economy

PART 1:

Great growth, but for how long?

BY SUSAN GIBSON AND JASON STAHL

John Wheeler can forecast his landscape maintenance contracts through the year's end, but it's the design/build side that is harder to forecast. The president of Wheeler Landscaping Inc. in Chagrin Falls, OH, has a variety of design/build jobs lined up now but wonders how long that trend will last, especially if the economy "cools" as the experts say it will.

"We've budgeted an increase in our design/build work this year, but most of the work comes not that far in advance. We had a record month in April but will it hold out?" he asks.

That's the question on many people's minds as they juggle two conflicting trends: managing today's strong demand and dealing with uncertain prospects about next year's business. Economists tell us that the Federal Reserve's six interest rate hikes, the stock market's volatility and some rising prices in certain sectors are starting to have that "cooling" effect. The question is, how much and how long will it last?

Certain economic trends seem to point to a slight slowdown, but what will that mean for the landscape and lawn care industry? Currently, few industry professionals see any signs of a slowdown.

"It's not here yet," says Neil Thelen, president of Landmark Landscapes in Norcross, GA. "Landscape normally is at the back end of a slowdown. We could see something in about 12 months."

The next year isn't looking bad for Mike McCoy, president of McCoy Landscape Services in Marion, OH, who says the strong economy has made business easy. He reports that most of his contracts came unsolicited, boosting the firm over its previous goals.

Right now, the problem isn't so much a slowdown as it is managing the incredible growth this industry has seen during the last nine years. The profile of the Green Industry in 2000 is one of untapped opportunities for more business, labor shortages that continue to plague landscape managers and a host of new issues, regulations and market developments that may make life even more interesting in the next few years.

ERIC MULL PHOTOGRAPHY

Year in review:

Full steam ahead

Last year, landscape managers predicted an average of 15.5% growth for 1999. Our research this year (see "How we got this information," page 36) shows even more optimism, with expectations of a mean revenue increase of 18% for 2000.

Where are they getting this growth? Some landscapers and lawn care operators are expanding via franchises while others are opening up new branches, up-selling existing customers, finding new clients on the Internet and squeezing more profits through greater efficiencies.

Nevertheless, there are several factors that make life difficult today or hold the promise of having a major effect on tomorrow's business.

Down and dirty competition

Low-ball competition keeps maintenance prices (and profits) low, especially in the head-to-head residential markets. Few contractors voluntarily get into this price-war situation and several, in fact, are planning to boost their prices this year.

"We're shifting to a new pricing structure and are looking to grow

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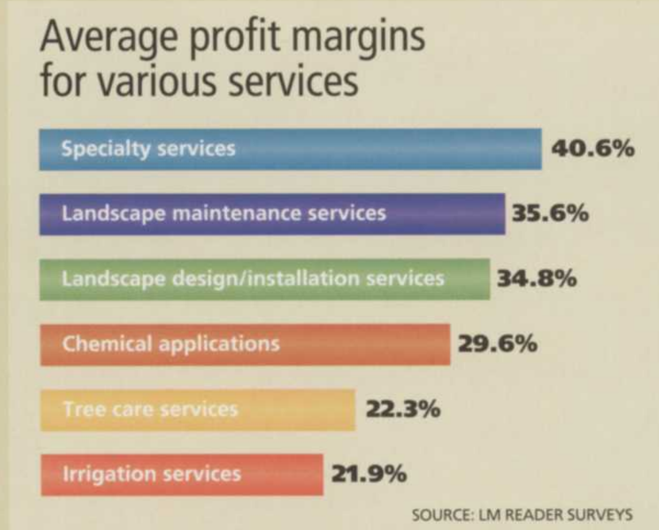

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through that, not through volume," says Jerry Gaeta, a partner with The Good Earth Inc., a full-service landscape firm in Mt. Pleasant, SC. The time seems right, he notes. "We have a backlog of work and enough people who want our services that they will wait two to three months."

Michael Hornung, president of Valley Green, a lawn care services firm in St. Cloud, MN, says that low-balling is nothing new. "We've had some low-balling in our market, but it seems someone is always going to do it. Some of those who used to low-ball finally raised their prices and their businesses are growing as well as ours."

Despite the competition, Hornung reports Valley Green's 30% to 40% average growth has caused him to finally set limits. "It has just been nuts and we've started to hold growth back. Actually, that's worked well because we can be on the customer's property more often and we're not working our people to the bone."


Chris Karcher finds "good" customers

While low prices are a valid option, too many landscapers price themselves out of the profit picture. And many of the prices are too low to encourage professionalism or growth of the industry as a whole, say some insiders.

"It's very competitive out there," says Chris Karcher, owner of a new NaturaLawn franchise in Shawnee, KS. "A lot of companies want to compete by offering low prices, but they're doing a disservice to the industry. Our challenge right now is targeting customers who are convinced that lawn care isn't about who is cheapest."

Tom Davis, president of Bozzuto Landscaping in Laurel, MD, agrees: "Competition is stronger and pricing is still tight. Personally, I hope the low-ballers get acquired soon."

"Low-balling used to be an issue for us," notes Billy Gray, vice president of The Southern Landscape Group in Pinehurst, NC. "But now that our reputation's out there, it no longer is an issue because people know we deliver high quality."

Gray says that while more new start-up companies have joined the market in the past year (mainly "guys with one truck and a lawn mower," he notes), the number of larger companies offering quality service has stayed the same.


Dwight Hughes: Interest is high

The firm's emphasis on quality lifts it out of the price-cutting muck and has another important benefit — attracting quality employees. "We are the employer of choice locally because we offer good pay and benefits," Gray reports.

Gary Nichols, owner of Twin Oaks Landscaping Inc., in Fairfax, VA, rarely comes in as the low bidder. He expects his $300,000 firm to increase revenues as much as 15% this year, but not by low-balling on landscape design/build. He won't bid on such work because "that's on a low-ball situation. There's a totally different profit margin involved there," he adds.

Dwight Hughes, president of Dwight Hughes Nursery, Cedar Rapids, IA, expects more competition to continue. "New competition is a national issue. There is a new interest in horticulture and more people in the community college programs. They'll keep entering the business."

Don't expect the debate on low-balling to go away. Like Hornung, many feel that pricing plays a major role in setting industry standards for success and an appearance of professionalism.

"Everyone is so focused on saving money on payroll, yet they're not charging enough to do the work," he says. "Plumbers are getting $100 per hour and we're still getting $30 to $40. That's why we can't find the employees we want. When we're getting a customer on price and not on service, we suffer for it."

Inflation & the hunt for profitability

Like other industries, many landscape operations undoubtedly found higher profits by reaching new levels of productivity, rather than through increases in prices.

While our economy has enjoyed an unprecedented run of stable prices, some prices are creeping up — health care costs, gasoline, water and wages. And some operations are starting to feel the pinch.

"I'm feeling significant cost pressures, especially in the areas of insurance (mainly health care costs) and gasoline," reports Neil Thelen. "I'm going to take a pricing action of a broad nature this year, which is something I haven't done for six years."

While Thelen considers his pricing options, some contractors like Jerry Gaeta have already decided to tack on a gasoline-hike surcharge.

"We're going to be moving our prices up because the cost of gasoline is moving so fast it's not giving us room to pass it along to our customers," he explains. "I'm on fixed maintenance contracts, but with 30 trucks running a week, I can't pass it along. We'll have to readjust all our equipment rates to cover it."

Jerry Gaeta says prices must rise.

The LM reader surveys report that 71.6% of our respondents plan to raise prices this year, with only 28.4% holding at current levels.

Profit margins also depend on growth and healthy revenues. According to the survey respondents, the most profitable services continue to fall to specialty work and landscape maintenance, with design/installation close behind.

Within those wide segments, of course, there is plenty of variation. Take the profit you can expect for a single plant sold to either residential or commercial customers, says Gaeta. "That $24 plant you sell to the residential customer will only get you $15 or $16 for a commercial landscape." That's one reason why his firm focuses on high-end residential landscapes.

Consolidation fallout keeps coming

The consolidation in both landscape and lawn care markets continues, as do mergers and acquisitions on the supply side. This causes uncertainty in local marketplaces, changes in the way landscape managers must operate and, sometimes, rational pricing!

Landscape contractors in several markets have commented on three developments relative to the consolidation of firms:

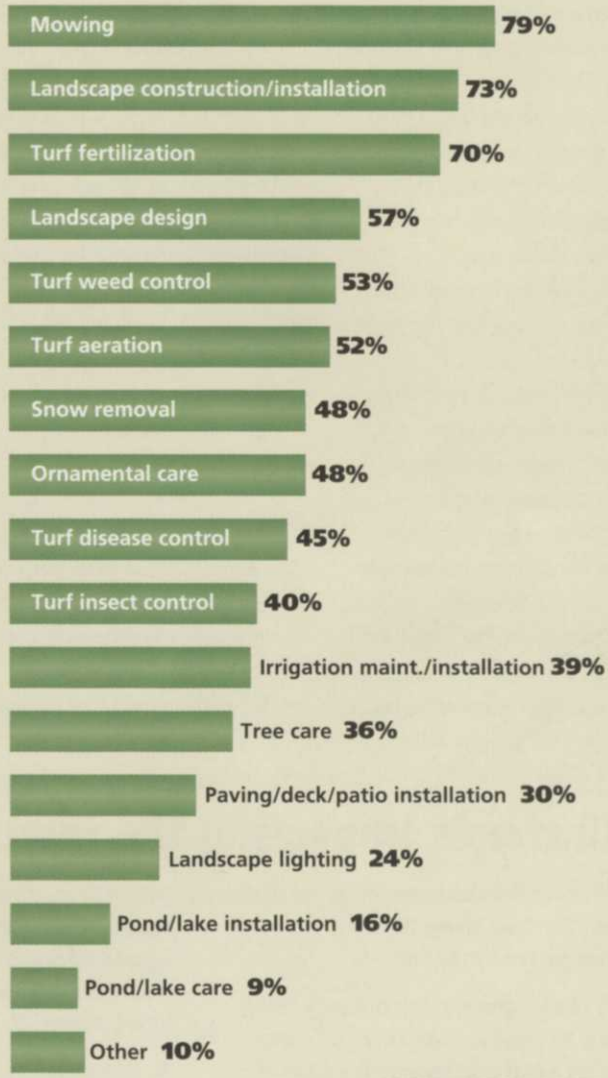
1. Some consolidated firms are backing away from their higher proportion of design/build work to concentrate on developing steady maintenance business;

2. Some consolidators are hard at work trying to systematize and standardize their diverse operations — a process that may yet take some time;

3. Some firms are "buying" business through low, unprofitable pricing (and denying they're doing it).

It may take some time before the consolidators develop the operations they want, but, in the meantime, several non-consolidators landscape companies are benefiting from the situation.

Most popular landscape services offered in 1999



SOURCE: LM READER SURVEYS

"The mergers in our marketplace have caused those firms to move on to the largest projects," explains Larry E. Brinkley, president of BLT Landscape Services, Dallas, TX. "That's left a void with the medium to small-sized jobs." This has been advantageous for BLT, which concentrates on medium-sized commercial and high-end residential work.

The shakeouts that are inevitable when competitors merge are also proving beneficial for landscape managers looking for experienced managers. Several commented on their good fortune to hire experienced people from consolidating firms.

While the nearest consolidated firm is 100 miles way from Mike McCoy's company in Marion, OH, they compete

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in the same market — Columbus. Since he hasn't gone head-to-head with the bigger firms on bid jobs, he has a rather charitable view of them. "It seems that consolidated companies are doing a great job," he says. "I think there will always be room for smaller companies, though."

Neil Thelen is waiting for the consolidated firms in Atlanta to make a serious play. "Our market is atypical — we have several top firms who have always been competitors, and now they're working hard to figure it out," he says. "With that many firms, you're going to have some confusion, but it will be a juggernaut when they eventually do figure it out."

He's watching closely. "It will be really interesting to see how this plays out. I think the consolidation will improve the professionalism of our business here in Atlanta, but everyone needs to be prepared for almost anything. You can't have too many prima donnas on the dance floor."

On the lawn care side, both Centex of Dallas and Weed Man of Mississauga, Ontario, are making active moves into the marketplace. Weed Man just announced revised plans to penetrate the United States lawn care market through a series of sub-franchise arrangements and has attracted several high-profile lawn care owners, while Centex is concentrating on acquisitions.

Supply chain changes

Supplier mergers and acquisitions are changing traditional distribution systems, the availability of certain products and many face-to-face relationships.

Just a few examples of the activity on the supplier side include: the BASF/American Cyanamid deal; the merger of Novartis and Zeneca into Syngenta; The Andersons' and Nu-Gro's combined purchase of the professional turf business from The Scotts Co.; John Deere's new emphasis on moving its dealers into after-sale services; Turfco's direct sales program; Ferris Industries' purchase by Simplicity; the launch of several e-commerce sites focusing on the landscape industry; and AgriBioTech's bankruptcy.

All of these are expected to impact the normal buying and distribution systems, but time will tell if those impacts are positive or negative. Most likely, here's what you'll find:

▶ New names, new faces and new ways of buying. As suppliers merge or tweak existing distribution chains, some will cut staff, reassign territories or "streamline" the buying process.

▶ Less products and potential limitations on developmental research. Some crossover prod-

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10 trends impacting the industry

Whether the economy continues to expand or slow, these 10 trends won't change. Here they are:

1. "Easy" growth – It's not only fairly easy to grow an operation, it's sometimes a real challenge to limit growth. Survey respondents named landscape design/installation the fastest growing segment, followed by maintenance.

2. Uncertainty about the future – Is the economy cooling? Will it affect construction, disposable income for consumers and commercial maintenance budgets? It's hard to prepare for this.

3. Consolidators are getting it together – While the rate of consolidation has slowed, the consolidated companies are starting to standardize operations and bring on some real competition.

4. New, tougher competition – New competitors enter this market constantly, making competition tough and squeezing prices, particularly in the maintenance side of the business. This won't stop.

5. Demanding customers – Blame it on instant messaging if you like, but today's residential and commercial customers are much more fussy and pushy about getting "extras" in a deal. And they want it now!

6. Ouch! Lack of labor hurts – Labor shortages are a fact of life and there is no solution on the horizon. Some organizations make the most of the situation with good management, benefits and mechanization.

7. Regulations with bite – Key issues challenge landscapers around the country, including: availability and use of pesticides; blower noise and engine exhausts; ozone-alert restrictions; control of irrigation installation; and water restrictions.

8. Diversity in services and customers – Innovative contractors and LCOs are expanding into new areas, franchising new services and seeking employees from new sources.

9. Supply chain blues – Manufacturers are merging at a dizzying rate, the ABT seed consolidation's fallout has yet to fall out and dealer/distributor chains continue to confuse and frustrate industry professionals. This will continue as long as mergers and acquisitions are profitable.

10. High-tech goes "green" – Laptops, palm devices, digital photography, new software and the Web continue to attract the attention of tech-savvy landscape managers. But how many are mechanizing for better productivity?

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ucts may not be economically feasible for production anymore, so expect to try new ones. Others may have to be spun off if they compete within a merged organization.

▶ Expect some rocky transactions if you've always worked with the same suppliers and supply chains. New people and systems mean a new learning curve for everyone.

▶ E-commerce sites promise much but it will take some time to see how well they deliver. Some have the potential to influence pricing/delivery both positively and negatively.

Winning the retention game

How landscape managers keep their employees

Incentives/bonuses	67.4%
Uniforms	52.2%
Retirement savings plans	38.0%
Promotions	31.5%
Transportation	28.3%
Recognition programs	23.9%
Education reimbursement	21.7%
Profit-sharing plans	19.6%
Health care programs	9.8%

SOURCE: LM READER SURVEYS

In-your-face regulations

Moves to regulate landscape operations at both local and national levels are becoming more visible and aggressive, especially in certain markets. Last month's loss of Dursban is a prime example (see story on page 16). Massachusett's strict regulation of pesticide use on public properties is another major development.

The Dursban move was not a surprise; rather, it was the speed of the decision that hit the industry so hard. Several landscape managers say they saw it coming and had made their plans accordingly.

Michael Kowalchuk, former owner of Gro-Control Inc., Westland, MI, stopped using it six years ago because of a state law requiring him to put a warning plaque on his truck. He's spent enough time in the industry to know that pesticide regulation will ultimately affect business, despite the emergence of alternative products.

"People want results if they're paying for a service," he says. "They're pretty impatient. If you can't deliver because you don't have the tools to do the job, your market will definitely be affected."

Many landscapers are dealing with restrictions brought on by drought or overbuilding, and they have had to defend the use of water for landscaping.

"We're down 20 inches below normal for the last 18 months and may be looking at severe restrictions or bans," reports Neil Thelen. "Malta (Metro Atlanta Landscape and Turf Association) has been speaking up for water rights in our area."

Larry Brinkley reports an informal coalition of landscape managers in the Dallas area has organized to discuss water issues and develop information for use in public debates. Thanks to the information, many of the restrictions were limited, he says. "They backed off on it."

He also reports talk of restrictions on the use of backhoes, mowers, fork lifts and other equipment during Dallas' many ozone alert days. "They're talking about limiting use until after 10 a.m.," he says, noting that those rules create new logistical problems for his managers.

Larry Brinkley says water is a big issue.

Regulators in Illinois and Minnesota have been stepping up pressure to make sure that installation of irrigation lines is limited to plumbers or electricians. For someone like Michael Hornung, who has seen his irrigation business double in each of the past three years, Minnesota's move is a threat. "This is going to hit me directly," he says.

The controversy about blower noise continues to bedevil landscapers in some areas of the country, especially California.

Wayne Richards, COO of Cagwin & Dorward, Novato, CA, explains, "The banning of blower use in cities is a big concern. Even though suppliers and contractors actively try to educate the public about the value of blowers, this is a purely emotional issue spearheaded by residents who are not concerned about the economic impact resulting from the bans. The California Landscape Contractors' Association is actively soliciting political support to arrive at compromises."

"Government regulations on the H2B program have had a negative effect, with increases in the prevailing wage rates," says Ronald Schmoyer, president of OneSource Landscape & Golf Services, Tampa, FL. He also cited EPA regulations and Florida restrictions on water use as serious issues.

'Spoiled' customers?

Aren't you a more discriminating customer with your purchases these days? Maybe it's logical to expect your clients, both residential and commercial, to be pickier. But how picky is okay? Some landscapers complained that unrealistic expectations, burdensome communication schedules and requests for "extras" are driving them crazy.

"My number one challenge is dealing with people," says Dwight Hughes. "They want immediate communications. If you don't call them back the same day they call, they'll be calling you back again."

It's not an issue of customers as much as managing their expectations, Hughes explains. "I have the greatest cus-

> "You have to be flexible and give customers all they want and more. But we've been training them to expect it — now it comes back to bite us."
>
> — *Michael Hornung*

tomers in the world, but they all want it now. I had a customer call me three times and all she wanted was for us to take out one plant. Then, a new fast-food restaurant here gave me six days' notice to schedule and get their entire landscape placed."

Michael Hornung agrees. "You have to be flexible and give customers all they want and more. But we've been training them to expect it — now it comes back to bite us.

"Seven years ago, less than 1% of our customers wanted us to call before visiting. Now, 8% do," he notes. "We treated one lawn all year and then found bugs in the trees. The owner expected that he wouldn't have to pay for the extra tree treatment. He cancelled on us."

Jerry Gaeta sees it as a continuing trend. "Yes, customers are getting to be fussy, but that's how they are. Many of them are wealthy and want something extra. People everywhere are more demanding."

Snapshot 2000: Overview of an industry

Individual stories of growth range from 20% below 1998's levels to more than 100% growth in the last 12 months. How do they get these levels? Respondents to LM's State of the Industry survey showed the usual wide range of services offered in 1999 (see chart below). More than half of the respondents named at least six of these services in their mix.

Rising revenues

The optimism continues, with 69.4% of respondents reporting they expect an increase in revenue for the next 12 months and only 27% expecting revenues to stay put. Merely 3.6% of them expect a decline in sales.

The average landscape contractor's approximate revenues for 1999 were $1.22 million, compared to the average lawn care company's revenues of $322,000.

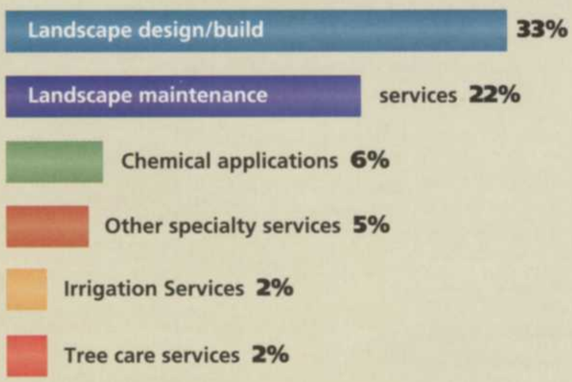
Current customer mix on average is 59.2% residential, 37.2% commercial and industrial and 3.7% other.

"We're seeing high demand for services in installation, maintenance, irrigation, tree care and environmental restoration," reports Wayne Richards.

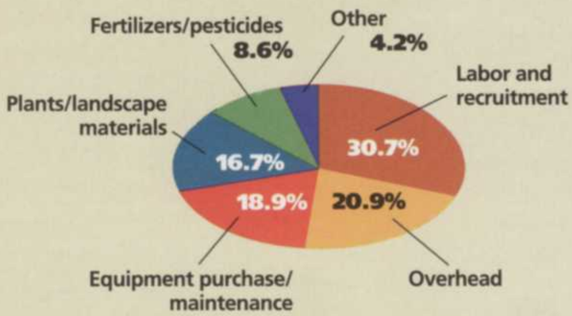
Hornung sees other areas of growth. "Irrigation has really taken off with virtually no advertising," he says. "And after marketing (a year-round lighting franchise) one week, we've picked up $35,000 in revenues."

Fastest growing service segments

(percent chosen as fastest growing business segment):



Typical '99 annual operating budget



Operating lean, mean and green

How can you be lean and mean without a clear picture of your operating budget? Readers in our survey knew their budgets inside and out, and had an average operating budget of $495,000. This breaks down to an average budget for grounds management of $1.34 million; landscape contracting $518,000; and lawn care company $240,000.

Our survey's respondents had several challenges this year. The average rankings show that 72.6% listed labor availability as their number one challenge, followed closely by developing good field supervisors/fore-

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