The Model has Changed

By Richard B. Kelsky

In what seems like the blink of an eye, the check cashing industry has changed. Your business model *must* change with it. And it must change ***now***.

In recent years – particularly the boom ones that preceded the current recession – many check cashers adopted an ostrich's approach to change. True, some trotted out the ladders, brushes and cans of Benjamin Moore, and called in the contractors and signage companies, but most did not think in terms of changing business models – disappearance of government checks, managing cash flow, P & L and balance sheet, direct deposit, debit cards, changing emphasis from transaction fees on in-store transactions to recurring revenues, and how marketing (an historic check cashing no-no) could drive revenues. Few, if any, considered analyzing their business at 20 percent less volume.

As we move deeper into this decade, the pace of industry change will only accelerate.

For tough-times guidance on business models, I suggest learning from recent immigrants entering the industry. They couple solid financial analysis with an unwavering faith in the opportunity in this country, and a commitment to succeed now, when the going is hardest. It's also wise to look toward counter-cyclical and counter-directional hedges that can offset losses in current revenues – today and over time.

Recession is always a period of great creativity. In sector after sector, technology is enabling productivity gains and more efficient management of cash, and just about everything else. But technology is also changing the expectations of customers regarding what they'll pay and to whom.

These times have produced much red ink for some check cashers, even as others have been reinventing and rebuilding their businesses. Most who count themselves as casualties admit to being unaware or unable to react to what's been happening. Those who've disappeared from the industry landscape typically suffered that slowest of business deaths, the one brought on by a thousand cuts.

Avoiding that fate means learning to embrace change and seek out opportunity. If others have given up, are unable to alter their approach, or cannot see a direction for the future, make their losses your gain. Here are some key observations to bear in mind as you move forward.

The Business is Evolving.

The primary evolutions in this business are toward the ***immigrant model***, and recognition that ***ancillary and recurring revenue streams*** will determine future success.

Government checks are disappearing. There's no arguing this. The Feds are getting out of the check business, and the states are following close behind.

In some states, citizens have been successful in mandating a paper check option. But as cost pressures and large-bank lobbying efforts are brought to bear on state legislators and regulators, it's just as likely that attempts to preserve the paper check option are falling on deaf ears.

Direct deposit to prepaid cards is a short-term shot at mitigating that loss of government checks - and a long-term opportunity of building recurring revenue – but direct deposit and debit cards have to be managed on an ongoing basis to give them staying power (they won't manage themselves!), and you have to start working on your long-term plan today.

Cash lives. Despite the relentless drumbeat of debit card vendors, you are still in the check cashing business. That business cannot be ignored and must be nurtured. Cash remains an important component in American lives. So the next time someone tells you cash is an extinct species, ask them if they handed their debit card to that guy who just plowed a surprise foot of snow from their driveway, or towed their car off a lonesome stretch of road at 3 a.m. Or just walk by a large bank branch on a Friday evening in a major city: six ATMs, and all with a line.

Your Customer Base is Evolving.

The economic crash has lost you some longtime customers. Whether they return to cash checks in the future, no one can say. Commercial check volumes have also been dramatically impacted by the recession. You will have to work smarter to grow your customer base and new lines of business.

At the same time, increased regulation is working to expand the unbanked population. The banks' response to regulation – which has capped or eliminated certain fees – is to limit, charge, or charge more for services which, until very recently, have been provided for free, or nearly for free. The result? More folks will be filing for divorce from their banks and realizing it's actually less expensive and easier to use your services.

Quickly changing their tune, banks have rapidly retreated from seeking out the traditional unbanked customer. Just look at their marketing, of which they are doing plenty. I heard of one that was offering a free e-reader in exchange for opening an account with $10,000. That tells me the bank's target isn't people living paycheck to paycheck. Instead, they're going after an audience that has the leisure time to read. People who can afford to move $10K from another account for a free gift. Their other target appears to be Gen Y – with high-tech account management promises and automated this-and-that. The problem for them is that now comes with a price tag.

To earn a greater share of the evolving unbanked's (and underbanked's) business, you need to better understand the shifting demographic of the customer base, and the marketing and market trends that are expanding your opportunities. Consider these:

Baby Boomers: This group thrives on old-time familiarity, and steadiness of service. The problem is, this group is aging and moving away from paychecks into government benefits. But just as aging Boomers are moving toward fixed-income, banks are creating and increasing fees, so their interest in banks is not likely to grow. Keep up the good work with this group and immediately institute programs to inspire customer loyalty and provide an increased range of services, including direct deposit.

Generation X: Gen X – those born from the '60s to as late as about 1980 – is moving into midlife. Their stage of life, coupled with the fact that Xers came of age with PCs, means they're partial to more traditional marketing, but with a technology lean.

Generation Y: Gen Y – people born from about 1980 through the early 2000's – require an open mind to new methods of marketing, plus conveying the feeling that you care about them personally. Remember, this is the group that came of age with the Internet. The notion of a "mass market" – that listened to broadcast TV and blindly bought what Madison Avenue told it to – is foreign to Gen Y. Its members have grown up in a peer-to-peer marketplace. An endorsement of a product or service by their digital "friends" – and a caring touch - has a much greater influence on their purchasing decisions.

Your Market Reach is Evolving.

Smartphones have made it possible for you to reach out much farther and faster into your existing and potential markets than ever before. Since most post-Boomers communicate by text or through social media, you need to use those methods to communicate with them.

As your market grows more diverse in step with America's population, you'll also need to figure how best to reach out and touch it. Begin formulating a more sophisticated strategy to reach customers via their smartphones. Here's something you might not know, but really should: Recent studies have found that Hispanics are the fastest growing group of smartphone users and that African Americans and Hispanics access the Internet on their smartphones far more frequently than the population as a whole.

The old-school idea that your market is limited to those who already enter your premises, and that they must live within a six-block radius from your store, is just that: Old School. With the right combination of technology and traditional approaches you can reach existing as well as potential customers. Employ a combination of low-marginal-cost, high-penetration internet and smartphone marketing, onsite marketing, and loyalty programs – you can (and must) reach beyond your old geographic borders to draw new customers and expand your business with current ones.

Of course, expanding your market reach beyond your old-school neighborhood may mean extending it *into* the neighborhood of another storeowner that you never before considered a direct-competitor. Like it or not, you can't avoid dealing with the shifting economics that come with being part of a maturing and fast consolidating industry. What you can do is use every technical advantage to come out on top in this Darwinian struggle to adapt and thrive.

All of this activity will involve data and data analysis. So you need to get to work to make sure every single one of your customers – and every transaction - is in your database – and you may have to purchase supplemental databases, as well. *Consider this: It's impossible to communicate with a walk-in customer when they're not in your store.*

The Economics are Evolving.

Borrowed Money Isn't All It's Cracked Up To Be. In a declining revenue scenario, debt – or more to the point, debt service – is bad. Unless it is for growth under a realistic plan, if you don't have debt, don't start now. Focus on profitability. Do you have a set of readable monthly financial statements? Do you actually understand them? Do you understand the difference between profitability and cash flow? Do you know how you spend your time each day? Do you start each day with a plan (even if you don't stick to it)? Or do you just seem to move from mini-crisis to mini-crisis? Those who continue to think they can manage their business by the seat of their pants will end up losing their shirt.

Ancillary and recurring revenue. Ancillary revenue is becoming more important. Whatever the source, whether wires, debit cards, bill payments, ATMs, money orders, alternative energy providers, or POB transactions, you need to focus attention on these types of products. A combination of intelligent product selection, offering of multiple competitive products, and marketing can produce significant bottom-line results. Take for example competitive wire companies: smaller established wire companies which cater to single country markets, have numerous agents in their home country, and are sought out in the communities they serve here.

Similarly, as I stressed last year, because each customer's transaction pattern will drive the correct debit card for them, you need to offer a selection of debit cards. Customers keep their debit card relationships longer if they are happy.

Debit cards and other ancillary products can produce recurring revenue – even though the customer is not in your store. This shift – from on-site transaction revenue to off-site ***recurring revenue*** – will take time. You need to start now to build recurring revenue streams for the future.

The Immigrant Model

In addition to adopting a more disciplined managerial approach, expectations "per store" must change. A few years back, there were many people in this industry who made a living from only one store. While that's still possible, it is becoming increasingly less common. In fact, it's becoming increasingly difficult for two or three stores.

The good news is there is already a successful model you can emulate: The immigrant multi-store owner. Many longtime owners of single store operations might be tempted to look at the current market with a self-pitying longing for bygone days that will never return. Not so the immigrant multi-store owner, who looks to the future and sees untold possibilities, if only he can achieve sufficient scale. Rather than a feet-in-concrete view of one store that hits an improbable home run, this model relies on hitting singles – lots of them. It's a combination of "Don't put all your eggs in one basket" and "The whole is equal to the sum of its parts." It also includes other lines of business, if state law permits.

The math behind this model goes something like this: 2 big stores x $200,000 (check cashing income) = $400,000 (Risky.) But 20 smaller stores x $30,000 (check cashing income) = $600,000 (Less Risky and More Profitable.) And 20 stores x $30,000 (check cashing income) + $25,000 (other lines of business income) = $1,100,000. (Even Less Risky and Even More Profitable.) Which would you rather have? Two four-window stores with revenue at risk and sky-high overhead, or 20 one-window stores, with stable core revenue, respectable ancillary and recurring revenue sources, other lines of business and manageable-overhead? The answer is obvious.

Granted, the sustainable multi-store number may not be 20 in your market – or you may not be in a position to acquire that many locations. Depending upon your market and your appetite, it could be five, or six or seven stores. The important thing is to adopt a mentality that sees multi-store scale as a hedge against risk, and a door opener to greater top and bottom line growth then you'll ever see from a one-shop op.

Ultimately, success under the new model hinges on figuring out how much you can reasonably expect to make from each location, building ancillary and recurring revenue, and working and living within your means. As I've reminded readers before, never ask more of your business than it can give. No model – no matter how attuned to change and how successful – can survive an owner who places unrealistic demands on the business.

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