

COVER STORY

By Diane Brady and Christopher Palmeri

The Pet Economy

Americans spend an astonishing \$41 billion a year on their furry friends



If there's still any doubt whether the pampering of pets is getting out of hand, the debate should be settled once and for all by Neuticles, a patented testicular implant that sells for up to \$919 a pair. The idea, says inventor Gregg A. Miller, is to "let people restore their pets to anatomical preciseness" after neutering, thereby allowing them to retain their natural look and self-esteem. "People thought I was crazy when I started 13 years ago," says the Oak Grove (Mo.) entrepreneur. But he has since sold more than 240,000 pairs (a few of which went on prairie dogs, water buffalo, and monkeys). "Neutering is creepy. But with Neuticles, it's like nothing has changed." Nothing, except there's a fake body part where a real one used to be.

Americans now spend \$41 billion a year on their pets—more than the gross domestic product of all but 64 countries in the world. That's double the amount shelled out on pets a decade ago, with annual spending expected to hit \$52 billion in the next two years, according to Packaged Facts, a consumer research company based in Rockville, Md. That puts the yearly cost of buying, feeding, and caring for pets in excess of what Americans spend on the movies (\$10.8 billion), playing video games (\$11.6 billion), and listening to recorded music (\$10.6 billion) combined. "People are no longer satisfied to reward their pet in pet terms," argues Bob Vetere, president of the American Pet Products Manufacturers Assn. (APPMA). "They want to reward their pet in human terms." That means hotels instead of kennels, braces to fix crooked teeth, and frilly canine ball gowns. Pet owners are becoming increasingly demanding consumers who won't put up with substandard products, unstimulating environments, or shoddy service for their animals. But the escalating volume and cost of services, especially in the realm of animal medicine, raises ethical issues about how far all this loving should go.

It wasn't so very long ago that the phrase "a dog's life" meant sleeping outside, enduring the elements, living with aches, and sitting by the dinner table, waiting for a few scraps to land on the floor. Today's dog has it much better. APPMA reports that 42% of dogs now sleep in the same bed as their owners, up from 34% in 1998. Their menu reflects every fad in human food—from locally sourced organic meat and vegan snacks to gourmet meals bolstered by, say, glucosamine to ward off stiff joints. Half of all dog owners say they consider their pet's comfort when buying a car, and almost a third buy gifts for their dogs' birthdays. Richard G. Wolford, chairman and CEO of Del Monte Foods Co. (DLM), refuses even to use the word

"owner." "Anyone who has a pet understands who owns whom," says Wolford, who is owned by two Jack Russell terriers. His company's pet business has gone from nothing to 40% of overall sales through acquisitions of brands such as Meow Mix and Milk-Bone in the past five years.

The rising status of pets has started an unprecedented wave of entrepreneurship in an industry once epitomized by felt mice and rubber balls. There are now \$430 indoor potties, \$30-an-ounce perfume, and \$225 trench coats aimed solely at four-footed consumers and their wallet-toting companions. Even those who shun animal couture are increasingly willing to spend thousands on drugs for depression or anxiety in pets, as well as psychotherapy, high-tech cancer surgery, cosmetic procedures, and end-of-life care. About 77% of dogs and 52% of cats have been medicated in the past year, according to APPMA, an increase of about 20 percentage points from 1996. Some spending can be spurred by vets who find such services more lucrative than giving shots or ending a pet's life when it contracts a painful or terminal disease.

GRAVY TRAIN

Once acquired as sidekicks for kids, animal companions are more popular now with empty-nesters, single professionals, and couples who delay having children. What unites these disparate demographic groups is a tendency to have time and resources to spare. With more people working from home or living away from their families, pets also play a bigger role in allaying the isolation of modern life. About 63% of U.S. households, or 71 million homes, now own at least one pet, up from 64 million just five years ago. And science is starting to validate all those warm feelings with research that documents the depth of the human-animal bond.

It doesn't take a scientist to figure out that there's money to be made in this environment. Companies from Procter & Gamble (PG) and Nestlé (NSRGY) to fashion brands including Polo Ralph Lauren (RL) and thousands of small entrepreneurs are sniffing around for new opportunities in the pet sector. After consumer electronics, pet care is the fastest-growing category in retail, expanding about 6% a year. More new pet products were launched in the first six months of last year than in all of 2005. And that doesn't account for the ways existing products are being recast to woo pet lovers. Del Monte has refocused staples to look more like human snacks—from Sausages breakfast treats shaped like bacon and eggs to Pup-Peroni rib snacks so appetizing that Wolford had to stop a TV anchor from popping one into his mouth on air. Even Meow Mix now comes in plastic cups rather than cans.

The typical target of such products is a pet lover like Graham Gemoets, a caterer in Houston, who showers luxuries on his beloved "chi weenie" (Chihuahua/dachshund mix), Bradford. "He's my best friend and my best-accessorized friend," says Gemoets, whose splurges for Bradford include a \$1,200 Hermès collar and leash, as well as \$500 Chanel pearls for parties. "I know it's crazy, but I've had him for five years, and if you priced it out per month, it's like a phone bill."

Thanks to passionate consumers like that, the quality gap between two-legged and four-legged mammals is rapidly disappearing in such industries as food, clothing, health care, and services. The race now is to provide animals with products and services more closely modeled after the ones sold to humans. Most of the pet business world's attention is directed at the country's 88 million cats and 75 million dogs. The reason is simple. As Philip L. Francis, CEO of PetSmart Inc. (PETM), the world's largest pet specialty retailer, explains: "You can't train a fish or groom a snake."

PetSmart, for one, has shifted its mission from being the top seller of pet food to helping consumers become better "pet parents." Along with making his 928 retail locations homier and hosting pet parties, Francis is rolling out blue-shingled "pet hotels" (kennels) in his stores. They feature private suites with raised platform beds and TVs airing shows from Animal Planet for \$31 a night, as well as "bone booths," where pets can take calls from their owners, and porous pebble floors where dogs can pee. Cats get live fish tanks to watch in their rooms and separate air filtration systems so their scents don't drive the dogs crazy. The hotels, along with services such as grooming, training, and in-store hospitals, have helped PetSmart expand its service business from essentially nothing in 2000 to \$450 million, or 10% of overall sales, this year. Pet owners are now less driven by price than "emotion and passion," says Francis, who shares a bed with his wife and their mutt, Bit o' Honey.

Those are the same primal urges that drive the fashion world. Mario DiFante, who staged New York's first Pet Fashion Week last August, has an elevated view of the place of dogs and cats in the family hierarchy. As he puts it: "Many of us consider pets as the new babies." That means clothing furry little ones in an ever-expanding range of sweaters, raincoats, leather jackets, and dresses. For Lara Alameddine, co-founder of Little Lily, a better word might be "babes." Her four-year-old company clears \$1 million a year selling products including doggie slippers, bikinis, and even canine versions of Oscar-night gowns. It's popular with celebrity dog owners such as Paris Hilton, who often dresses up her Chihuahua, Tinkerbelle. "We're catering to the owner's sense of style," says Alameddine. "There are no bones on our clothes."

Pet products now aim to make people feel they're being extra good to their little ones—much as toymakers have long encouraged parents to spoil kids. Along with doggie spas, there are mobile pet-grooming vans, pedicure services, professional dog walkers, and massage therapy for animals. Trainers like Cesar Millan—better known to millions as the Dog Whisperer—find that their expertise is suddenly in greater demand. Along with having the No. 1 series on the National Geographic Channel, Millan boasts best-selling books, DVDs, a line of products, and his famous Dog Psychology Center of Los Angeles that's a favorite with Hollywood clientele (see BusinessWeek.com, 7/27/07, "A Short Leash on Pet Luxuries?").

The growing willingness of owners to spare no expense for their animals has also made the outsourcing of the yucky aspects a burgeoning business. More than 350 service agencies with names such as **Doody Duty**,

Scoopy-Poo, and Pooper Trooper have sprung up solely to relieve owners of the need even to pick up a pet's waste in their yard by doing it for them. With annual growth nearing 50%, "the pooper scooper industry is now experiencing a lot of consolidation," says Jacob D'Aniello of DoodyCalls, which has 20 locations nationwide.

But few parts of the business have seen as much diversification and expansion as the pet food business. As with humans, there's a growing concern about the nutrition, taste, and even ethical standards of what goes into a pet's stomach. Owners increasingly mirror their own preferences—for vegetarian cuisine, kosher meals, and even locally sourced food—in feeding their pets. And when things go wrong, the reaction is as explosive as if the victims were children. Consumers were outraged by a massive recall of melamine-contaminated pet food that killed or sickened thousands of U.S. cats and dogs. Because pets are now such valued members of the family, says Duane Ekedahl, president of the Pet Food Institute, "it had a higher impact than maybe it would have had 10 years ago."

As food becomes a more emotionally charged issue for people, owners are more inclined to get emotional about what's on their pets' menu. Witness the growth of what one industry executive calls the "Godiva-ization" of food, with a demand for meats fit for human consumption, visible vegetables, and nutritional supplements. It has become common to reach for a canine or cat equivalent of ketchup, such as Iams Co.'s (PG) popular "savory sauce" for dogs that comes in Country Chicken, Savory Bacon, and Roasted Beef flavor—descriptions that are, needless to say, lost on the actual consumer.

THOROUGHLY VETTED

Fancy food products are easy targets for critics of indulgent pet owners. But a far more controversial issue is animal medicine, especially at a time of urgent national debate about human health care. Americans now spend \$9.8 billion a year on vet services. That doesn't include the over-the-counter drugs and other supplies, which add \$9.9 billion in costs.

The annual compound growth rate for core veterinary services alone has been about 10% over the past decade, and the menu of services is becoming more elaborate by the month. Much of the inflation in pet care is due to medical advances that have people digging deep for everything from root canals for aging cats to cancer surgery for rabbits. "There has been an evolution of the entire profession," says Tom Carpenter, president of the American Animal Hospital Assn. "Pocket pets and animals who wouldn't even have been taken to vets now go for regular visits."

Suzanne Kramer of Chicago spent close to \$380 on vet visits and drugs to treat a tumor in her hamster, Biffy, before he died last year. "Some might say: Well, he's just a hamster,' but I loved him," says Kramer. Barbara Miers of Rochester, N.Y., also took her son's hamster, Henry, to a vet and bought antibiotics for a tumor, even though the animal was nearing the end of his life span and died shortly after the final treatment. For Miers, the issue had parallels

to human health. As she puts it: "Do you not give old people health care because they're old?"

No wonder "it's a good time to be in our profession," as Carpenter says. A vet's job has become more wide-ranging and thus more lucrative. There are even animal grief counselors to help families cope with the demise of beloved pets. Not only is state-of-the-art technology such as magnetic resonance imaging, with costs that range around \$1,500 a scan, now available in small-town labs, but consumers' expectations of medical care have been transformed. They want the same best-in-class care for their pets that they want for themselves.

That's creating a market for new products like Pfizer Inc.'s (PFE) dog-obesity drug Slentrol, which will cost \$1 to \$2 a day. Reconcile, a new drug from Eli Lilly & Co. (LLY) for "canine separation anxiety," is based on the active ingredients in Prozac. Lilly has not suggested a retail price for Reconcile, and vets have a lot of latitude in deciding how much to charge for it. Overall, sales of pet health products have grown at a compound annual growth rate of 8.8% in recent years, more than double the rate in the late 1990s.

There's little doubt that human-quality care has helped to extend radically the life span of pets. Dogs routinely live 12 to 14 years now, a big jump from the average a few decades ago. John Payne, acting CEO of Banfield, the Pet Hospital, likes to boast that his cat, Gizmo, stayed perky until he died last November at the advanced age of 23 1/2.. More than 60% of new customers of his chain, which has more than 600 locations nationwide, enroll their pets in wellness plans. One reason is that standard pet insurance often doesn't cover preventive care. While pet insurance is still in its infancy, with 1% of owners having coverage, the number of clients is growing by double digits each year. Jamie Ward invested in a \$25.77-a-month plan with Veterinary Pet Insurance (VPI) for her American Staffordshire terrier, Loki, only to discover that it didn't cover any of the \$2,000 in expenses for a kneecap injury. (VPI says it abided by the terms of the contract.)

The ever-expanding roster of drugs and treatment can run into tens of thousands of dollars in expenses, creating a dilemma for owners. Steve Zane of Hoboken, N.J., choked slightly when a veterinarian presented him and his wife, Lily, an estimate of \$3,700 to help cure liver failure in their cat, Koogle, over Christmas. "We looked at each other and said: Well, he's family," recalls Zane, a graphic designer who's still paying off the final bill for the recovered cat. "If it had been \$15,000, I think we would almost have had to say no."

The anthropomorphization of pets has also created the perception that they have human problems such as separation anxiety and depression. While a number of vets say such issues are real, especially just after the death of a dog's four-footed chum or the removal of puppies, others say it simply creates yet more opportunities for new products. Americans are expected to spend 52% more on medicines to treat their pets this year than they spent five years ago. Drugmakers love the category because, compared with human drugs, there's less risk of

liability, less competition, and less pressure to switch to generics because so few consumers carry pet insurance. Even so, Dawn M. Boothe, a professor of clinical physiology and pharmacology in the Auburn University College of Veterinary Medicine, argues that "the recovery of costs" for drug companies may take a long time as people may scoff at pricey treatments for pets.

Much of the attention is going to the growing problem of pet obesity. As many as 40% of dogs are estimated to be overweight or obese, with similarly high rates among cats, thanks to the indulgent habits of their owners. Being plied with carob bonbons all day while getting rolled around in an all-terrain stroller (retail price: about \$210) is not an ideal lifestyle for any animal. People who overeat or don't get enough exercise tend to draw their pets into the same behavior, vets say, and the growing inclination to regale pets with treats has come at a cost to their waistline. Along with creating interest in new anti-obesity drugs, it's prompting interest in diet pet food. It has also created a market for procedures including pet liposuction, which is becoming more common in cities like Los Angeles where owners are used to getting nips and tucks for themselves.

And for some pet lovers, no medical procedure is too extreme. Plastic surgeons offer rhinoplasty, eye lifts, and other cosmetic procedures to help tone down certain doggy features, from droopy eyes to puggish noses. Root canals, braces, and even crowns for chipped teeth are also becoming more popular.

Some might question whether all this primping and pampering of pets has the makings of a bubble that could have owners telling Fido to get his own damn bone once the economy takes a turn. After all, Paola Freccero admits that when she grew up in Massachusetts, "Pets were pets. You didn't dress them, you didn't feed them special food, you didn't take them to play dates." But thanks to the advice of her vet and what she read on the Internet, she wouldn't serve up anything but the best for her puggle (pug/beagle mix), Lucy, including treats at \$2 apiece. And from the moment Eric Olander paid \$500 for a plane ticket to get a stray chow chow mix from Atlanta to his home in Los Angeles, the dog has been a focal point of his life. "I call him my 401(k) with paws," he says, "because that's where all my money goes."