

Natural Ovens of Manitowoc

Natural Ovens of Manitowoc provides an outstanding example of how one man with drive, persistence, a flair for imaginative marketing and a passionate vision can create an enduringly successful company. Natural Ovens (NO) has managed to grow from almost nothing to a \$9.6 million company with a record of sales growth and profitability that consistently beats industry averages. Furthermore, all this successful growth has been achieved in a mature industry and in a relatively low-growth region of the country.

History and Background

Natural Ovens was founded in 1976 by Paul Stitt, a biochemist and food scientist by training. In the 1960s and early '70s, Stitt had worked in the R & D departments of two large U.S. food companies. He left both positions feeling a high level of frustration with his employers. Each had been unwilling to commercialize the low-cost, nutritionally sound food supplements he had been working on. Fired by the first and then the second company, Stitt had found himself blackballed in the industry for three years in the mid 1970s, unable to get even an interview. He had spent the three years working in his basement on food supplement ideas and, in his words, "trying to get something going."

Eventually Stitt wound up opening a small nutritional food store in Manitowoc, a town of 33,000 seventy miles north of Milwaukee, Wisconsin's largest city. He quickly discovered that he could not find acceptably high quality bread with which to stock the store. Subsequently, a small bakery came on the market, which Stitt bought after persuading a bank to lend him almost all the purchase price. Stitt's wife ran the food store while he ran the bakery, learning about the baking industry on the job.

Patterns of Growth

Product Line Expansion. Since its start in 1976, Natural Oven has experienced steady growth both in geographic market area and in its product line. Product line expansion has usually occurred as the result of repeated customer requests. For example, persistent inquiries about a lighter bread and a higher-fiber loaf led to an introduction of those products in the late 1970s. More recently, muffins and bagels have started being baked by NO to meet customer requests for

those products. From an initial line of five loaf breads, today the company sells 17 kinds of breads as well as rolls, muffins, bagels, granola and pancake and waffle mixes.

Geographic Market Expansion. Natural Ovens began as a small bakery selling to its local Manitowoc market. Since then, NO has used clever marketing tactics and Stitt's talent as company spokesman to crack market after market at minimum cost, relying mostly on careful cultivation and channeling of consumer word-of-mouth. (See **Sales and Marketing** section for further discussion.) NO expanded first to Milwaukee, then the Twin Cities, and finally and most importantly to the Chicago area, which now accounts for over 50% of company sales. Today NO produces more than 20,000 loaves daily from its central Manitowoc baking facility, and distributes its goods in most major grocery chains in Wisconsin and the Minneapolis/St. Paul and Chicago metro areas. The company also sells nationally via mail order, and markets certain ingredients it has developed, such as a derivative of flaxseed, to other bakers around the country.

Performance Figures (for fiscal years ending July)

	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>1995</u> (annualized)
Net Sales (US\$ mill.)	\$5.5	\$6.1	\$7.4	\$8.2	\$8.6	\$9.5
Pretax Profit	(0.6)	3.2%	7.3%	4.5%	5.9%	6.3%
						Industry Average Profit Margin 3%

Key Strategic Issues

Product Quality. Natural Oven's competitive edge has been, in two words, product quality. The founder's background in food science and nutrition have produced a company culture that firmly places product quality as top priority. Quality begins with the company's recipes and production techniques, developed by Paul Stitt and the baking staff over many years of research and development. The company pays top dollar for first-quality ingredients. Store shelf-life of product is normally 1.5 days, to ensure freshness.

To maintain quality control, all production employees, whether in receiving, mixing, baking or packing areas, are inspectors with an explicit mandate to toss out defective items; in the words of production manager Glenn Hietpas, "anyone can throw out anything." Defect rates are tracked and, because each batch is tied to a particular production team, above-average defects in a batch can easily be traced back to individual workers for correction. There are monthly meetings for each production shift to air problems. Except for the highly skilled mixers, workers are regularly

rotated among activities to keep attention levels up. NO is a nonunion shop; all supervisors are on the floor, working the line alongside staff. The company's ethos, often repeated, is that NO charges a premium price and must therefore deliver a premium product.

NO's demanding customers also play a key role in quality control. The company's newsletter, packed into every loaf, includes a toll-free number for mail orders, but many customers use it to call in with comments. Customers also write directly to NO, whose address is given in the newsletter, or speak with store managers who pass the comments on to NO. The company's employees themselves all eat the company's bread at home, providing another constant channel for feedback.

Financial Management. Natural Ovens most trying strategic challenges have tended to revolve around financial management. The company's founder came from a scientific and technical rather than business background, and that is where his interests continue to focus (to this day, Stitt keeps up with ten scientific journals). For its first ten years, the company's finances were managed by Stitt himself, and, he confesses, by the seat of his pants. Money was borrowed whenever needed and repaid whenever available, with no formal cost controls, budgeting or cash flow forecasting. The lack of controls put the company at jeopardy several times, particularly so as it had historically been undercapitalized, with a consequently heavy reliance on bank loans to finance operations and expansion.

The most serious financial challenge came in the late 1980's, when the company moved into new quarters four times the size of its old plant. Construction costs ran well above budget, and additional unexpected fit-up costs were incurred after the company moved in. The result was a severe cash flow squeeze. At the same time, NO's bank was acquired by another bank and new bank management, valuing at \$800,000 the building on which the old management had lent \$1.6 million, promptly called its mortgage note. Bankruptcy threatened.

Even if his bank hadn't insisted on it, the crisis forced Stitt to recognize NO's urgent need for a tough, knowledgeable financial manager. At the bank's recommendation, he hired Jim Peters, a refugee from a Big Six accounting firm who was now a "CFO-for-rent" for several small companies. Ironically for the bank who recommended him, Peters managed to find another bank who not only attached a higher valuation to NO's building but also gave more favorable terms. NO also benefited from the good supplier relations Stitt had nurtured--at one point, supplier payables were stretched to nine months! Since then, the company has managed to grow revenues

3-4 week trial period). The organizational hierarchy is flat and general staff meetings infrequent. Financial results are now regularly shared with employees, who have become co-owners via the profit sharing plan. There is also a tax-advantaged employee savings scheme.

Natural Ovens has a working environment that reflects (and reinforces among staff) its ethos of good health through healthful eating. Employees are provided a free lunch each day, unlimited in quantity, with a menu designed to maximize productivity and minimize employee mood swings through the serving of natural foods low in sugar and preservatives. Smoking is banned. Vending machines purveying mass-market snack foods are not present, nor are their lease revenues for the company (Stitt describes it as "blood money").

Company values are also reflected in employee benefits. "Wellness pay" of an extra half day's wages is paid after each four weeks of work. In contrast, the company provides no sick pay for short-term illnesses. Seventy-five percent of nonsmokers' health insurance premiums are paid by the company, versus only 35% for smokers.

In an industry characterized by high employee turnover, Stitt describes his turnover as "fairly low." Wages are not the highest in the area but benefits, particularly the free lunch, are above average.

The Future

Paul Stitt, now 55, and his wife have recently decided not to grow the business beyond its current regional base. Furthermore, the Stitts plan to pass the company on to a nonprofit foundation, rather than to their children, upon their deaths.