

Traditional Case 3: Michael Petrow

Smart Rosenberg, Dowling College

Natasha Petrow could see the look of concern in the eyes of her husband, Michael, as the two of them prepared to leave their Levittown, New York, home on a Saturday morning in May 2006, to take the thirty-minute drive to New Age Laundromat, in College Point, New York. One of them would take this drive daily, ostensibly to pick up cash that had been collected by the attendants at the laundromat in the prior twenty-four hours, but also to have some face time with the attendant as well as the customers. Since this was a Saturday, however, and both of them were on their day off from their regular jobs, Michael as a safety inspector for the Metropolitan Transit Authority and Natasha as a freelance consultant in the computer industry, they took advantage of the opportunity to drive in together from College Point; they would swing past Clean-Rite Laundromat, in Glen Cove, New York, to also pick up cash and to check in on business.

As Michael started the engine of his recently purchased white Lincoln Continental, clear that he had always equated with success, Natasha turned toward him and gently placed her left hand on the steering wheel. "Misha," she asked affectionately, "why do you always worry about the business so much?"

Michael, a small, restless man with an irrepressible laugh, shook his head emphatically. "Natasha, I am happy with New Age's growth. I am happy with the location. The laundromat has fit in well with the local community." He sighed deeply. "I am concerned about Clean-Rite."

Michael purchased Clean-Rite in August 2001. He and Natasha had decided a few years earlier that even though they both worked long hours in their full-time jobs, they would make an investment in a business as means to generate a cash flow and an additional source of income for their family. After researching different types of business investments, they decided to refinance the mortgage on their house to enable them to purchase the laundromat in Glen Cove, on the north shore of Long Island, about twenty minutes from Levittown.

Clean-Rite did well from the start, with sales climbing each week, as a result of strategies they

developed that had not been offered by the prior owner and given the growth of the business in Glen Cove, Michael and Natasha decided to expand, and they sought a second location for a laundromat, which they ultimately found in College Point, in the borough of Queens, in New York City. Unlike the business in Glen Cove, which was previously a laundromat, the store in College Point had been vacant. After Michael refinanced his house a second time, as well as using the equity from Clean-Rite, to obtain the capital necessary to make the investment in the new business, New Age Laundromat opened its doors in April 2005.

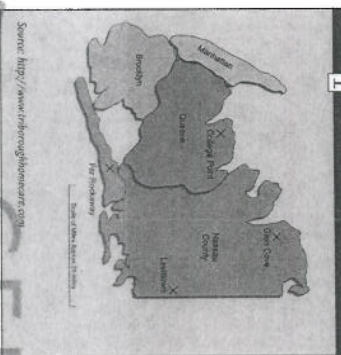
"Misha," said Natasha, several minutes later, at about the time that the relative tranquility of Long Island had transformed to the hustle and flow of College Point, Queens. "We have worked hard to build up two businesses. They are different, but they are both good."

Michael smiled at his wife nervously. "That's true, Natasha. What troubles me, though, is that I don't know how much more we can get out of Clean-Rite. The business grew well the first year, showed. Maybe the life of these businesses is only five years. You take what you can, and you move on to a new location."

"I don't agree with you," Natasha chided. "Both laundromats bring in income. If one is an important part of both communities. We have loyal customers. We have done well. We have talked about making this more than a part-time thing. We are now considering a third location—East Rockaway—and we know it's not easy driving back and forth every day. (See Figure 1 for a map of the locations of the laundromats.) But if we continue to expand, we do have options. We can take on a partner."

"It is a family business," Michael said emphatically still shaking his head. Since they both had full-time jobs, their responsibilities as it applied to the business were divided evenly between them. Accordingly, it was decided that Natasha was responsible for human resource matters and Michael was responsible for technical resource matters.

FIGURE 1 Queens and Long Island, New York



As the car pulled into a space on College Point Boulevard a half a block from New Age Laundromat, Natasha put her hand on her husband's shoulder and smiled at him warmly. "Misha, we have worked very hard and I am very proud of what we have accomplished. Never forget that it wasn't so long ago that we came to this country with nothing."

Family History

Michael Petrow, age forty-seven, had immigrated to the United States fifteen years earlier from the Ukraine. His home was the industrial city, Zaporozhye, not far from Kiev and Chernobyl. His sole purpose for coming to America was for the opportunity to build a career.

Michael left the Ukraine during Perestroika, the period that began in June 1987 when Mikhail Gorbachev, the leader of the Soviet Union, introduced the economic restructuring of the Soviet economy. Although reforms were established, the economy worsened and the quality of life deteriorated, leading to the eventual destruction of the Soviet Union in December 1991. On the day that Michael was to fly to the United States from Moscow, the city was in chaos. The army had positioned tanks in the streets and Michael was

relieved that the military allowed his flight to leave. Following the dissolution of the Soviet Union, the Ukraine became one of fifteen independent republics faced with the challenge of rebuilding its economy. Michael has never returned.

Having received his formal training as a teacher in the Ukraine, Michael realized that he would need to start over in the United States. He only had a tourist visa, so he applied to the government for political asylum. He was denied, as he was told that the Ukraine needed to hold on to people with his level of education. One week prior to his deportation, however, he won a green card in the Department of State's annual lottery. He would become a U.S. citizen within four years.

When he arrived in New York, Michael came with \$200 in his pocket. He lived in basements of houses and he worked seven days a week. He washed dishes in restaurants, pumped gas, worked in a food shop, and saved his money. He learned English and he studied engineering and business.

In 1982, Michael met Natasha, who had recently emigrated from southern Russia, near Chechnya. Natasha had received formal training as a pediatrician, but with her strong background in chemistry and mathematics, she decided to become a computer analyst in the United States. After a brief courtship, they married. In 1985, they took out a \$90,000 mortgage and, together with their savings, they bought their home in Levittown at a price of \$138,000. Shortly thereafter, Michael sent for his parents, who were happy to move to the United States to live with their son and daughter-in-law.

Michael was very driven. He had wanted to evolve into something better than what his parents had achieved in the Ukraine. He was pleased to have his U.S. citizenship and he was clearly bothered when people would dismiss all immigrants as second class and undervaluing of the opportunities of living in the United States.

I do not like that the illegal immigrants who have been coming here from Mexico and some other countries are permitted to stay without recourse. While I understand that they satisfy a need for cheap labor in the US, there are too many problems with social welfare. These people are living off of other people who pay taxes. We certainly can't deport them. These

people are largely good people, but they need to learn English, they need to become legal citizens, and they need to pay their fair share of taxes. Otherwise, things are not equal. I too am an immigrant. I too have worked hard. But I am paying taxes that help to send these people's children to school and to provide them with medical care. These other immigrants need to assimilate into American culture, just as I did. The U.S. government is doing a disservice to these people in the long run. The country will suffer from segregation not only based on income differences, but also based on cultural differences. The government needs to formulate a plan to deal with the problems of immigration. And these people need to be motivated, and not to be content with what they have. Look at me...I am an American capitalist!

Michael was reaping the benefits of the American dream. From a personal and a financial perspective, he was living relatively comfortably.

He often remarked to Natasha, "I resent it when people fail to recognize the personal struggles and sacrifices that we've made in our lives. It has not been easy."

Clean-Rite Laundromat, Inc.

Michael and Natasha researched different types of service businesses to invest in before deciding that a laundromat would be the safest venture. They reasoned that they would need to minimize their risk since they had never run a business before. They determined that a laundromat would generate a slow but sure return on investment. Michael believed that if they didn't make too many mistakes, their investment would work for them.

They had narrowed the choice down between a laundromat and a restaurant. Michael ultimately concluded that when people are pinched financially they would cut back on eating away from home. Conversely, he believed that people needed to do their laundry regularly. A laundromat, he reasoned, would not be subject to economic fluctuations.

Once they zeroed in on the type of service business, they needed to find a laundromat that was affordable. During the second half of 2000 and the first half of 2001, they took several road trips with David, a professional broker in the sale and resale of laundromats, who had been introduced to Michael by one of his MTA coworkers named Luis. In each of the neighborhoods that they visited, the three areas of focus were (1) the percentage of renters, (2) the level of competition, and (3) the incidence of crime. An unfavorable finding for any of these three factors were deemed to be dealbreakers, but perhaps most important was that the demographics of the neighborhood needed to show a high percentage of renters. They found this to be the case in Glen Cove, a community that with its strong Hispanic population seemed to indicate to Michael that the renters would consist largely of families with a lot of children.

The preexisting laundromat in Glen Cove that Michael purchased and renamed Clean-Rite had 600 square feet of space. It had sixteen washers and fourteen dryers. At the time of purchase, the laundromat had been operational for nine years. (See Figure 2 for a photo of Clean-Rite Laundromat.)

The laundromat pitcher was on the border with the next town, Great Neck, but virtually no direct or new competitors. The reason for this was that Great Neck is a community that was affordable to mostly households on the upper end of the economic scale, prohibited sewer systems. Without

FIGURE 2 Clean-Rite Laundromat, Inc.



access to a sewer, any new laundromat in this area would need to invest \$500,000 in a water treatment system.

Given the low level of competition and the location's close proximity to his home, Michael was eager to make use of his equity, and he used his house as collateral so that he could purchase the business for \$125,000.² He and Natasha both possessed a powerful motivation to learn how to run a business, and this was their opportunity.

After introducing the drop-off service in Glen Cove, the business really took off. Clean-Rite was embraced by the community, as word spread among local residents about this useful service, and sales revenue grew by more than 20 percent in the first year. Michael and Natasha were excited about their business venture, and after a couple of years, they decided to seek out a second location.

New Age Laundromat Inc.

For the second location, they wanted the opportunity to build the business from scratch. This would involve a different process altogether, where they wouldn't see a return on their investment for a longer period of time. They could take the chance of spending money without getting anything back in the near term, however, because there was now a steady flow of income from the first business. They borrowed \$400,000 to start up the second business, once again placing their investments (i.e., the equity in their home and first business) at risk in the event that the new business would fail.

Following a lengthy search of much of the New York metropolitan area,³ the location that Michael ultimately identified for the new laundromat was on the main commercial thoroughfare in College Point, Queens. Michael selected a middle-class neighborhood, populated mainly by renters who did not have access to washing machines and dryers in their homes. "The location must be in a solid working class community," was his mantra.

The different neighborhoods throughout New York City had varying levels of crime, and although the previous tenant, a furniture store, had at least six different owners and some encounters with the police, Michael concluded that the neighborhood was relatively safe and free of gangs. He would say to Natasha, "I want to help improve the quality of

life for the residents of this community, and I want to provide a clean and safe service that would be a source for jobs in the neighborhood."

To further protect his customers, Michael purchased a video surveillance system for \$2,000. With this system, Michael was able to monitor the store not only from a computer in the office that he set up downstairs at the laundromat, but also from his home computer. He reasoned that from a psychological standpoint, his attendant would feel safer knowing that the boss was watching. Michael put up signs in the laundromat that indicated there was a surveillance system in effect. This made the customers feel safer, too, he felt. New York State law prevented him from installing a microphone as part of the surveillance system, for privacy reasons. He justified the investment to Natasha, "Besides location, I want to emphasize safety, and having the camera deterrence any laundromat from others."

Michael established the same hours of operation as New Age as he had at Clean-Rite. The laundromat would be open from 7:30 a.m. until 7 p.m., Monday through Friday, and from 6 a.m. until 11 p.m. on Saturday and Sunday.

New Age had 1,600 square feet of space. The construction of the laundromat, which included all the plumbing and electrical requirements, represented a cost of \$150,000. The period of time that elapsed prior to the start of the actual construction seemed rather long to Michael, as he learned that he needed to wait for the necessary permits from the New York City Department of Buildings and from the utility, Consolidated Edison. This waiting period in connection with the construction was six months. The physical construction of the laundromat, on the other hand, took only two months.

"In retrospect," Michael acknowledged, "the construction process might have moved more smoothly had we hired an attorney." However, in the interest of cutting his expenses, he went through this process only with his general contractor. Together, they took advantage of a service that had recently been instituted by Mayor Bloomberg known as 311, whereby individuals dial in and are given access to information, and guided through the red tape of dealing with various city agencies. "By dealing with the city without an attorney, I figure that we saved

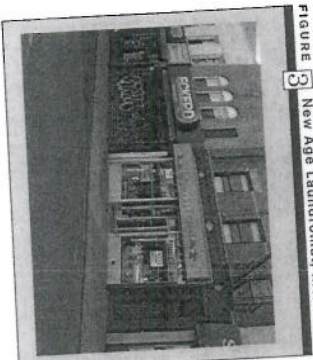


Figure 5 New Age Laundromat, Inc.

approximately \$25,000 in legal expenses." (See Figure 3 for a photo of New Age Laundromat.) Michael decided to have fifty-five machines installed in the new laundromat, twenty-seven washers and twenty-eight dryers. The cost of this equipment, all of which was manufactured by Dexter, was \$250,000. Michael financed the construction along with the cost of this equipment with the \$400,000 loan from his bank.⁴

Additional equipment other than washers and dryers was installed in the new laundromat, as well. These machines, however, were installed primarily as a customer service, and they included a soda machine, gaming machines, an automatic teller machine, two television sets, and two vending machines.

"The soda machine was installed free of charge by PepsiCo," he explained, "on the condition that I stock the machine exclusively with Pepsi products." His only other expense related to the soda machine would be for electricity. Any profits derived from it were his to keep. The cost of the gaming machines that were installed in the back of the laundromat was picked up by the vendor, Sunstar Vending Corporation. Michael was allowed to keep a percentage of the profits. Similarly, the ATM was the property of a third party, but Michael kept a small percentage of the profits. Michael purchased the two televisions and had them mounted on the walls of the laundromat,

again with the intention of differentiating his business from rival laundromats in the neighborhood that did not provide this additional service for their customers.

The vending machines provided a significant source of income for the business. One of these machines contained detergent and laundry products. The other contained snacks. Michael bought the products for these machines at Costco and BJ's, the warehouse stores, and also at Jetco, a vendor of food and cleaning supplies. Michael used three sources for vending sales to take advantage of price differences. Profits from vending were 300 percent over their cost.

Unlike Clean-Rite, which had no real competition, competitors did exist in College Point for New Age. When Michael was considering the location, he walked in to the closest laundromat, which was two blocks away. He could tell from his cursory inspection that the laundromat had not seen helpful improvements for several years. The owners were Chinese. To Michael, they came across as indifferent to their customers because they did not speak English. It was a family business, and they did not hire workers from outside their family. Michael checked other parking, and when he opened New Age a short while later, he made sure his services were twenty-five cents cheaper across the board.

Six blocks away was another laundromat, also run by a Chinese family. They owned the building, and it had a parking lot. Michael recognized that a parking lot could be a definite asset, but given the cost, it was not realistic. He was confident that most of his customers were within walking distance of their apartments, and he intended to provide customer service in other ways. "I know who my customers are, and I feel that I know what they want," he would proudly say.

In its first week of operation, New Age's sales revenue was \$600. For the week of April 8, 2006, exactly one year later, the sales revenue was \$6,000. Sales were not consistent, however, as Michael found sales during the winter and at month-end, when families had to pay bills and to drop. Sales were averaging \$5,500 per week, and clearly, Michael and Natasha were pleased. Based on location, demographics, and potential competition, they projected weekly sales to rise to \$7,000 after another year, and

EXHIBIT 1 Income Statements

	2005	2004	2003	2002	2001
CLEAN-RITE LAUNDROMAT, INC.					
Sales	220,800	213,600	204,000	185,400	150,000
Operating Expenses	187,680	175,172	152,080	133,488	99,000
Earnings before Interest and Taxes	33,120	39,448	46,920	51,912	51,000
Interest Expenses	0	0	0	0	0
Earnings before Taxes	33,120	39,448	46,920	51,912	51,000
Taxes Paid	6,824	7,692	9,384	10,382	10,200
Net Income	26,496	31,756	37,536	41,530	40,800
NEW AGE LAUNDROMAT, INC.					
Sales	285,960				
Operating Expenses	214,620				
Earnings before Interest and Taxes	71,490				
Interest Expenses	35,214				
Earnings before Taxes	35,776				
Taxes Paid	2,155				
Net Income	23,621				

to \$10,000 after five years. (See Exhibit 1 for the income statements on Clean-Rite and New Age.)

Laundry Services

The two types of customers at both laundromats are walk-in customers and drop-off customers. At both locations, walk-in customers represented 60 percent of the business and drop-off customers represented 40 percent.

The four different types of washers, depending on the size of the load, range from \$1.50 to \$5 per load. From smallest to largest, the washers handled twenty, twenty-five, forty, and fifty-five pound loads. The dryers were all twenty-five cents for every eight minutes.

For the drop-off customers, the charge for folding service was seventy-five cents per pound. One of the differences between the two locations, driven by a difference in demographics between the Glen Cove location and the College Point location, was that Clean-Rite provided free delivery for drop-off customers. Roughly one quarter of the drop-offs at Clean-Rite utilized this, the motivation for

which was again differentiated service and a loyal customer base. Michael's father did the deliveries. The amount of driving required was not excessive, but Michael sometimes felt guilty for obligating his seventy-year-old father, and he wondered perhaps if he'd sell the Glen Cove location, then his father would not have to work so hard.

Staffing

Michael employed three female attendants at each location. All of them were Hispanic, which was critical, in that these employees were from the community that the laundromats served. Moreover, the attendants needed to speak Spanish, because some of the laundromats' customers only spoke Spanish.

The customers at Clean-Rite were 70 percent Hispanic. The customer base was relatively homogenous, given seasonal employment on Long Island that tended to bring in a large supply of workers from Mexico and other Spanish-speaking countries. The neighborhood in College Point was more diverse, and the customers at New Age included

immigrants from Europe and Asia, as well as from Hispanic countries.

Unemployment was higher in College Point, so Michael found it easier to find good employees at the new location. The key for him was that his attendants could build a relationship with the customers, regardless of location. They needed to be clean and personable. In addition, Michael liked to employ female attendants who were attractive, as he believed that they would help to draw male customers to the laundromat.

The attendants were started at the minimum wage. They were all full time, so in 2005, Michael paid approximately \$38,000 in salary expenses at each location. The attendants were paid by check, with the appropriate deductions taken for social security. Michael also provided disability insurance, which he noted was three times more expensive for women than for men.

Many of Michael's operating costs were fixed (e.g., rent, depreciation). His utility costs were variable, as were his maintenance costs, based on the usage of his laundromats.

Technological Innovation

Michael dreamed about an additional aspect that would further enhance his laundromats business practices. The washers and dryers in his laundromats only took cash. Some laundromats, though, have machines that work off a smart card system. Michael knew that such a system, where the store would be less cash dependent, could have a competitive advantage, but at 600 and 1,500 square feet, respectively, neither Clean-Rite nor New Age seemed to be ideal candidates for such an investment. He knew that larger laundromats, generally 4,000 to 5,000 square feet, invested in these systems, since otherwise there would be too much cash on the premises at any one time. He was not aware of any laundromats near his locations that utilized smart cards, however. The ones that he was familiar with were in Manhattan, the Bronx, and Brooklyn, and in the towns on Long Island with large Hispanic populations, such as Hempstead and Bayside. At \$30,000 to install the system, and at \$300 per machine, Michael saw this now as cost prohibitive. Nonetheless, if he were to add a larger laundromat to his business portfolio, he

could envision the many benefits that such a system could deliver for his customers. For the drop-offs, he could utilize variable pricing. For the drop-offs, a smart system could track everything except tips, including customer history and trends. Similar to the point of sale systems at most dry cleaners, such an innovation would certainly look professional to the customer, and given the right situation, Michael would make the necessary investment for this.

Far Rockaway

By early 2006, Michael and Natasha were back on the road, seeking out another laundromat. Through their contact, David, they discovered that a 4,000-square-foot laundromat was up for sale in Far Rockaway, in Queens, sixteen miles from College Point. Once known as "The Playground of New York," the popularity of this area, a resort declined in the second half of the twentieth century, the result of the accessibility of newer vacation spots as well as increased urbanization. Several public housing projects were built in the area through the years, the mark-up of the community had changed, and consequently, the incidence of crime had increased. In 2006, Far Rockaway was struggling as a community, economically something that was quite apparent to Michael and Natasha as they surveyed the area.

Yet the idea of branching out challenged their earlier criteria in seeking out potential facilities.

The asking price for the laundromat was \$300,000, the same price that Michael paid to build New Age. The attraction clearly was that with the size of this facility, Michael could justify the installation of a smart card system. He figured that an investment in such a system could knock out any competition within a one-mile radius, as he firmly believed that technology would make a difference in this business.

Having a third business appeared greatly to Michael and Natasha. To make it happen, however, certain questions would have to be resolved: Would Michael be able to obtain the necessary financing to purchase a third business? Alternatively, should he sell Clean-Rite, where growth has plateaued, in order to be able to buy the new location? More fundamentally, though, were Michael and Natasha capable, both physically and emotionally, of further expansion of their family business?

The Decision

Michael was greeted fondly by his patrons as he entered New Age Laundromat and Natasha ushered him behind the front counter. You see, she said softly, "We are successful."

Michael nodded, opening the cash register. "Do you think we can take on more?"

"Yes, I do. This is our life, Mishka." She paused briefly, then continued, "It's good to expand. We can create a third corporation, to provide a shelter if the situation doesn't pick up at Clean-Rite. And you have always said that we can continue to take on long-term debt. The secret is to avoid short-term debts, right?"

"Natasha," he explained, "Our rent and utility bills are choking off our profits. Our rent is \$5,100 a month for New Age and utilities here are \$6,000 a month. In addition, we are paying \$600 a month in property taxes, which is ridiculous, since the building that we are in was built in 1924. These costs are out of line at Clean-Rite, too, and because our growth there has slowed down, our operating costs are eating into our margins. And we can't increase prices to deal with our higher costs, since our customers have low incomes. We simply can't use New Age to hold up Clean-Rite."

"Well, maybe we can increase our volume of sales with the new location..."

Michael snapped, "Did you see the neighborhood? Do you think our little laundromat can turn it around? He noticed one of the customers at a dryer looking toward him, and he lowered his voice. "Clean-Rite is a small store. The equipment is still good, but because of its physical limitations, I don't think it pays to replace the equipment when it begins to break down."

"I'm not sure," Natasha replied. "Whatever we get out of Clean-Rite is gray, as far as I'm concerned. After all, we have no debt at all there."

Michael shrugged. "All right, give me a little more time to think about it. These are important questions. Our little business venture has certainly taken on a life of its own. And like you, I am passionate about it. I want to keep making improvements. Let's take another ride out to Far Rockaway. Let's see if we should move forward there. And let's look at our numbers. I want to do what's best."

Michael stepped in front of the counter. A little girl was crying and he lifted her out of her stroller to kiss her gently on her cheek.

Notes

1. It was perhaps fitting that Michael and Natasha find their home in Lathwain, the grandson of William Lathwain, who capitalized on the housing crunch in the years following World War II, offering affordable housing to returning GIs and their families. In the form of many detached, single-family houses that became the archetype community for the New York City suburbs and the American dream, some that after ten years, high-rise apartment houses had replaced in value. (654,000).
2. The purchase price included the cost of all the existing equipment in the laundromat.
3. Perhaps the primary constraint in this search involved how expensive the drive would be to get to either of Natasha's homes.
4. The property for New Age Laundromat was leased.
5. The cost of these machines ranged from \$1,500 to \$6,000. Clearly, when New Age Laundromat was being constructed, Michael needed to consider this, coupled with the need to optimize his space with the right mix of machines.
6. Reported crime as a percentage of the population in the 10th precinct, which included Far Rockaway, was 1 percent according to the NYPD from the calendar year 2003. Michael had not read this, however, that this was the national rate for the 1990s period, which covered College Point. His perception was that crime was worse in Far Rockaway.