

# New Players Making Impact on For Profit Landscape

## Seventeenth Annual Status Report on For Profit Child Care

by Roger Neugebauer

While the recession has slowed the overall growth of the for profit child care sector, many new players are entering this arena bringing fresh perspectives and new energy.

In the past two years we have added 12 new organizations to the Exchange Top 40 — North America's Largest For Profit Child Care Organizations (see page 18). Many of these organizations have been started within the past five years.

Even with some of the largest and oldest organizations there are new players. Four of the six largest chains — Knowledge Learning Corporation, La Petite Academy, Childtime Learning Centers, and Nobel Learning Communities — have brought in new leaders in the past 18 months.

To glean some insights on how these new players view prospects for the for profit sector, we interviewed two of the new leaders — Tom Heymann and Gary Graves. Heymann was appointed chairman and CEO of Knowledge Learning Corporation, which has become the second largest child care organization in North America (and most likely the world) with its recent acquisition of Children's World Learning Centers. He was previously presi-

dent of the Disney Stores and led other customer service-driven companies in the restaurant and technology arenas. Graves, who was appointed CEO of La Petite Academy in late 2002, also followed a path with strong emphasis on customer service in heading companies primarily in the restaurant industry for PepsiCo and most recently as COO of a national parking company.

**Exchange:** How would you compare the child care industry with other industries where you have worked?

**Graves:** I think there is a lot in common. My experience has been in multi-site corporations with geographic dispersment and a heavy emphasis on customer interaction. The major differences are in the areas of regulation (with child care operating under much more restrictive regulatory control) and labor (with labor being a much more significant component of the P&L in child care).

**Heymann:** One major similarity with my work at KLC and Disney is that in both cases what we offer has to appeal to children, but we also need the approval of parents. So we have to be sensitive to the needs of both children and parents. In child care, the services we provide

are infinitely more important, but our relationship to parents is similar to the Disney model. Disney was known for the focus it provided on the relationship of "cast members" to guests. In child care a major focus of our efforts is on strengthening the relationships between center staff and families.

One major difference is employee training. In my previous roles we needed to train staff on sales and customer service. In child care, not only do we need to train employees on customer service, but we also need to provide in-depth training on education — our employees have so much more to learn, to be responsible for.

Another stark contrast is the lack of collaboration within the child care industry. In other industries, members have come together to promote the interests of the industry. In child care we have so many common issues and common bonds, yet we have not come together effectively. There is a great opportunity for the industry to become much stronger. I am committed to supporting this.

**Exchange:** These past three years have been slow ones for large national chains. When the economy picks up again, will

large national chains return to strong profitability and start growing again?

**Heymann:** There will be incremental growth and some new pockets of opportunity, but nothing like in the early years. This mimics my experience in other retail businesses where no one will be quadrupling in size any more. It's not likely that any of the chains will be adding hundreds of new centers or doubling in size. Where the growth will come is with acquisitions.

**Graves:** At La Petite we're not banking on a quick turn around. To begin with, our industry has so much unused capacity right now — with most organizations operating at about 60% capacity — that it will take a while to use up this existing supply. Also, I think that people are going to be really cautious — I think they are going to wait for two good economic quarters before they loosen their purse strings.

**Exchange:** Will child care continue to be a cottage industry with the large chains operating a tiny percentage of all the centers, or will there start to be dramatic consolidation as in other industries?

**Graves:** This is one of the most fragmented businesses in the world outside of dry cleaning. But I don't think there will be significant consolidation. Why would companies consolidate? What are the cost savings? Not many costs in our business are scale-driven. I think it would be very hard for large acquisitions to drive enough improvement either through higher revenues or lower costs to offset the "premium" you pay to acquire a business. Frankly, with some excess capacity, I think you're better off focusing on growing same-academy profitability versus acquiring more capacity.

Also, since there are few barriers to entry, there are always new players entering the business. It always

## Most Serious Threats

Leaders of the 40 largest for profit child care organizations identified the following, in priority order, as the most serious current threats to their organizations:

1. Competition from the public schools
2. State of the economy
3. Shortages of qualified teachers
4. Changes to state regulations/licensing requirements
5. Decreases in public subsidies
6. Child being injured in an accident at one of your centers
7. Shortages of teacher aide candidates
8. Accident involving a center vehicle
9. Availability of center liability insurance
10. Competition from new centers
11. Lack of affordable space for expansion
12. Pressure from parents to teach more academics
13. Competition from unlicensed providers
14. Computer failures/software glitches
15. Abuse allegations against center staff by parents
16. Compliance with American's with Disabilities Act
17. Child snatching from your center in a custody dispute
18. Growing demand for flexibility in hours of care
19. Intrusion by an armed or unstable person
20. Actual occurrence of an incidence of sexual abuse at one of your centers

surprises me that so many people want to get into this business, with its low margins, but it seems to hold an attraction for people leaving big corporations and looking to start their own business.

One of the things I find very interesting is that the "newest" players in the for profit world that have more than 100 centers appear to be franchise driven. One of the reasons could be that the unleveraged returns on investment are below 5% for the majors, so why take capital risk when you can get a 5-8% margin on franchisees' revenues?

**Heymann:** I think there will be some consolidation at the top, but if we go from having multi-site companies operating 6% to having them operate 8% of all centers this won't alter the structure of the industry.

**Exchange:** For the third consecutive year leaders of the 40 largest for profit child care companies identified "competition from public schools" as the most serious threat to their organizations in our annual survey. How do you think recent initiatives to enact "universal" pre-k programs operated through state departments of education will impact the for profit sector?

**Heymann:** I applaud efforts to extend preschool services to disadvantaged children. There is no question how important the early years are — all children deserve the best chances possible. The problem is that solutions being proposed are in complete conflict with the interests of the taxpayers. These need to be redirected to make sure that the disadvantaged have plenty of solid opportunities.

My observation is that we have a crisis in the output of public education, not in

early childhood education. This is because early childhood education operates in a highly competitive marketplace. Every day in our centers if we don't do a good job, our customers will walk away. This is true for both for profit and non profit centers. The temple where my children attended preschool had to be just as customer-focused as a Children's World center. The public schools on the other hand, face no such accountability.

Instead of current universal pre-k initiatives, I think we need to take these dollars and expand the existing subsidy system by extending thresholds of eligibility. Families earning \$75,000 a year may not need the same government subsidies as families earning \$25,000 do. And, families earning \$75,000, as well as families earning \$25,000, need to know that when their children go to public school they will not be in a class of 35 children.

**Graves:** I think the initiatives have great goals and are admirable, however the implementation is flawed. I am not afraid of competing on a level playing field with high standards. But the current climate is unacceptable. To begin with when public schools offer child care services, they do not need to comply with the same licensing requirements. And, when states contract with private providers they demand high staff standards but impose low reimbursement rates. The pre-k program in Georgia has driven up costs and driven down rates. I am concerned that Florida will go down the same path as Georgia has. Under the current program's design, I would be hard pressed to invest in new sites in either Georgia or Florida because it's very hard to get an acceptable return on that investment. I believe if you look at the major for profits that are not franchisee systems, you'll find that location counts in Georgia have declined due to closures.

## The Exchange Top 40 North America's Largest For Profit Child Care Organizations

Organization	Headquarters	CEO	Centers*	Capacity*
KinderCare Learning Centers	Portland, OR	Dave Johnson	1,269	167,000
Knowledge Learning Corporation	San Rafael, CA	Tom Heymann	850	112,365
La Petite Academy	Chicago, IL	Gary Graves	648	89,835
Bright Horizons Family Solutions	Watertown, MA	David H. Lissy	510	59,000
Childtime Learning Centers	Novi, MI	Bill Davis	483	52,000
Nobel Learning Communities	West Chester, PA	George Bernstein	168	28,100
Child Care Network	Columbus, GA	James F. Loudermilk	117	15,881
Children's Courtyard	Arlington, TX	Edward Follen	76	13,255
The Sunshine House	Greenwood, SC	Dennis Drew	97	13,010
New Horizon Child Care	Plymouth, MN	Susan Dunkley	89	12,410
Minnieland Private Day School	Woodbridge, VA	Jackie M. Leopold	85	9,579
Allegheny Child Care Academy	Pittsburgh, PA	Harold Lewis	38	6,845
Mini-Skool	Scottsdale, AZ	Douglas MacKay	39	6,000
Children's Friend	Warner Robins, GA	F. Dewayne Foskey	40	5,824
Rainbow Child Development Centers	Lathrup Village, MI	Patrick G. Fenton	40	4,322
Sunrise Preschools	Phoenix, AZ	Robert Orsi	17	3,376
The Phoenix Schools	Sacramento, CA	Jacqueline Colbert	20	3,362
Action Day Nurseries/Primary Plus	San Jose, CA	Carole Freitas	15	3,325
Hildebrandt Learning Centers	Wilkes-Barre, PA	William J. Grant	30	3,053
Creme de la Creme	Greenwood Village, CO	Bruce T. Karpas	8	2,512
Pinecrest Schools	Sherman Oaks, CA	Don L. Dye	11	2,505
Country Home Learning Center	San Antonio, TX	Sharon K. Ford	8	2,504
Stepping Stone School	Austin, TX	Rhonda Paver	14	2,389
Children's Choice Learning Centers	Plano, TX	Nate McClintock	8	2,239
Children's Lighthouse Management	Fort Worth, TX	George Michael Brown	8	2,160
Tot-Time Child Development Centers	Plymouth Meeting, PA	Donna M. Bongarzone-Fluehr	19	2,110
Creative World School	Tampa, FL	Billie McCabe	17	2,012
Creative Playrooms	Solon, OH	Joan P. Wenk	7	1,900
Kid's Country	Snohomish, WA	Lynnda Langston	11	1,778
Bobbie Noonan's Child Care	Frankfort, IL	Judith Nevell	13	1,700
Children's Creative Learning Centers	Sunnyvale, CA	Ty Durekas	15	1,682
Rogy's Learning Place	East Peoria, IL	Don Meyer and Rick Rogy	13	1,526
Seven Oaks Academy	Westminster, CO	Ronald S. Faillaci	11	1,497
Kiddie Kare Schools	Fresno, CA	James Fisher, Jr.	10	1,492
Celebree Learning Centers	Bel Air, MD	Richard O. Huffman, III	11	1,477
Sunny Daze	Edmond, OK	Mike North	7	1,394
Child Care Connection	Lincoln, RI	Kevin Fusco	11	1,280

### National Child Care Franchising Organizations

Organization	Headquarters	CEO	Centers*	Capacity*
Kids R Kids International	Duluth, GA	Pat Vinson	109	21,800
Goddard Systems	King of Prussia, PA	Philip A. Schumacher	160	21,000
Primrose School Franchising Company	Acworth, GA	Jo Kirchner	118	20,408
Kiddie Academy	Bel Air, MD	Michael J. Miller	70	9,535

Data on capacity in above chart is the total licensed capacity for all centers as of January 1, 2004. Data for "Franchising Organizations" include both franchised and company owned centers. Based solely on information supplied by organizations listed.