

Pet Smarter

Four years ago Chewy's college-dropout founders couldn't get a meeting in Silicon Valley. Now they're running one of America's biggest privately owned e-commerce sites.

BY SUSAN ADAMS

In December 2012, desperately needing money to expand Chewy, his year-old pet-supply startup, Ryan Cohen traveled from Fort Lauderdale to Palo Alto and walked into a half-dozen venture capital firms on Sand Hill Road unannounced. He didn't get past the receptionists. Three months later he tried the same tactic again. "I'm relentless," says Cohen, a college dropout from Montreal. "It felt like it should work." It did not.

Yet four years later Chewy is one of the nation's largest and fastest-growing privately owned e-commerce companies, on track to book revenue of \$900 million in 2016 and more than \$1.5 billion in 2017. Relying on a customer-service strategy Cohen calls "Zappos on steroids," Chewy deploys 416 of its 3,400 staffers to answer phones and texts in round-the-clock shifts at the company's 70,000-square-foot headquarters in Dania, Florida. To ensure speedy delivery to his 3 million patrons, he has built three fulfillment centers, each the size of ten football fields, and has plans to open three more by early 2018.

Chewy has already grabbed 43% of the online sales of pet food and litter in the U.S., just behind Amazon's 48%, according to market research firm 1010data. (Big-box retailers Petco and PetSmart are both in the single digits.) "We want to be the No. 1 pet retailer in the world," Cohen says. He has a long way to go. Chewy has yet to turn a profit, and the way it's spending money to acquire customers, it's not clear it ever will.

Cohen, 31, is compulsive about executing, and about other things, too. "I have OCD," he says—though he's never been diagnosed—while digging into a lunch of steamed salmon and vegetables at Chewy HQ. His diet is primarily two meals: steamed vegetables with fish or chicken. He sleeps three hours a night, reading feedback on

Chewy's Facebook page into the wee hours. Positive reviews, he says, "give me goose bumps."

The son of a teacher and a glassware importer, Cohen fixated early on becoming an entrepreneur. At 15 he discovered the dark art of affiliate marketing, collecting fees for referring customers to e-commerce sites. He got so good at it that he started banking thousands of dollars a month. While looking for a programmer to help build his affiliate sites, he met Michael Day in a Java chat room. Day dropped out of the University of Georgia to join forces with him, and in 2011 they sank \$150,000 of their own money into an online jewelry startup in Florida. But after a visit to a Miami trade show, they felt intimidated by how much there was to learn about gems and precious metals and realized they had no passion for the business.

Then Cohen had an "aha" moment while buying food for Tylee, his apricot-colored teacup poodle. "She's my No. 1," he says, "and I'm married." Cohen, who shares his bed with Tylee and his pregnant wife, sees himself as a "pet parent." Typically, pet parents spend freely on premium foods, often made with ingredients fit for humans, like grass-fed, free-range, hormone-free New Zealand lamb, the main ingredient in K9 Natural Lamb Feast, available on Chewy.com at \$190 for an 8-pound box. Pet parents who don't sleep with their furry offspring can buy a Big Barker pillow-top orthopedic dog bed



Going to the dogs: Ryan Cohen says it was Tylee, his teacup poodle, who inspired the decision to sell pet food instead of jewelry. "For me, it was feeding my baby."

JANEL TOPPIN FOR FORBES



on Chewy for \$400. In 2016 the U.S. pet-product market was projected to hit \$47 billion, according to market research firm Packaged Facts, with e-commerce accounting for as little as 5%.

Betting that the population of big-spending pet parents would grow and that their buying would move online, Cohen and Day sold their jewelry inventory for 80 cents on the dollar, scraped up some more cash from their personal bank accounts, converted their jewelry site into Chewy.com and started buying products from distributors. They found a third-party fulfillment center in Easton, Pennsylvania, and launched

in late 2011 with 50 dog- and cat-food brands, matching online prices with competitors' and offering discounts on first-time orders. Even though Cohen and Day answered customer calls themselves, 24 hours a day, and didn't take salaries, Chewy lost money. But sales grew, hitting \$26 million by the end of 2012.

Though Cohen had struck out in Silicon Valley, Chewy attracted interest from Boston's Volition Capital. In late 2013 Volition invested \$15 million after watching Chewy exceed its growth targets. "Ryan had crushed all his numbers," says Volition partner Larry Cheng.

When Cheng asked Cohen whom he'd most like to have as board chairman, Cohen named Mark Vadon, founder of jewelry site Blue Nile and flash-sale site Zulilly. Cheng made the introduction, and Cohen flew to Seattle to meet with Vadon, who was impressed by Cohen's attention to detail. "He knew the specific economics of his transportation contracts with carriers," says Vadon, who agreed to serve as Chewy's chair and to invest \$5 million of his own money. Five more investors followed, including T. Rowe Price and BlackRock, for a combined total of \$236 million. Cohen won't reveal Chewy's valuation, but longtime e-commerce analyst Sucharita Mulpuru, who recently moved from Forrester Research to Shoptalk, a retail conference organizer, pegs it at \$4 billion.

The capital allowed Cohen to shift his plans into high gear. He decided to take fulfillment in-house, even though he and Day, now Chewy's chief technology officer, knew nothing about warehouse operations. To find experienced staff, Chewy sent out hundreds of invitations to Ama-

ten holiday cards, which cost the company \$940,000 in postage alone.

One pet industry veteran, who says he knows three people who are familiar with Chewy's finances, doubts the company will reach profitability. He says Chewy's average sale is \$75, its average margin after discounts 30% and its average cost of delivery—which Chewy offers for free on orders of more than \$49—around \$12. A competitor estimates that Chewy's customer-acquisition cost could run as high as \$200 per first sale, given that the company pays to appear at the top of Google searches for each of the hundreds of brands it carries. "The bottom line is that Chewy is incredibly predatory, and they're willing to lose money to grow their volume," says the industry veteran.

Confronted with those numbers, Cohen merely smiles. He won't specify his unit economics but says they're positive. He says customer retention is high, as is the lifetime value of those customers. "They're smart to be really aggressive and to push really hard right now,"

says e-commerce analyst Mulpuru. "There's a window of opportunity to be this darling in the e-commerce space. But I do question the lifetime value of their customers. In the age of the Internet it's so easy to switch."

Starting with Amazon, the competition is formidable. Jet.com,

HOW TO PLAY IT

BY WILLIAM BALDWIN




Ransom E. Olds, James Cash Penney, Howard Johnson, BlackBerry and Netscape were pioneers in assembly lines, merchandising, franchising, messaging and browsing. But Henry Ford, Sam Walton, Ray Kroc, Apple and Google made the big money. Investors captivated by the first-mover advantage of Pets.com 17 years ago suffered a spectacular flameout. The winner in online dog food is

going to be a latecomer. You can make a big score with the inventor of an industry (Amazon, FedEx). But balance out any what-if bets in your portfolio with a good measure of what-is. A place to start: **Vanguard Small-Cap Value** ETF.

zon employees on LinkedIn and managed to hire 100 of them. By mid-2014 the company had opened a 600,000-square-foot fulfillment center in Mechanicsburg, Pennsylvania.

Cohen also poured money into customer service. Your schnauzer doesn't like the Blue Buffalo Wilderness Salmon Grain-Free dog food you bought for \$48? Chewy will issue a refund and suggest you donate the food to a local shelter. Canceling your auto-ship order because your Siamese passed away? Chewy sends flowers. Last year Chewy mailed 2 million handwrit-

the bulk e-commerce site acquired by Wal-Mart last year for \$3.3 billion, has moved into pet supplies and is undercutting Chewy's prices on bulk sales of some products. And Petco and PetSmart, with revenue of \$4 billion and \$7 billion, respectively, remain the biggest specialty players in pet retail. But Cohen says he is convinced that e-commerce will eventually take at least 50% of total pet product sales and that Chewy will log more than \$5 billion in revenue by 2020. "We'll be done growing," he says, "when we're 6 feet under." 

FINAL THOUGHT

 "Make your customers comfortable and they will give you their lives."

—PAUL ORFALEA



MARGIN PROPHECY

GETTING BUZZED

IN 2008 HIGH SCHOOL TEACHER **MERRILEE KICK**, NOW 53, GOT THE IDEA FOR BUZZBALLZ, SINGLE-SERVE COCKTAILS THAT COME IN BRIGHTLY COLORED CONTAINERS. TODAY HER CARROLLTON, TEXAS, COMPANY EMPLOYS 60 AND SELLS ITS DRINKS IN 40 STATES. ANNUAL REVENUE IS \$20 MILLION.



How much cash did you need to get off the ground?

I was trying to get \$300,000. I was told, "You're a woman, this is a male-dominated industry, and we don't think you're going to survive."

What about family money?

My husband said, "I will not support this. Don't use any of our 401(k) or savings." I took \$27,000 from an inheritance. I took out a home-equity line of credit for \$69,000. A bank said if I put that amount down, it'd give me \$178,000.

Why didn't your husband want to help?

He's a CFO, and he was terrified I'd lose every penny. He changed his direct deposit from our checking account to a private bank.

How did you get Buzzballz into retail outlets?

I sent a letter to 17,000 convenience stores and 5,000 liquor stores. All of a sudden sales started taking off. —Susan Adams