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Dear FAS Customer,

This year has been a challenging year for retailers, including florists. As the end of the year approaches, one would like to be hopeful that the new year will bring opportunities for sales growth and improved profitability. However, recent announcements by one of the industry's largest companies suggest that retail florists may not see their jobs become any easier in 2005.

When Teleflora bought AFS about four years ago, the presidents of the respective companies conducted interviews with several industry publications. In an interview published in the January, 2001, issue of SAF's *Floral Management* the top executives of the two companies were questioned about supporting order gatherers, i.e. companies that collect orders that are subsequently transmitted to "real florists" for fulfillment. Coincidentally, one of the owners of AFS at that time was actually one of the largest order gatherers in the United States. After pondering the definition of "order gatherer" and questioning whether order gatherers actually had a negative impact on retail florists, one of the "new Teleflora" executives stated, "Our philosophy says that we don't direct the consumer to a florist dot-com. ... The only thing Teleflora can control is that we are not going to compete with our florists. ... But with Teleflora, you're never going to see an 800 number, you're not going to see a dot-com." In the January, 2001, issue of *Florists' Review* another of Teleflora's senior executives discussed Teleflora's marketing program saying, "These campaigns will direct new customers to our florists' shops--not to us. There will be no national 800 number or dot-com address in any of the new Teleflora's ads, print or television. We don't believe in competing against our members--just supporting them." These comments were obvious jabs thrown at FTD for FTD's consumer-direct activities conducted through www.ftd.com. Similarly, you may have been told repeatedly by Teleflora's representatives that Teleflora didn't compete against its members like "that other wire service". Many long-time FTD members did, in fact, terminate their relationships with FTD when FTD began its consumer-direct competition against member shops.

On November 6, 2004, Teleflora reversed its we-will-not-compete-against-our-members stance. In a letter to its members Teleflora stated that www.teleflora.com was being converted into a consumer-direct site. When consumers place orders through teleflora.com, Teleflora processes the orders and sends the orders to retail florists for fulfillment. Teleflora points out in the letter that it will be paying florists 80% of the order amount for filling these orders and that Teleflora "uses a retail florist for every purchase", apparently in an attempt to distinguish itself from FTD's 73% compensation and direct-ship programs. Consumers can also place their orders by calling 800-TELEFLORA. Teleflora had actually begun its order gathering operations long before making this change to www.teleflora.com. Several years ago Teleflora purchased Flower Club from Gerald Stevens, although Flower Club didn't promote its affiliation with Teleflora. The Flower Club used its web site www.flowerclub.com and phone number, 800-800-SEND, along with direct mail to generate consumer orders. For years some of Teleflora's most loyal supporters continued to naively state that Teleflora bought this company to "shut it down". Not only was Flower Club never shut down, but its web site was recently updated to say "*Teleflora's* Flower Club", now clearly indicating the affiliation of Teleflora with Flower Club.

In the magazine articles Teleflora's executives repeatedly suggested that the merger would result in lower wire service costs for member florists. As with the we-won't-compete pledge however, florists have found that the opposite has occurred, as fees have skyrocketed since the merger. In fact, the developments discussed above, designed to "help (Teleflora's) members", were accompanied by other holiday greetings. Teleflora also announced that it is creating a new $20 monthly fee to fund Teleflora's Quality Program and that Teleflora will increase the Dove handling fee and order processing fee by $0.25 per order, to $1 per order. Then on the heels of these announcements, Teleflora broadcast a Dove message stating that Teleflora was introducing a new line of 11 bouquets priced between $29.95 and $34.95. One could reasonably summarize these developments by stating that Teleflora announced it was beginning to compete against its members with its consumer-direct web site, raising its fees substantially, and significantly lowering the prices of many of the items its member shops will be receiving--something FTD did over several years--all within the span of about a week!

These changes at Teleflora will certainly cause shock waves that will be felt throughout the industry. The Quality Program alone will cost retail florists over $5.5 million a year, based on Teleflora's published membership. Retail florists simply don't have another $5.5 million to give up. The Dove fee increase will also create a new financial burden for florists. In January, 2001, Teleflora represented that it processed about 20 million orders a year. If half of those orders were to be transmitted over Dove, that extra quarter an order, though it doesn't sound like much, would take another $2.5 million out of florists' pockets.

Although these changes represent tremendous increases in actual costs to florists, the greater damage will occur as florists lose even more orders to order gatherers. In the "old days", before the explosion in the growth of order gatherers, all orders were exchanged between "real" flower shops. Industry averages showed that a shop could keep its labor costs at about 30% of gross sales, cost of goods sold at about 30% of gross sales, and operating expenses at about 35% of gross sales, generating a net profit of about 5%. Florists could pay all their bills on time, pay themselves and their employees a decent salary, and still build equity in their businesses. Then, order gatherers began to turn this model on its head. When retail florists lose 10% of their business to order gatherers, they lose approximately 30% of that 10% in gross revenue to sending commissions and clearinghouse fees, and their net profit drops to 2%. As florists lose 20% of their sales to order gatherers, the net profit becomes a net *loss* of about 1%. When order gatherers capture 30% of florists' sales, the net loss is about 4% of gross sales. Using the same cost allocation described above, if florists were to ever lose 100% of their sales to order gatherers, i.e. about 30% of their compensation, florists would experience net losses of about 25% of gross sales! As unlikely as this last scenario may seem today, it clearly illustrates the negative impact florists feel as they continue to lose marketshare to order gatherers. Could this be why so many shop owners say they are filling as many orders as ever but finding it harder than ever to make a profit? Many shops have incurred several years of losses, eroding the equity they had built in their businesses.

This environment was brought about by a wire service industry that made it very attractive for businesses to collect orders and forward the orders to real florists for fulfillment. When an order gatherer sells a $50 arrangement, they make a $10 sending commission (20% of $50), they typically charge a "service fee" of about $10, and the wire service that processes the order will pay the order gatherer a rebate of $5 or more. So, for a few minutes on the phone, or perhaps with no labor at all in the case of orders being collected over the Internet, the gatherer can generate net revenue of $25 on the order. On the other hand, a florist receives only $36.50 (73% of $50) for filling that $50 order. A shop with a COGS of 30%, or $15.00 of the $50 order, would receive less than the order gatherer ($21.50 vs. $25) for processing the order, and remember, the flower shop has still got to pay the designer, driver, and operating expenses. Most retail florists don't consider this a fair distribution of compensation. To look at this from another perspective, suppose one of your local competitors decided he needed to make some changes because he was having a tough time financially. He got a great idea. He fired his designers and drivers. He sold his delivery vans and eliminated the costs associated with those vans, including gasoline, maintenance, insurance, etc. He even stopped buying flowers. The guy still has to get his orders placed though, so he decides to wire the orders to your shop located just down the road from his. Would you take your competitor's orders at a 30% discount so that he could drastically improve *his* profitability? Would you *pay* him to send the orders to you at a 30% discount? I think most shops would answer "no" to both questions, yet this is exactly what tens of thousands of florists do when they fill orders collected by order gatherers. I think many florists view these orders in much the same way they view a "normal" incoming wire order saying, "Well, this is an order I wouldn't have gotten any way", but this simply isn't the case. Order gatherers aren't just collecting orders that consumers need wired to distant cities. In many cases, customers in your city use an order gatherer that takes the order and wires the order to a florist in your city for delivery to a recipient also located in your city. The wire services and order gatherers are effectively turning these entirely local orders into discounted incoming wire orders for your shop.

One of the newer business models florists are being forced to compete with involves products that are direct-shipped to the recipient without any involvement of retail florists. FTD offers many of these products, including floral arrangements, on its consumer web site. Another company, ProFlowers, has built its business by telling the consumer that its direct-shipped arrangements are far superior to the flowers bought from a retail florist. ProFlowers' web site illustrates a distribution channel used by traditional florists in which it takes 8-12 days for flowers to make it from the farm to the importer, to the wholesaler, to the florist. In contrast, their flowers go direct from "the field" to the consumer in only 1-3 days. ProFlowers' web site states, "While other flowers are traveling and aging, our flowers have arrived fresh from the fields and will stay fresh for 7 days." In February, their site stated, "Orders arrive via FedEx 5-9 days fresher than traditional floral networks and with morning dew still clinging to their petals. ... To date, over 2 million people have already received flowers that are twice as fresh at about half the price."

Your first reaction to seeing your products unfairly compared by a competitor might be one of frustration. You might say, "Well, at least we own the same-day delivery segment of the market." You would be wrong. The same site that disparages the products you make a living selling includes an option for "Same Day Delivery". Incredibly, ProFlowers sells the very products it criticizes in other sections of its site. These orders though, are wired to retail florists through one of the florists' "partners" for same-day delivery. Even more incredible is the fact that florists themselves provide this capability to a company that degrades florists' business practices and products.

FTD and Teleflora have created a monster. In order to maximize revenues they are attempting to recruit every florist under the sun to pay ever-increasing dues and fees. However, to satisfy shops' insatiable desire for more incoming orders, the wire services have entered into relationships with companies who are competing against florists, and they both are competing directly against their member shops with their own order gathering businesses. However, as the membership grows and as more shops install wire service technology, the order volume is divided among more and more shops, each of which receives a thinner slice of the pie, forcing the wire services to search for even more order volume. There appears to be no escape for the wire services from this vicious cycle, and this seems to be at least part of the reason that FTD and Teleflora have created their own order gathering operations. Generating their own orders also allows the wire services to exercise more control over the distribution of those orders. For example, by generating its own orders a wire service can implement an effective collections program by dumping orders on shops that have past-due accounts. These shops often happily fill these orders, apparently unaware, until later, that they have been “working off” their account balances.

The overall floral industry will undoubtedly continue to grow and prosper. If the current trends continue though, independent retail florists could be facing a rough future. Ironically, with the exception of the still relatively small direct-ship segment of the industry, florists can control their own destiny. After all, most of the order gatherers still depend on a local florist to produce and deliver their products. Retail florists are at a crossroads--at least the ones who have not yet closed their doors and walked away. You must ask yourself how long you will facilitate the operations of those that are competing against you for your customers and orders. How long will florists pay those companies and support those companies through the purchase of technology, floral products, and services? How long will you fill orders for companies whose businesses are marketed primarily by disparaging the products and services you sell to make a living? What percentage of your sales are you willing to allow to be intercepted by an order gatherer and sent back to you at huge discounts?

Florists must get together to address developments that are threatening their livelihood. Yet so many seem so unwilling to take action to protect their own interests. Understandably, some florists are frightened by the uncertainty that “doing something” could create, but the undesirable and certain results of doing nothing should be far more frightening. Other shop owners place a strange sense of loyalty to their competitors ahead of loyalty to their own businesses, employees, and families. I have personally witnessed shops turn down a Florist Direct order--an order from a fellow florist for which they would receive more compensation and be paid immediately by credit card--and request that the order be sent so that their competitor can take 7% of the order from them and pay them a month later. This seems to defy logic.

Change in this industry is inevitable. Some florists may believe that the industry is too large and too fragmented to coordinate any effort to influence and control the change that is sure to occur. However, FTD was begun by just a handful of florists in 1910, when the “T” in FTD was an abbreviation for “Telegraph”. Technology allows florists to be better connected today than at any time in history. Floral news literally travels from coast to coast in minutes as information is passed along via phone, fax, email, and Internet message boards. For example, you can read what your fellow florists think about these latest developments by reading the florist message board at www.floristboard.com. Florists who attend state, regional, or national meetings are able to network with other florists from all across the United States. And FAS users, fortunately, have options not available to shops that utilize wire service technology. Your FAS system allows you to process wire orders through the Independent Florists’ Association (IFA) and through FloralSource International. With these latest events, I think it’s no longer a question of “Will florists do anything?”, but rather a question of “*When* will something be done and *who* is going to do it?” What will you do?

If you have any questions about the issues discussed above, please call FAS at (800) 830-6160. We look forward to hearing from you soon. Thanks.

Yours truly

Gary M Reed

Gary M. Reed
President