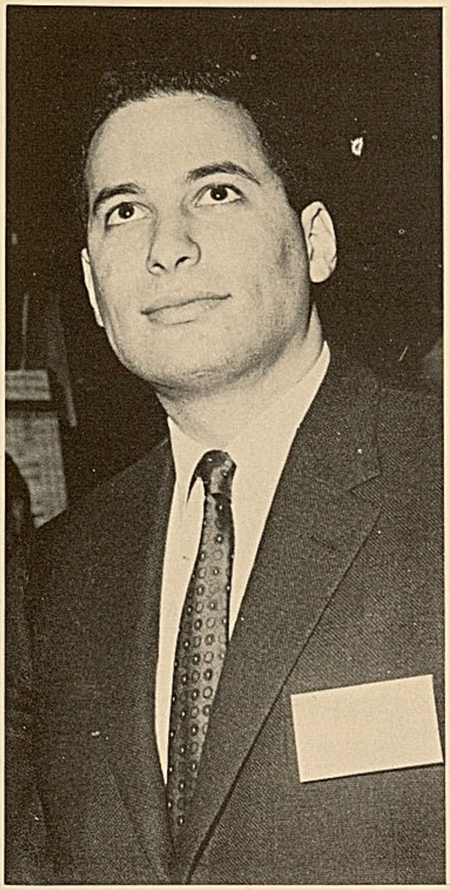
PROFILE OF A GIANT

Following is an address delivered by Leonard N. Stern, Executive Vice-President of Sternco Industries, Inc., to an assemblage of members of the New York Society of Security Analysts on July 29, 1966. The address published here was preceded by a short introductory slide-viewing program which Mr. Stern used to show why the tropical fish hobby has become as popular as it is and why Sternco has been able to use the hobby as a peg on which to hang a 330% increase in sales in the seven-year period 1958-1965.



Leonard Stern, Executive Vice-President, Sternco Industries.

BACKGROUND

My father, Mr. Max Stern, who is President of Sternco Industries, is also President of Hartz Mountain Products Corp. Hartz Mountain Products is the leading supplier of live birds and bird foods in this country. Hartz Mountain and its predecessors were founded by my father in 1926 upon his immigration to the United States from his native Germany. It was his pioneering conviction that live pets and, in particular, the sale of live canaries could be made available to the American consuming public through retail outlets on a mass distribution basis. It is in this respect that my father made his mark and subsequent success in the pet industry in this country. Through the efforts of Max Stern, live canaries, and later other livestock, were, for the first time, offered for sale by the major variety chains across the nation. It naturally became a simple extension from the sale of live canaries and other birds to the sale of their supplies through these high traffic outlets.

In 1959, your speaker entered Hartz Mountain Products and assumed important management functions with that Company. However, at that time, Hartz Mountain's business was primarily devoted to the mass merchandising of cage birds and their related supplies. It was then that the blossoming tropical fish industry caught our fancy, in terms of potential for future development. To begin our penetration of the tropical fish market, we embarked upon a series of acquisitions designed to enable us to establish a line of trademarked tropical fish supplies, as well as a distribution organization capable of distributing these trademarked goods to the major chain outlets. In line with our thinking, in late 1959, we acquired the Longlife Fish Food Company that was to give us our primary trademark position in this newly developing industry. The Longlife name is the leading name in fish foods. Subsequently, a few months later, we purchased the Aquarium Supply Company which gave us our nucleus of service distribution.

Shortly after these acquisitions, Sternco Industries was formed to organize the activities of both these companies and to plan for a coordinated expansion.

Our imagination was sparked by the tremendous potential of this new industry because our business is one whose products can be basically characterized as having qualities of *affordability* and *repeat purchasability*. Ours is a business that will continue to grow with the increase in leisure time, per capita income, and growing population.

MERCHANDISING PHILOSOPHY

In many ways, our philosophy of merchandising can be compared with the merchandising of razor blades and safety razors. The volume is in the blades, not in the razors. But you can't have one without the other. The sale of tropical fish or goldfish to the consumer is not the end of our business, but merely the beginning. The "razor blades" of our business are the fish foods, replacement of tropical fish, remedies, decorations and supplies.

Back in 1960, when we pioneered the idea of national distribution of tropical fish and supplies, the major variety chains and other national retail outlets in this country were unable to secure uniform products, standard pricing, and dependable service from any one supplier. They were obliged to rely on perhaps twenty or thirty local suppliers throughout the country with the ensuing chaos such a distribution pattern creates. Each local supplier had his own line of merchandise most often distinct and different from the merchandise carried by other local suppliers. Most of these suppliers priced their merchandise according to local conditions; guppies in New York could cost the customer 3c each and the same fish in Los Angeles could cost as much as 7c or 8c each. This meant the major chains were unable to engage in centralized buying, and could not guarantee their local store managers uniform or satisfactory service. Back in 1960, there were many areas in this country and in Canada for which no local delivery of livestock and pet supply specialties was available.

With the organization of Sternco Industries this entire picture changed!

Today, any national chain can rely upon local weekly Sternco service at standard prices on a line of quality livestock and dry goods anywhere throughout the United States and Canada. To accomplish this, we have established a system of 17 regional warehouses, 26 branches, and, in areas where it is not profitable for us to operate our own distribution centers, we have established a system of 13 regional franchise distributors who maintain regional service centers within their franchise territories.

To give you an idea of extensiveness of our distribution, today we are servicing 20,000 stores per month . . . making 1,000 stops each day to deliver merchandise and take orders in stores in the United States and Canada.

It is because of this complete distribution system that Sternco Industries enjoys the loyalty and confidence of its important customers coast-to-coast.

The Sternco concept of sales, service and merchandising has created a customer loyalty second to none . . . and the scope is being improved and expanded continuously. No detail is being overlooked . . . from the design and manufacture of special store equipment to the training of store personnel.

Almost all major retailers, who maintain live pet departments today, are Sternco customers.

MANUFACTURING AND BREEDING OPERATIONS

Distribution is one major part of our business. Profitable manufacturing is another. We are proud of our manufacturing facilities located in Harrison, N. J., covering approximately 220,000 sq. ft. In Harrison, all fish foods, aquariums, and store equipment needed by our distribution facilities are manufactured under our own specifications. Expansion and automation of these facilities are presently underway and these improvements should near completion by the year's end.

Millions of tropical fish are bred on our fish farm located outside Tampa, Florida, which covers 200 acres of producing ponds and includes approximately 100,000 sq. ft. of buildings devoted to the breeding and conditioning of tropical fish. We believe that our fish farm is the world's largest and, we think, the most efficiently operated.

Yet, with these extensive facilities we breed less than 20% of our own tropical fish requirements! The balance we purchase from others. We foresee a tremendous potential not only in increasing tropical fish sales, but also additional profit in our increasing ability to supply our distribution system with more Sternco bred tropical fish.

Many interesting and colorful tropical fish are imported to our Tampa facilities from all corners of the world to stimulate further consumer interest in pets. Each new fish, animal, or reptile increases the sales potential for aquariums, cages, foods, accessories, etc. So, our staff spends much time traveling the world in search of new pets, products, and ideas.

The introduction of live pet departments by the major chains was not accomplished simply by the availability of tropical fish and pet specialties on a local service basis. We also found it necessary to develop and make available the type of store fixtures which would lend themselves to the easy mass-merchandising of our products. We are pleased to have been the pioneers then, and still are in the construction and design of such specialized store equipment in both this country and Canada.

Gentlemen, we have set up a typical series of our standard display equipment right here for you to see. You see a simple, attractive display case designed to show off the pets to the best advantage. What you don't see are the lights, the wires, thermometers, heaters, filters, pumps — all of which are scientifically designed to keep the animals and fish in tip-top shape. This is now *standard* equipment with most major retailers. It has been manufactured by Sternco Industries.

Let me remind you that three years ago we did not even make a standard aquarium tank ourselves, and today this intricate store equipment is completely manufactured by our equipment manufacturing division. Sternco Industries bred no tropical fish in 1960 and not a single goldfish. Today, Sternco Industries is an important factor in each of these fields.

During the past year, Sternco Industries has further expanded its approach to the pet specialty market and entered the potentially high volume and lucrative fields of dog specialty supplies through our general pet supply division, named "Delta Products."

In Canada, we operate a fully equipped manufacturing plant located in St. Thomas, Ontario; special livestock facilities in Toronto, as well as branch warehouses in both Montreal and Vancouver, British Columbia.

Now that I've spent a bit of time dwelling on what Sternco Industries has done, let me focus on one of my favorite topics — our customers.

Let me not for one second try to convey to you the impression that Sternco Industries' success is a unilateral success; that Sternco Industries' accomplishments are accomplishments whose credit is solely due to Sternco management. Let me rather leave with you the impression that Sternco's success is no less than Sternco's customers' success; the successful merchandising of our unique products and whatever foresight we have had in the growth of our industry would not have materialized had not our customers felt the same way, and encouraged us in our continued expansion. I am happy to report that our customers still encourage us to expand and continue optimistic as to the future growth of our industry. The interest of our customers in their pet departments is understandable and economically justifiable. The square footage devoted to an expanded pet department is often among the most profitable selling space in the store. Pet departments are usually located toward the rear of the store or, in multi-story units, in the basement. They are purposely located in these areas because of their recognized drawing power.

Junior will drag mother through other numerous departments before finally reaching the Pet Shop. Our development of the pet business has been successful because of our customers' success and our further growth potential is linked firmly with theirs.

We are very proud of our position in our industry and even more proud that we are the innovators and the originators of the mass distribution concept of tropical fish, goldfish and their related supplies.

Another important service we render our customers is active assistance in the training and education of their store personnel in the handling of our unusual products. Sternco personnel, under the direction of our able Educational and Display Director, constantly promote the understanding of livestock care and merchandising to our customers' personnel.

Recent examples of our continued expansion are: the establishment of a new distribution facility in the Baltimore-Washington area, and the expanding of our service and distribution facilities in the Dallas, Texas, area.

Moreover, we are presently contemplating the addition of a local warehouse in the Omaha, Nebraska, area. There are many more areas where our service can be improved and we continue our constant evaluation of all possibilities for expansion.

I think you will be interested to learn that every new K-Mart (the discount store division of S. S. Kresge) and all new Woolco Stores (the discount division of F. W. Woolworth) are opening with complete live pet departments. Each passing week brings new customers to our roster of active accounts.

"Ours is a business that will continue to grow with the increase in leisure time, per capita income, and growing population."

FINANCIAL REVIEW

Now I would like to review with you the gratifying highlights of our financial history, marked by the consistent financial growth of Sternco over the past seven years.

Sales in 1958 were $5,014,000. Sales in 1965 were $21,577,000 . . . a 330% increase! Estimated sales for 1966 should be between $24 and $25-million. Earnings per share have gone from $.07 per share in 1958 to $1.28 per share in 1965 based on 881,752 shares outstanding at the end of 1965 and per share earnings for the year 1966 are estimated at $1.50 per share. I must add that our projections for 1966 profits were made before the July airline strike and it is still too early to judge the total effects of this work stoppage on our business . . . because air shipments play an important role in our distribution of live fish.

Profits have risen from $65,100 in 1958 to an estimated $1,300,000 this year. Stockholder equity for the twelve-month period ending March 31, 1966 has increased by 47½% over the previous year and we estimate that as of December 31, 1966 it will amount to $5,700,000, or $6.50 per share. Our current assets stand at $8,300,000 with only $3,000,000 in current liabilities. I am pleased to report that we have just concluded new agreements with The Prudential Life Insurance Company of America increasing our long term loan to $4-million under favorable terms. It appears our capital requirements have thus been fully provided for and we project that we now have sufficient available capital to continue our expansion program over the next couple of years without the necessity of resorting to additional equity financing.

CONCLUSION

As long as our country's per capita income continues to rise, our population continues to grow, and leisure time continues on the increase, we are convinced that the only restriction on our growth is the imaginative capacity of our management. And, fortunately, our management is young, industrious, and technically competent to solve the problems of our highly specialized industry.

And now I would like to introduce you to our top management team: Mr. Lovitz, President of our major American operating division, The Aquarium Supply; Mr. Segal, Vice-President of our Longlife Fish Food Division; and Mr. Driscoll, our newly appointed Corporate Comptroller.

I thank you.