dozen for a quarter. My inventory was two gross minnows and one gross worms, or thirty-six dozen in total. I usually sold out by 7 a.m. and my revenues were \$4.50 for three hours work. I could do that seven days a week for \$31.50 total revenue a week. My gross margin was one hundred percent (the inventory was free) and my net earnings were \$31.50 a week (no overhead, no marketing costs, no variable expenses). And, it was a cash business making about \$400 a summer, a veritable fortune in 1953 for a kid.

The fishermen learned after the first week that I would be there—rain or shine—every day. They also learned that—for a quarter or two—I did all the work and they didn't have to dig or net or go to the real bait shop in town which didn't open until 7 a.m. or maybe 8 a.m. I was sold out by then and off to the bakery for doughnuts.

I had figured out that all I had to do was go where the sale could be made easiest and earliest. I also figured out that I needed a better product—fresher, well-oxygenated, clean water with frequent changes, no lifeless worms, no dead floaters in the pot. And I learned the sweet spot for pricing was two dozen with a five cent savings. The average order value was fifty cents, eight to ten orders a day, heavier on Saturday, highly seasonal.

The other element to the business was the short, moon-faced kid with the perpetual smile of summer and the question asked to every fisherman, "Ever seen fatter minnows or livelier, Sir?" In my striped polo shirt and buzz cut, I was as irresistible as the product. The fishermen *wanted* to buy from me. Most of them saw themselves when they were my age. Plus they admired entrepreneurship and politeness.

So what did Don's Bait Shop have? It had great products and a great target market. It had great service. It had a great offer. It had great rapport with customers. And it had location and an "early-bird-gets-the-worm" strategy—literally. I can't see where anything has changed in the fifty-three years since then.

The Expansion

After the first few weeks, I decided to add white bass lures to my Red Wagon Bait Shop. Lake Erie used to have schools of white bass numbering in the thousands. They would boil the surface of the lake in a feeding frenzy, especially when the Mayflies or, as we called them, Canadian Soldiers, hatched and lived out their amazingly short twelve-hour lives. White bass are attracted to a white feather lure, usually two or four on a spreader attached to a four-inch oval-shaped wood float, a kind of giant bobber. Well, the feeding frenzy was so violent that you could catch four fish as fast as you could cast and reel in your rig. I can remember fishing with my brother and our father and taking as many as six-hundred white bass at a time. We froze them and actually ate bass filets all year. Many lures and bobbers were constantly lost in the action and the fishermen would have to re-rig and re-supply. I learned that they would pay me to make their rigs.

I started creating my own lures to sell and shaping and painting my own bass floats. Of course, this involved the purchase of fish hooks and, so, it was off to the Western Auto store and the fishing aisle for least-cost hooks. The white feathers I obtained free from a chicken coop down the road. The rest was a little paint and time

spent in the garage. Result: An additional \$14.00 a week. My business had grown by almost forty-five percent.

The Market Growth

Now, a lot of people would buy a bigger red wagon. But, I actually remember sitting on the granite pier with my feet in the water and thinking about how to make more money. I discovered I had a loyal customer base and I had some excess capacity. My chores in those days involved weeding and hoeing a half-acre family garden. We canned vegetables, tomatoes, corn, and grew all of our own produce, including carrots, lettuce, radishes, and a variety of other garden delights. There was more produce than we could ever eat and we shared a lot of it with neighbors. We lived right on the bank of Lake Erie and the abundance was phenomenal. We had Beefsteak tomatoes that went two pounds each.

I proposed a deal with my parents whereby I would expand the planted area and maintain the garden in even better condition if they would allow me to harvest and sell a wagon-load of assorted produce each day. They agreed.

You see, all those fishermen had to come back to the boat yard. Some had fish, some didn't, but all had to go home to the family. They would start coming in from the lake about 2 to 3 p.m., generally in time to catch the Cleveland Indians game on the radio at the Avon Lake Tap and knock back a couple before going home. So, there I was with—you guessed it—Don's Red Wagon Produce Stand. I made their lives easier by providing beautiful peace offerings and bounty for the table. I worked this gig from 2 p.m. to 4 p.m. and *always* sold out. "Excuse me, Sir. Ever seen such huge tomatoes and so many for a quarter?" Tomatoes were a quarter a basket (usually five big ones). Carrots were ten cents a bunch. Beans were fifteen cents a basket (big, overflowing, green or yellow). Lettuce and cabbage was a dime a head. The net additional revenue for another three hours of work: another \$4.00 a day and about \$24.00 a week.

Now the business was bringing in almost \$70.00 a week. And my only costs were fish hooks and seeds. My net EBITDA was about \$69.00 a week. I had an \$800 summer business and, at a multiple of 5 times EBITDA, it had a valuation of \$4,000. There were grocery stores in Avon Lake, Ohio in 1953 that weren't doing that well!

Both Don's Bait Shop and Don's Produce Stand had exactly the same business model: product, service, offer, rapport, location. Thirty-seven years later, I would start the Olde Maine Lobster Company, and I was still netting my product from the water at no cost and selling it by catalog for \$22.00 a pound delivered to your door. Even today, as a consultant, I still have a one hundred percent gross margin business.

Sure, the old Avon Lake Boat Club location has now morphed to become a catalog and a website, but the fundamentals of the business remain exactly the same: a strong target audience, immediately identifiable, good products, good service with innovation, doing business with people you like and who like and respect you, and finding ways to sell more stuff to the same customer, preferably at a high margin.

We direct marketers sometimes tend to get a little tangled up in our socks. We try to make it all so complex and formulaic, so analytical and metrically introspective that we forget what it was we set out to do: find good products to sell to loyal customers and give them service and an offer that makes it easy to buy from you; plus be there earlier and longer and at the right place at the right time—and smile and ask for the order.

I've been thinking about shining up the old red wagon and heading down to the lake early in the morning . . . I don't need too much more than \$69.00 a week . . . and it would be such fun again to ask, "Ever seen such fat and lively minnows, Sir?"

The Second Quarter 2006 Regional Economic Outlook

The second quarter of 2006 is progressing well. Economic growth is strong and all regions are performing positively and reporting strength in almost all sectors. The only negative is high gas and oil costs which have the potential of becoming nasty and creating a drag on stability.

Among catalogers, the first four months of 2006 have been healthy and projections are being met or exceeded in both business-to-business and business-to-consumer operations. Again, the cautionary note is energy costs and the potential for creating a slowdown in the summer months and beyond. Prospecting and online growth are both receiving solid investment and most catalog and multichannel companies are actively growing their new customer files and aggressively marketing to their existing customer base.

This has become a four-year plus expansion where the only slowdowns have been seen as a result of natural events (severe weather). In the past thirty years, the U.S. has not had such a prolonged growth performance, nor has it been experienced in nearly all regions of the nations. Regardless of oil shocks or the effects of military action in several hotspots, the economy continues to produce even as the national economic status deteriorates. At some point, this has to slow down, but it doesn't appear to be anytime soon.

I admit to a deep concern over the price of oil. I have clear memory of the 1970s and rationing, as well as interest rates at twenty percent and inflation at sixteen percent and higher. Should that occur, the economy may not withstand the pressures.

Signs of Regional Stability or Status Quo

Region One (CT, ME, MA, NH, RI, VT)

Region Two (NY, NJ, CT, PR, VI)

Region Three (PA, NJ, DE)

Region Four (OH, KY, PA, WV)

Region Five (KY, MD, TN, VA, NC, SC)

Region Six (GA, AL, FL, LA, MS, TN)

Region Seven (IL, IN, MI, WI, IA)

Region Eight (MO, IL, IN, KY, TN, LA, AR)

Region Nine (MN, WI, ND, SD, MT, MI)

Region Ten (KS, CO, MO, NE, NM, OK, WY)

Region Eleven (TX, LA, NM)

Region Twelve (CA, UT, AZ, NM, OR, WA)

Slower (Individual states)

Louisiana

Mississippi

The Second Quarter 2006 Circulation and Prospecting Outlook and Recommendations

Synopsis

The short-term economic outlook for the catalog industry continues to be robust and very positive. The intermediate-term outlook remains positive for the second half of 2006, and the long-term outlook through 2007 remains positive.

Continue Prospecting

Continue with moderately aggressive growth strategies for circulation and prospecting plans and force new customer development to sustain the positive momentum. There continues to be nothing (except oil prices) in the economic outlook for the second and potentially third quarters of 2006 that justifies any cuts in prospecting or reductions in customer circulation. Keep mailing, emailing, telephoning and searching.

Nation at a Glance

There have been several minor changes to the state-by-state circulation strategies, all increases in circulation pressure.

State	Mailings	State	Mailings
Alabama	Normal	Maryland	Increase
Alaska	Normal	Massachusetts	Increase
Arizona	Increase	Michigan	Normal
Arkansas	Normal	Michigan—Up. Pen.	Normal
California	Increase	Minnesota	Increase
Colorado	Increase	Mississippi—North	Evaluate locally
Connecticut	Increase	Mississippi—South	Evaluate locally
Connecticut-Fairfield	Increase	Missouri—North	Normal
Delaware	Increase	Missouri—South	Normal
District of Columbia	Normal	Montana	Normal
Florida	Increase	Nebraska	Increase
Georgia	Increase	Nevada	Increase
Hawaii	Normal	New Hampshire	Increase
Idaho	Increase	New Jersey—North	Increase
Illinois—North	Increase	New Jersey-South	Increase
Illinois—South	Increase	New Mexico—East	Normal
Indiana—North	Increase	New Mexico—West	Normal
Indiana—South	Increase	New York	Increase
Iowa	Increase	North Carolina	Increase
Kansas	Normal	North Dakota	Increase
Kentucky—East	Normal	Ohio	Increase
Kentucky—West	Normal	Oklahoma	Normal
Louisiana—North	Evaluate locally	Oregon	Increase
Louisiana—South	Evaluate locally	Pennsylvania—East	Increase
Maine	Normal	Pennsylvania—West	Increase

Puerto Rico	Normal	Virginia	Increase
Rhode Island	Increase	Washington	Increase
South Carolina	Increase	West Virginia—East	Normal
South Dakota	Increase	West Virginia—West	Normal
Tennessee—East	Normal	Wisconsin—North	Increase
Tennessee—West	Normal	Wisconsin—South	Increase
Texas	Increase	Wyoming	Increase
Utah	Normal		
Vermont	Increase		
Virgin Islands	Normal		

Ω

Exciting Advances in Print

A number of new and innovative ideas are creating even more savings and efficiencies—as well as higher response rates—in the world of printing

Digital Individualization

Having returned from the Vermont/New Hampshire Direct Marketing Conference in Manchester, Vermont, hosted by The Orvis Company, several fascinating printing advances were seen and are worthy of exploration.

A company in Portland, Maine, MPX, is a unique provider of a suite of printing and fulfillment services for direct marketers. The website is www.mpxonline.com. The person to speak with is Curtis Roberts, Manager of Business Development, (207) 774 6116 ext. 3323 or cell (207) 233 8729; email: croberts@mpxonline.com.

One of their fascinating print products has increased response rates significantly due to its extreme personalization. Here's how it works.

A giant post card shows the faces of twelve people on the front, similar to a high school yearbook. The person in the upper left photo is the recipient of the mailing and the variable address and personal information as well as an offer is aimed specifically at that person. People respond to their picture and their name, and this specialized mail piece takes full advantage of that reaction.

MPX is finding highly innovative ways of combining printing with marketing technology, as well as digital individualization. As the online and print worlds continue to converge, every opportunity to individualize and get down to the personalized message for one is essential and must be explored.

Imagine the impact of a catalog cover with a customer pictured on it, or a grandchild; and what level of response would you expect if you received an email with HTML that pictured you or showed you and your last product purchased together.

Take a look at the MPX website and explore their concepts. Ask whether they might have something that will increase awareness and response and be useful in your new customer acquisition, old customer reactivation or customer retention.

Lower Press Operating Costs and Mailing Costs

Here are the latest resounding innovations from our old friends at Quad/Graphics. First, they now can offer variable data for use in catalogs. Quad/Graphics can begin with a pre-printed personalized piece and build a complete catalog around that variable piece and then address and message the outside with specific information for that same person targeted in the variable core. This is Quad/Graphics' *SmartMatch*. This has enormous application potential for both business-to-business and business-to-consumer catalog enhancement.

Another innovation (and one Quad/Graphics and I first conceptualized over 20 years ago) is what I call RotoMail. If you think of going to a movie and coming in half way through then sitting through the replay and leaving when you reach the place where you came in, you will have the idea. Think of a gigantic revolving carrier-route sorting table, rotating in front of you with all the various carrier-routes passing by. You enter the 'pool' of addresses at some random carrier-route, say at 2 a.m., and begin inserting your catalogs into a giant co-mail with other mailers. When the whole sortation has revolved and you come to the carrier-route you first entered on, you are done at maybe 7 a.m. and you jump off. You've just RotoMailed. Quad/Graphics has built huge pools of customers and they can in-line/co-mail/co-bind and mix all of the pools' mailings in one giant carrier route. As you can imagine, the resulting postage savings could be enormous, and the marketing options for both small and large mailers are staggering.

But that was not enough for Quad. They have come up with a twist. In addition to the multiple catalogs co-binding and co-mailing on the same stitcher, they added their *MultiBlend* pocket in-line, after the trimmer. This allows them to deposit a pre-bound catalog of a *different* trim size and have it entered in the giant carrier route sortation, as well.

For significant cost-savings on press charges, Quad/Graphics is phasing out its 32 page presses and replacing them with 64 page presses. If you look at the primary costs in printing, labor (including benefits) is significant. Because of the economies of scale, one 64 page press can produce the output of three 32 page presses and it requires one-third the number of press operators, a 66 percent savings on labor. Again, creating innovation for customer benefit, Quad/Graphics has figured out how to position these 64 page presses as *facing*, meaning the two consoles for controlling the presses are side-by-side. This allows a six-person crew to operate two 64 page presses. That is a reduction from the thirty people it took to run three 32 page presses which were not facing. Over time, this level of productivity improvement will result in lower overall costs.

Quad/Graphics is doing exciting things, as they always have done. The person to talk with to find out how you can benefit from these innovations and cost-savings is Jim Rudek. Jim's email is Jim.Rudek@qg.com. His telephone number is (414) 566 2021 in the Sussex, Wisconsin office. I've known and worked with Jim and Quad/Graphics going back to the very early 1980s and I am constantly amazed by their creativity, vision, innovation, and unequalled dedication to their customers' success. There is still a print

production frontier to be gained and Quad/Graphics is consistently ahead of that frontier, pulling the catalog world into the future and finding ways to do it better at less cost. You need a company like that on your team. Ask the tough question: “What innovations have my printer created to lower my costs? Just exactly what have they done for me lately?”

The View

What’s Next?

You’re probably not going to like this. It is a complexity far more disturbing than the concepts of paid search, key words, ad words, or anything else you have had to grapple with in the last ten years. The Internet is going to shift from the PC to the TV.

Not only that, but the online channel will no longer be static; it will be dynamic and it will be in a video format. Web TV. Motion pictures. Talkies. Big screens and little screens (cell phones and Treos and Blackberries, oh my).

Intelligent life forms have drifted away from the inanity of television in general and the banality of reality shows. It just can’t get any dumber. Instead, increasing numbers of intelligent people (those who have all the money) are spending more time on online projects, research and interests. And that trend will grow over time.

The Internet is evolving and will continue to evolve into a visual media as well as a content media. Most information—most search—will have a video component, a movie if you will. But the real evolution will be the emergence of thousands of highly-specialized Internet “channels.” These will be like URLs or the old ‘website.’ And these chunks of special interest channel time and space will be bid on and paid for by merchants wanting to attract customers to their live-action, video platform.

You will bid on and pay for channel space and time in the same way you now bid on key words and ad positioning. If you have the highest bid for Internet ‘prime time’ in your narrow area of special interest you will be positioned at the top of the Web TV Guide. Let’s take the ancient art of gilding, as an example. Gilders use thin sheets of beaten gold to gild or decorate objects. It is a very obscure art and the supplies are not easily found. With the Gilding Channel of Web TV, a gold-leaf supplier will be able to educate new gilders, show advanced techniques to masters of the art and to sell gold- and silver-leaf and other supplies. If there are five suppliers for gilding products, they will compete in an auction for a piece of the web channel for the gilding shows. The supplier that spends the most gets a chunk of the best mega-channel (maybe Google WebTV) and the best time slot. Those who don’t spend, get 3 a.m. on SquatOnline.

Think of this as Internet online Direct Response TV, but hopefully with class. Okay, probably not. “Hi, I’m Billy Mays! I want you to buy my WonderBroom!”

Regardless of the intellectual quotient, the Internet and the online channel are absolutely morphing as you read this. Next year’s online channel strategy will be completely new and the old web page fundamentals and usability studies will be left in the dust, and you will be learning how to be a movie producer and how to create online screenplays that tell a consumer or a business story. All the metrics will be different and

it will involve an entirely new structure of cost and break-even. Getting a name and getting that name to your WebTV channel at a cost that you can afford is the name of the game.

Look at it from the transaction side. There will sit customers watching interesting programs that merchants have 'put up' on the channel. They will have remotes with a button labeled "Purchase." As the show unfolds and the content convinces them you are the right WebTV show to watch, they will push the button and a transaction will occur—seamlessly and instantly using all encrypted information requiring no shopping cart or information to be obtained. The WebTV channel host will get their cut, the airtime broker will get their cut, the channel search and auction firm will get a piece, and you will have arrived at a whole new reality of online marketing. Five years. Count on it.

Ω

The *Libey Economic Outlook* is published seven to eight times annually by MeritDirect. The information provided is published for information purposes only and does not constitute recommendations for investment or other financial activities. No guarantee of business performance is made or implied and readers are encouraged to seek adequate professional advice prior to making strategic and financial decisions or investments, or altering planned business activities. Copyright 2006 by Donald R. Libey. No reproduction or dissemination of this material by any means whatsoever, electronic or printed, is permitted without written consent of the author and publisher. Copyright infringements will be pursued to the full extent allowed by law. The *Libey Economic Outlook* is provided to clients of Libey Incorporated and its strategic partners and affiliates, MeritDirect, Amtower & Company, and SpyderHost, Inc.

Libey Incorporated *Consultants & Recruiters to Direct Marketing*

**811 Church Road Suite 105
Cherry Hill, New Jersey 08002
Tel: (877) 903-9448 Fax: (866) 221-8346**

**280 South 79th Street Suite 1401
West Des Moines, Iowa 50266
Tel: (515) 537 2307 (Don Libey's Direct Number)**

**E-mail: libey@libey.com
www.libey.com**