Additional Case 4

Wild Oats Markets, Inc.

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In 2006, Wild Oats Markets, Inc. (Wild Oats), was the number two natural foods retailer in the fast growing organic and natural foods market. With 111 stores in 25 states at the end of 2005 and sales of $1.1 billion, Wild Oats was struggling to return to the fast growth it had once enjoyed in its early years. Between 1995 and 2000, the company grew from $98.5 million in sales to $838 million, for a compound annual growth rate of 53 percent, and at one point, Wild Oats surpassed the industry leader, Whole Foods Market, Inc. (Whole Foods), in number of stores. However, since 2000, Wild Oats' growth was less stellar, averaging 6 percent annually, and the firm reported cumulative losses as a result of restructuring charges. Meanwhile, Whole Foods grew at 21 percent compound annual rate over the same period and delivered healthy profits. Organic food sales in the United States grew from $6.1 billion in 2000 to $13.8 billion in 2005, a compound rate of about 16 percent per year compared to conventional food sales which grew at a 2–4 percent compound rate.[1]

Early in August 2006, Wild Oats reported that sales at existing stores had grown at a slow 1.3 percent annual rate, and attributed the slow growth to greater competition from conventional supermarkets. Indeed, heavy purchases of organic produce by Wal-Mart and Safeway were causing supply shortages. Meanwhile, Whole Foods had just reported comparable store sales growth of 10 percent. Perry Odak, Wild Oats' chief executive since 2001, had been struggling for five years to help the company recover from problems created by a string of acquisitions, but some analysts were beginning to doubt whether he was the man to do it. To add to Odak's challenges, the company was being stalked by billionaire grocery store investor Ronald Burkel.[2] The outlook was, at best, uncertain.

EARLY HISTORY

In 1984, 25-year-old husband and wife team Michael Gilliland[3] and Libby Cook raised a mortgage on Gilliland's mother's home and used cash advances on 17 credit cards to acquire a small convenience store across from the University of Colorado.[4] Gilliland, who had once tried opening a crepe stand in New Orleans, Louisiana, and running a parasailing business, recalled, "I was looking for a business I could run on my own. I had a feel for customer service and I knew what the market liked. I fell into retail." Gilliland, an English major, called the store Stella's after the character in *A Streetcar Named Desire*. Gilliland and Cook's first attempt at retailing proved very successful, and sales grew from $100 on the first day to $4,000 a day within six months. Indeed, the store was so popular that the pair had to hire a bouncer. "It became a very cool place for college students to hang out. The fact that we let our employees drink beer on the job added to the party atmosphere."

In 1985, Gilliland and Cook partnered with Randy Clapp to acquire a second convenience store in Boulder, Lolita's, which also proved success.[5] A third store, added in 1986, was more of a challenge. "My wife worked as a lawyer during the day to keep us

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afloat," said Gilliland. "Thinking we were infallible, we opened a gourmet/natural foods/convenience store called The French Market in the Basemar Center in Boulder. The store lacked any focus, was terribly mismanaged (by me) and was a disaster for two years. Fortunately, Stella's and Lolita's were profitable enough to keep us afloat."[6] In 1987, Gilliland, Cook, and Clapp acquired the Crystal Market, a vegetarian natural foods store that also sold used bicycles, Guatemalan clothing, and quartz crystals.[7] "It was our first exposure to natural foods. Unlike most people in this industry, we didn't start out as vegetarians. We were converted by the business." Gilliland, Cook, and Clapp changed the name of the Crystal Market to Wild Oats Vegetarian Market and converted one of their convenience stores to a natural foods store. "With Wild Oats, we committed ourselves to good, wholesome foods produced in an earth-friendly, responsible manner. It was a lot more fun than the convenience store–type markets we were running. And it also had more of a future." Two more stores were added, bringing the total by the end of 1990 to six. In 1990, Wild Oats instituted its 5 percent Day Charitable Giving Program. One day, each quarter, each store donated 5 percent of sales to a local charity chosen by store management.

RAPID GROWTH, 1991–1999

In January 1991, Gilliland, Cook, and Clapp, opened a store in Santa Fe, New Mexico, their first store outside of Colorado and their first natural foods supermarket. "It was a slam dunk from opening day on. From there on, we just had great momentum."[8] In May of the following year, the company opened two more stores in New Mexico (Santa Fe and Albuquerque), and another store in Colorado, bringing the total for the company to nine at the end of 1992.[9]

As the chain expanded, the founders felt they were beginning to lose touch, and introduced a staff survey to obtain information that they once obtained informally. "In our business we need to keep our staff happy because they're the first line of defense when customers come into the store," said Cook. In response to the survey results, in 1992, Wild Oats created the Wellness Benefit, which allowed employees to claim up to $2,000 per year for anything they thought would benefit their health, including roller blades, a massage, a snowboard, or a visit to the chiropractor. Over 90 percent of Wild Oats employees participated. Many bought a bike, one a vasectomy. A $200 Baby Benefit covering things related to the care of a baby was also introduced.[10] In 1992, Wild Oats generated sales of $36.6 million and operating income in excess of $1 million.

In 1993, Wild Oats opened another store in Colorado, and acquired a store in Kansas City, Missouri. The employee surveys were increased to twice per year in 1993, and became compulsory; participation increased from under 50 percent of store staff to approximately 90 percent. Wild Oats computerized, compiled, and sorted the results by store, yielding a Happiness Index. Gilliland, Cook, and Clapp then read the results, screening out negative comments they considered nonproductive. "It can bum managers out. If there are 30 great comments and 5 negative ones, they'll fixate on the negative," said Gilliland, who personally delivered and discussed results with store managers. "Every round of surveys brings a surprise," said Gilliland. For example, in one survey, the staff at the store with the best working conditions and most benefits yielded the worst complaints. "We'd assumed it would be the happiest store, but it wasn't," said Cook. In response to feedback, the company introduced a host of changes, including profit sharing, additional training, and other benefits. "Each round brings in about 20 ideas and keeps the corporation in touch with the front lines. For example, I would never have thought of the Wellness Benefit. My idea of what's important is different from an hourly worker's," said Gilliland. Gilliland thought the surveys therapeutic, citing a decline in store staff turnover since their inception.[11]

The company launched a frank, award-winning handbook for new employees in 1993. It began with "A Long, Strange Trip," a history of Wild Oats by Gilliland with the tone of a letter to a friend, and highlighting both the company's early successes and its failings. "Even though we are getting larger, Wild Oats is still pretty much a mom-and-pop store. We wanted people to know it is still owned by the first three people who bought it."[12] In 1993, Gilliland and Cook were named Entrepreneurs of the Year by *The Denver Business Journal*.[13]

In 1994, two stores were acquired in Las Vegas, Nevada, and another was opened in Colorado.[14] In response to its employee survey, Wild Oats introduced a profit sharing plan in which store employees, referred to as "wild things,"[15] received 15 percent of profits exceeding a predetermined monthly net profitability target.[16] "To the average cashier, it might amount to $1 in profit sharing every month. As you progress to higher positions at Wild Oats, the incentives increase," said Mary Beth Lewis, chief financial officer. Wild Oats hoped the plan would increase morale and productivity, boost recruitment, and decrease turnover. Each store posted its profit and loss statement to help employees track performance.[17] Revenues for 1994 reached $65.2 million and operating profits $2.6 million. Funding for the expansion was provided by Chase Venture Capital Associates.[18]

The pace of expansion quickened in 1995 with the opening of five stores (Colorado (two), Kansas, California, and New Mexico) and the acquisition of a further two in northern California. The acquisitions were converted to the Wild Oats Community Markets banner. The activity put a significant strain on the company and, although sales jumped to $98.5 million, operating profits fell to $0.8 million and debt mushroomed. However, the expansion continued. In 1996, the company acquired Alfalfa's Markets, Inc., an 11-store chain generating annual sales of $86 million for $39.1 million in cash and stock. Alfalfa's was Wild Oats' biggest competitor in Colorado, with six stores, and operated two more stores trading as Alfalfa's, in Santa Fe, New Mexico, and Seattle, Washington, and three stores under the name Capers in Vancouver, British Columbia.[19] Wild Oats also acquired a three-store chain in Utah in 1996, and opened a further seven stores. Two underperforming stores were closed the same year. Wild Oats retained the Alfalfa's and Capers names but converted the Utah acquisition to the Wild Oats banner. Alfalfa's and Wild Oats' headquarters in Boulder were consolidated into one. The acquisition of Alfalfa's, begun in 1995, made Wild Oats the number two in the industry behind Whole Foods, displacing Fresh Fields, which had been founded in 1991 and rapidly grown to the number two spot.

To fund Wild Oats' growth, in October 1996 the company made an initial public offering of 1.4 million shares at $25 per share, raising $31.4 million. The stock opened at $25.75 per share and fell immediately. Gilliland commented, "My net worth dropped significantly. It was a shock because it was such a hot deal, supposedly, up until the last minute. The funny thing is they didn't even give us a chance to screw up. We've exceeded all projections as far as comps and profits and everything else."[20] After the offering, Gilliland, Cook and Clapp owned 50.4 percent of the company.[21] The total store count reached 40 by the end of 1996, sales jumped to $192 million, and operating profits before exceptional items to $11.6 million. After the acquisition, Wild Oats overtook Fresh Fields Inc. to become the second largest natural foods chain behind Whole Foods, and operated in eight U.S. states plus Canada. In June 1996, Whole Foods agreed to acquire Fresh Fields.[22]

Wild Oats stores and Alfalfa's stores were similar in terms of merchandising but not identical. Wild Oats stores were considered better in terms of natural living (e.g., vitamins and supplements, toiletries) and Alfalfa's stores had the edge in perishables (e.g., produce, prepared foods). Wild Oats tried to capitalize on these differences, encouraging the stores to share best practices.[23] To this end, Wild Oats retained Hass Hassan, the founder, CEO, and president of Alfalfa's to be president of Wild Oats. Born in Pakistan, raised in London, and a life-long vegetarian, Hassan founded Alfalfa's in Boulder in 1979. Hassan reportedly clashed with Gilliland, resigning after less than a year. The management style of Wild Oats was more "ready, fire, aim" and the management style of Alfalfa's was more "process-oriented and maybe a little less dictatorial," according to Gilliland. "Both ways [had] their advantages and disadvantages, and I think everyone [tried] to come up with a happy medium."[24]

Wild Oats' expansion did not go unnoticed by the industry leader, Whole Foods. In the company's annual general meeting in March 1996, Whole Foods' chairman, John Mackay, reiterated his commitment to growth at the expense of short-term profitability to prevent competition from getting established. Mackey commented, "It's important to establish dominance. If we do, its unlikely competitors like Fresh Fields and Wild Oats can succeed. We don't mind competition as long as we have overwhelming firepower."[25] In June 1996, Whole Foods announced that it was to acquire Fresh Fields. At the end of 1996, Wild Oats competed with Whole Foods in California and in Florida.

In January 1997, Whole Foods announced that it would open a store in Boulder, Colorado, and intended to open in other markets where Wild Oats competed. Whole Foods' president, Peter Roy, explained, "We're expanding into Boulder because it is an excellent market and it only has one major player. Obviously, our margins in Boulder will not be the highest in the company but that's OK. Whoever does the best job, has the best service and operates in the best location will win the battle. We believe that we're cheaper. Our entry into the market will help consumers. It will bring prices down in many of the stores in Boulder."[26] Wild Oats' stock dropped 26 percent, to $13 a share.

Wild Oats' Mary Beth Lewis commented, "There's plenty of growing room in this business for both of us. The competition between us isn't rational. Why should we beat each other up?" Mackay's view was clear: "It was Wild Oats that first entered our markets in San Francisco, Los Angeles and Chicago. I'm damned if I always want to be the hunted. I've gone into Boulder because I think I can make money there. I also think I can blow up the bomb factory. Boulder is a stronghold of Wild Oats, one of their key markets where they used to be able to extract high profits. Now, no longer. One of my aims is to weaken their company and lessen the competition I face. We're a much bigger and stronger company and can sustain a war of attrition far longer. If we have to fight a war—and they fired the opening shots—I'll fight to win."[27]

Mary Beth Lewis expressed the view that the move would not harm Wild Oats: "Additional stores tend not to take customers away so much as attract new customers. We don't feel particularly threatened by them coming to town despite the tone they've taken with us. Our stores are concentrated in the Western U.S. We are the largest customer from the distributors we buy from. They are locating a single store a thousand miles away from their next nearest store. I don't believe that they can offer lower prices than us." Whole Foods planned to open in a 39,000-square-foot location. Typically, Whole Foods stores generated sales of $10 million in their first year. Wild Oats operated three stores of 25,000 square feet, 13,000 square feet, and 6,500 square feet in Boulder, with combined sales of between $20 million and $25 million, almost 10 percent of total company sales.[28] In response to the announcement, Wild Oats immediately remodeled its two nearest Boulder stores.[29]

Despite the threat, analysts remained bullish on Wild Oats' prospects. Gary Giblin and Mary Cartwrite of Smith Barney identified that Wild Oats' contribution at store level was higher than Whole Foods', but that it had higher central overhead. They wrote: "The good news for [Wild Oats] is that its efficient store model is structural and enduring whereas its lack of corporate expense leverage is temporary. [Wild Oats] has about as good a mousetrap as [Whole Foods]. We find [Wild Oats'] share valuation compelling. On the key multiples, it is cheaper than [Whole Foods]. Furthermore, it is cheaper than the broader comparable universe of category killer retailers and trades at a deep P/E discount to its growth rate."[30]

In 1997, Wild Oats opened seven new stores and made four small acquisitions, adding two stores in Eugene, Oregon (Oasis Fine Foods); two in Florida; two in Memphis, Tennessee; and three in Arizona. The company retained two of the retail brands acquired (Oasis Fine Foods and Sunshine Grocery) and converted the remaining stores. The company also announced plans to open in Chicago in the first head-to-head competition with Whole Foods.[31] Wild Oats typically paid between two and four times recast store contribution for acquisitions.[32] Margins at acquired stores decreased initially and increased after approximately six months.[33] After acquiring a store, Wild Oats performed a minor remodeling costing approximately $200,000,[34] including décor. The store remained open during the 8- to 16-week remodel period.[35] If the store name was to be changed, the new name was not applied until the remodeling was complete.

Analysts were generally supportive of Wild Oats' acquisition strategy. Mark Hanratty and Adam Cherry of Paine Webber thought that Wild Oats had "the management and systems in place to integrate its recent acquisitions."[36] Gary Giblin and Lisa Cartwright of Smith Barney thought that Wild Oats had integrated gently, "in keeping with its enlightened human resource management and focus on maintaining store level morale and productivity among the truly value-added employees integral to successful natural foods retailing."[37] And one analyst thought that Wild Oats would be shielded from the negative surprises acquisitions "sometimes reveal" because it had made many small acquisitions, creating "a diversified portfolio effect."[38]

Wild Oats looked for store locations offering 15,000 to 35,000 square feet for its supermarket stores and aimed to be an anchor tenant in a neighborhood mall or a high-visibility stand-alone store. For its urban stores, the company looked for 5,000–15,000 square feet in dense residential or commercial areas with high foot traffic. Within these broad parameters, the company was flexible with respect to store format, enabling it to customize its stores to specific sites and local markets. The company believed that this approach allowed it to reach a broader customer base.[39]

The company was also flexible in its merchandising approach, with some stores having a gourmet emphasis, some more mainstream, and one store at least being strictly vegetarian.[40] "I'm a great believer in figuring out where customers are and walking with them. It doesn't do you any good to put a hard-core vegetarian market in the middle of Pasadena, [California,] because you're going to go out of business. In Santa Monica, [California,] for instance, we have a more affluent customer base. We took the bulk bins out. Those customers weren't going to stand around and scoop out flour. But we can sell a $50 bottle of olive oil," said Gilliland.[41] To this end, Wild Oats offered both organic items and non-organic items, aiming to be 80 percent organic. Wild Oats set specific standards for its food products (i.e., preservative-free, organically grown, cruelty-free, not bioengineered, non-radiated, free of artificial coloring and flavoring, free of chemical additives) and natural living products (i.e., preservative-free, cruelty-free, formaldehyde-free, no aluminum packaging, free of artificial coloring and flavoring, full ingredient disclosure, limited animal ingredients).[42] Wild Oats also emphasized locally-grown produce.[43]

The company operated a central purchasing function, which set product standards and negotiated with vendors for volume discounts. Store department managers then decided what to order, allowing each store to customize its offering to its local market. The company had over 3,000 suppliers in 1997, but 20–25 percent of purchases were from one national distributor,[44] United Natural Foods Inc. (UNFI). Most goods were delivered direct to store by local distributors, but the company operated a small distribution center in Denver, and six commissary kitchens to produce deli food, baked goods, and take-out food for delivery to stores over a 100-mile radius. Wild Oats was often one of the highest-volume customers of a regional wholesaler or regional distributor even if it had only a few stores in a region.[45]

In 1997, Wild Oats had between 100 and 150 private-label items in approximately 15 categories, and planned to double this. Private-label lines included chocolate bars, gourmet breads, salsa, salad dressings, chips, pretzels, tortillas, pasta, pasta sauces, oils, canned fruit, and vitamins. Private-label items offered 5 to 10 percent higher margins than branded goods. Private label was approximately 3 percent of sales in 1997, and plans called for this to expand to 10 percent. The strategy was praised by analysts who suggested that natural foods customers were less loyal to brands than conventional foods customers.[46]

Wild Oats' average customer was female, 32 years old, with 15 years of education, a household income of $34,000, and a house worth $140,000;[47] 85 percent of Wild Oats' customer base was female.[48] Wild Oats didn't invest much in advertising except when opening a new store. The emphasis was more on store-level promotions, and in-store experience. Wild Oats aimed to make shopping "theater" in a fun and educational environment, with cooking classes, live music, children's events, harvest fairs, barbecues, and dog washes. Some stores had in-store nutritionists and massage therapists; all offered educational information on food. Stores were festooned with product brochures and recipe cards, and tasting stations allowed consumers to try new products. Most stores also had seating areas and offered juices, while some offered full café service.[49] Wild Oats produced monthly advertising flyers promoting between 30 and 50 items, and distributed them in stores, through newspapers, and sometimes through direct mail.[50] It even tried a major buy-one-get-one-free promotion in 1997.[51]

Wild Oats, like many other natural foods retailers, had relatively unsophisticated information systems compared to most conventional food retailers. In 1997, Wild Oats was installing a point-of-sale system and new inventory control software. It had not established electronic data interchange with its vendors.[52] In 1997, Wild Oats began Fresh-at-Five, a scheduling program to increase store labor hours at peak shopping times. This had been common practice for years for conventional food retailers.[53] Twenty percent of Wild Oats' employees were part-time in 1997, compared to 50 percent for conventional food retailers.[54]

In 1997, Wild Oats launched a $50 Fix-It Fund, available to any store employee to address a customer complaint,[55] and a $30 Birthday Dinner Benefit was introduced. The company instituted its Charity Work Benefit, paying employees for 1 hour of charity work per every 40 hours of Wild Oats work, up to 52 hours per year.[56] It also established Wild Oats University, a training program involving, among other things, a natural products test that employees had to pass before working on the store floor and a refresher course in order to improve retention of important information.[57]

In 1997, Cook began reducing her time commitment as vice president and general counsel in order to pursue other entrepreneurial activities.[58] Gilliland said of their business partnership, “From the start, she has been the voice of reason. I come up with all these ideas, some of which aren’t too great, and she acts as a grounding influence. It’s a good balance.” In December 1997, Wild Oats completed a common stock offering, raising $46.5 million net, and Gilliland and Cook’s ownership decreased from 22 to 15 percent each.[59]

In February 1998, Whole Foods opened a new store in Boulder, cutting prices by up to 20 percent and introducing a line of private-label items. Wild Oats’ sales decreased by 15 percent in Boulder.[60] Rumors abounded that Whole Foods might attempt a takeover of Wild Oats. In May 1998, Wild Oats adopted certain “poison pill” provisions that required potential acquirers of Wild Oats to negotiate with the board of directors and discouraged coercive takeover attempts.[61] Wild Oats also began offering discounted stock options (15 percent) that vested after five years as part of the profit-sharing plan. Wild Oats’ employees with one year of service were eligible.[62]

Wild Oats’ pattern of small acquisitions and geographic expansion continued in 1998. In six separate transactions, seven stores were acquired in seven states, four of which were new to Wild Oats. A total of eight new stores were also opened, including Wild Oats’ first store in Texas, home state of Whole Foods. Wild Oats entered a total of six new states in 1998. By the end of 1998, the company stores operated under seven banners: Wild Oats Community Market; Alfalfa’s Market; Beans, Grains & Things; Ideal Market; Oasis Fine Foods; Sunshine Grocery; and Uptown Whole Foods.

In 1998, the founders of Wild Oats launched a $3 million foundation. The first project to be funded was the creation of a wellness center adjacent to a Wild Oats store, offering alterative healing remedies and more, available to employees for free and to members of the community for a nominal fee.[63] By 1998, Wild Oats had launched the Wild at Heart Foundation, a foundation supporting humanitarian and environmental groups. In 1998, Wild Oats gave at least 7.5 percent of earnings to nonprofit humanitarian and environmental groups.[64] By 1999, Wild Oats had created a second wellness center.[65]

On the merchandising front, in 1998, Wild Oats launched its Dinner-A-Go-Go program, a home meal replacement offering with foods prepared in stores, in commissaries, and by third parties.[66] The company also launched the Wild Card Shopper customer loyalty card program. Half of its customers signed up for a card, but Wild Oats discontinued it after a survey found that customers thought the program was too much like the programs offered by conventional supermarkets.[67] Gilliland, on the Wild Oats Web site, invited customers to return their Wild Cards to stores, where they would be disposed of in an environmentally safe manner, quoting W. C. Fields, “If at first you don’t succeed . . . quit before you ruin what you’ve got.”[68]

In 1998, Wild Oats had 10 regional directors responsible for the stores in their area. Store managers reported to the regional director and typically had 10 department managers reporting to them in their stores. Because of the wide size range of stores, Wild Oats had between 25 and 200 employees per store.[69]

By the end of 1998, Wild Oats operated 63 stores under seven banners in 18 states plus Canada. It generated sales of $398.9 million, more than double 1996 levels, and operating income of $18.7 million, more than four times 1996 levels. Gilliland and Cook were named Retail Entrepreneurs of the Year by *Chain Store Age,* a monthly newsmagazine for corporate executives in retail.

In 1999, Wild Oats went on a major acquisition spree, buying 7 Nature’s Fresh Northwest stores in Portland, Oregon; 4 Wild Harvest outlets in Boston, Massachusetts; 11 Henry’s Marketplace stores in San Diego, California; and 9 Sun Harvest Farms stores in Texas, as well as 3 operating stores in Tucson, Arizona. At the end of 1999, after acquiring a total of 41 stores and opening a further 8, Wild Oats had more stores than Whole Foods. Wild Oats retained the banners of acquired stores, and operated under a total of 12 banners in 1999.[70] Gilliland envisioned a “federation” of regional retailers rather than a national chain of cookie-cutter stores operating under one banner: “Our customers have an anti-chain mentality. They have more of an emotional attachment to the store than to the local Safeway. Maintaining that community connection is very important to us. We try to customize each store to the individual market and take advantage of our size in systems operations buying."[71] In 1999, Wild Oats, converted some of its smaller stores in less expensive locations to People's Markets stores with fewer stock-keeping units (SKUs), lower operating expenses, lower prices, narrower profit margins, the feel of a 1960s co-op, and a name evoking Maoist China.[72]

In 1999, Wild Oats had approximately 400 private-label items, and planned to double this within a year. Private label represented approximately 8 percent of sales, and plans called for this to increase to 20 percent. By 1999, Wild Oats had arranged its Natural Living section to be more accessible, arranging products by function such as cardiovascular health, respiratory health, digestive health and cleansing, and immune system health.[73] In 1999, Wild Oats stopped selling North Atlantic swordfish, marlin, orange roughy, and Chilean sea bass because of conservation concerns.[74] It began offering turtle-safe, certified shrimp—shrimp caught in turtle excluder devices. Wild Oats had been introduced to these devices at its annual Wildstock conference. "It's our version of Woodstock. Every store manager and perishable department manager is invited, and about 120 vendors set up and display their wares."[75]

Wild Oats had a significant number of stock-outs in 1999, for which it considered United Natural Foods Inc. responsible.[76] Sales of $721 million and operating profits of $34.9 million were double 1998 levels. However, the balance sheet was burdened with $80 million of debt, and cash was tight.

CONSOLIDATION 2000–2006

In 2000, the strategic focus shifted to increasing sales per store and 17 underperforming stores were closed. Wild Oats began repositioning itself to attract more mainstream shoppers, increasing the size of its stores and the number of gourmet items, prepared foods, housewares and gift items it offered. One analyst asked, "You seem to be adding a lot more Gucci to the mix. Does this mean that Whole Foods has had it right all along?" "Wild Oats has learned from its competitors and witnessed a convergence of the natural foods and conventional foods markets," said Jim Lee, chief operation officer.[77] In 2000, the company took a charge of $42 million for restructuring, and also wrote off a $2.1 million investment in an e-commerce nutritional company.[78] Operating profits for the year were down to $29.4 million on sales of $838 million, and, because of restructuring charges, the company reported a net loss after taxes of $15.0 million. On December 30, 2001, the company found itself in breach of its financial covenants.[79]

In March 2001, Perry Odak, former chief executive officer of Ben & Jerry's Homemade Inc. was hired as CEO and president. He was faced with a wide variety of stores, 65 percent of which had been acquired, ranging in size between 2,700 square feet and 45,000 square feet; multiple retail brands; weak information technology (IT) infrastructure with a proliferation of systems; a huge number of SKUs, many slow moving; a large number of vendors; pricing inconsistencies across stores; a lack of operational controls; and high out-of-stocks.[80] In the last quarter of 2001, Odak took another $50.4 million restructuring charge.[81] In the next 18 months he replaced the majority of the company's management team; started an SKU rationalization program; switched distributors; centralized buying, merchandising and pricing; introduced operational controls; began installing a data warehouse; and initiated a store relocation program.[82]

The first major change after Odak took over was the Fresh Look program. This involved increased marketing,[83] weekly eight-page flyers instead of monthly, price cuts of between 5 and 25 percent on 2,500 items,[84] and increased staffing to improve service and attract a broader range of customers. The program was rolled out to 44 stores by November 2001. The company reported a larger than expected loss in quarter 2 of 2001, and the chief financial officer resigned, to be replaced by Ed Dunlap, who had experience at Gap Inc. Steve Kaczynski was appointed senior vice president of merchandising, coming from Giant Foods Stores, a large traditional grocer.[85] A banner consolidation program was initiated,[86] and a data warehouse program started. In November 2001, Gilliland and Cook resigned from the board. Wild Oats reported an operating loss before exceptional items of $4.5 million for 2001 on sales of $893 million.

In the first quarter of 2002, Wild Oats returned to profitability. In April 2002, the company unveiled a new supermarket format in a store opened in

California. It included expanded fresh produce and deli areas, lower shelving, reading areas, and new décor.[87] It used a new computerized planogram system for merchandising that was to be applied in all stores. Andrew Wolf, an analyst with BB&T Capital Markets, questioned the wisdom of this mass-market approach, citing Whole Foods' success. He remarked, "Whole Foods is a different economic model from a mass merchant, and is much more assortment driven."[88] Wild Oats initiated an SKU rationalization program to eliminate slow-moving items and replaced them with higher-margin value-added products such as marinated and stuffed meats.[89] The company also commenced IT programs for EDI, automated reordering of merchandise,[90] direct-store delivery receiving, and labor scheduling.[91] In September 2002, the company raised $48.3 million in equity.[92] Operating profits were $18.8 million in 2002 on sales of $919 million. Wild Oats' primary competitor in 2002 was Whole Foods, with which it competed in 70 percent of markets served. Wild Oats claimed that it had higher product standards and more competitive prices than Whole Foods.[93]

On June 14, 2002, Wild Oats announced that it was to switch its primary distribution agreement from United Natural Foods Inc. (UNFI) to Tree of Life Inc. (TOL), effective September 2002. TOL was expected to supply 30 percent of Wild Oats' merchandise.[94] The switch proved problematic, and the company suffered logistics problems and out-of-stocks in 2003. Remodeling stores and the SKU reduction program also proved disruptive, and operating profits fell in 2003 to $9.2 million from $18.8 million the year before. In 2002, Wild Oats and Whole Foods overlapped in 75 percent of markets served.[95]

In January 2004, Wild Oats switched the distribution agreement back to UNFI. A month later it opened its first distribution center, in Riverside, California, to supply fresh produce, private-label groceries, and some other items to the majority of stores west of the Mississippi.[96] In June 2004, the company raised $115 million in convertible bonds, $25 million of which was used to repurchase company stock.[97] In August, the company announced that it was to open health food sections in five Stop & Shop supermarkets.[98] The company made an operating loss of $6.3 million in 2004, which it attributed to disruptions in its logistics pipeline and competitive pressures.[99] Sales passed the billion-dollar mark, at $1.05 billion. Wild Oats also changed its accounting for deferred taxes in 2004, reporting a net loss after taxes of $40.0 million for the year.

On March 31, 2005, the company organized a revolving credit facility of $100 million secured on some of its assets with Bank of America.[100] In June 2005, Wild Oats received a disappointing CCC+ rating from Standard & Poor's on its convertible bonds.[101] However, in the second quarter the company returned to profitability. The company began a merchandising program to broaden the appeal of its product line to attract more mainstream shoppers. It was to offer lower-priced natural products and more gourmet lines, and ethnic offerings.[102] Some analysts questioned this approach, recalling that Wild Oats had tried this before and been unsuccessful. Many of the logistics challenges seemed to have been solved in 2005, and UNFI accounted for 37 percent of the company's purchases.[103] The company reported an operating income of $14.8 million for the year on sales of $1.12 billion.

THE WAY AHEAD: 2006–?

In April, 2006, Wild Oats opened its newest 37,000-square-foot prototype store, and planned to open a 40,000-square-foot store in 2007.[104] The cost to open a new leased store ranged from $2 to $6 million in 2006,[105] while a major refurbishment cost $1 million. Early in August 2006, Wild Oats reported comparable store sales annual growth of 1.3 percent, compared to 5.4 percent a year earlier. By comparison, Whole Foods reported comparable sales up by 10 percent.[106] Wild Oats attributed the slowdown to competition from conventional supermarkets. Perry Odak, chief executive officer since 2001, had long argued that the entry of conventional supermarkets into the organic category was good for specialists, but in 2006, the benefits were far from clear.[107] During the summer, there was a shortage of organic items, such as apples and milk, which was attributed to heavy buying by Wal-Mart and Safeway. Washington State, which produced two-thirds of U.S. certified organic apples, reported growth in demand of 53 percent between the 2003–2004 and 2004–2005 seasons,[108] and prices on some lines of organic produce were reported to be double that of conventionally produced products.

To add to Odak's challenges, in August 2006, Wild Oats was under threat from billionaire grocery store investor Ronald Burkel, ranked 335th in

Forbes' ranking of the world's richest people, who was buying Wild Oats stock. Wild Oats had poison pill provisions in place, preventing anyone from acquiring more than 15 percent of its stock, but Burkel had accidentally exceeded this and reached 17.3 percent. The company had agreed with him that he would limit his purchases to 20 percent.[109] At the time, Burkel was also rumored to be buying a significant stake in Supervalu, another large supermarket chain in the United States.[110]

With cash tight, Odak had limited space for maneuver. He planned to add 10 more stores in 2006, and refurbish six at a cost of $1 million each.[111] He was also driving up the number of private-label Wild Oats–branded items sold through the chain and looking to expand the company's footprint by selling these lines through other retail channels. The company was targeting 1,700 private-label SKUs by calendar year-end 2006,[112] comparable in number to Whole Foods,[113] and up from about 1,000 SKUs in 2000. Wild Oats lines were already selling through Peapod.com, Amazon.com, and in some Stop & Shop supermarkets in the Northeast in August 2006, and Odak was negotiating with more channels to expand this initiative.[114] Whether this would be enough to restore the retailer to its former glory was not clear.

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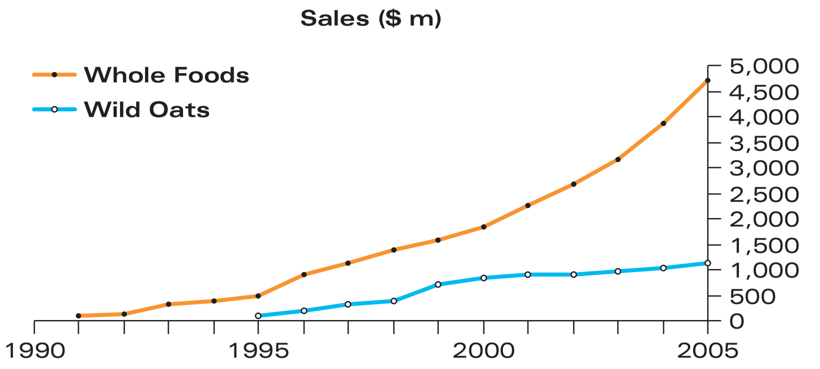
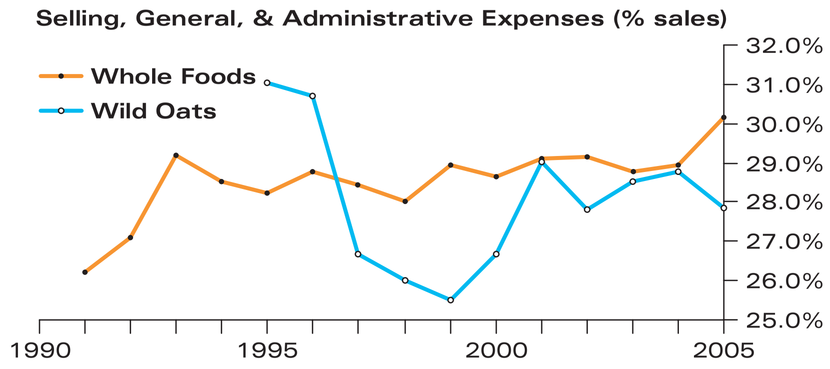
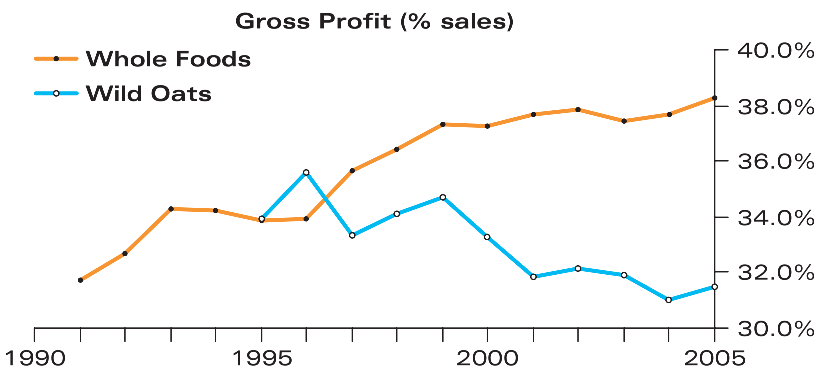
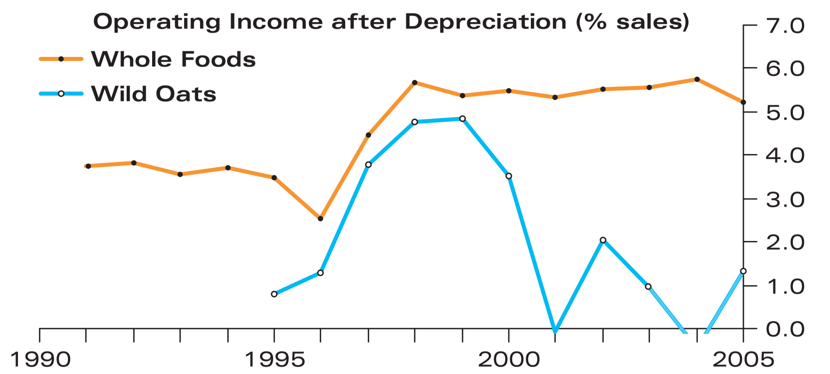
Appendix: Whole Foods and Wild Oats Financial Analysis









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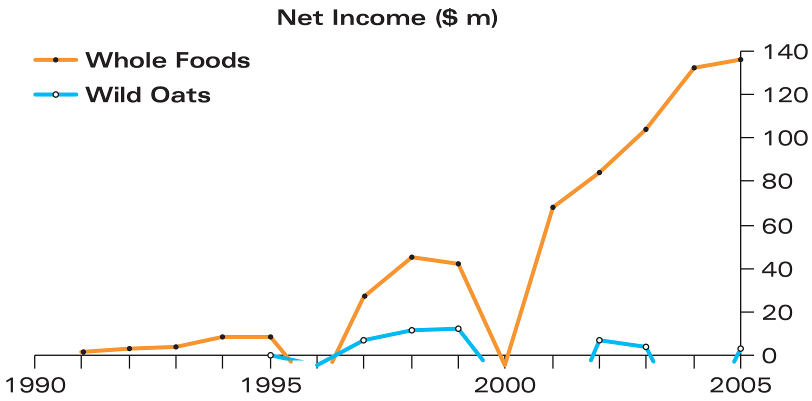

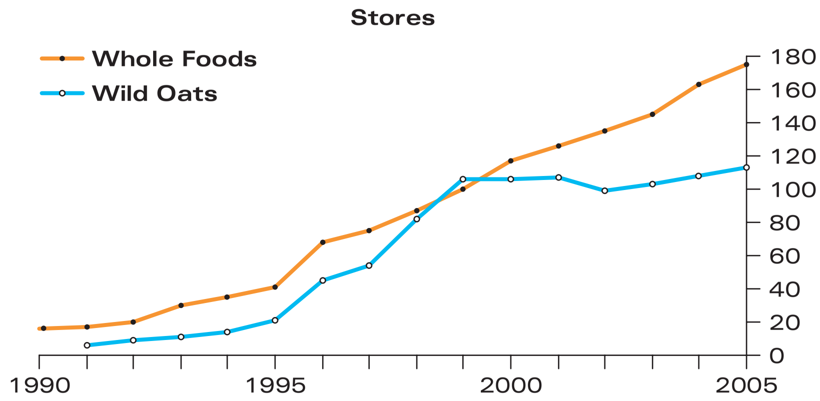

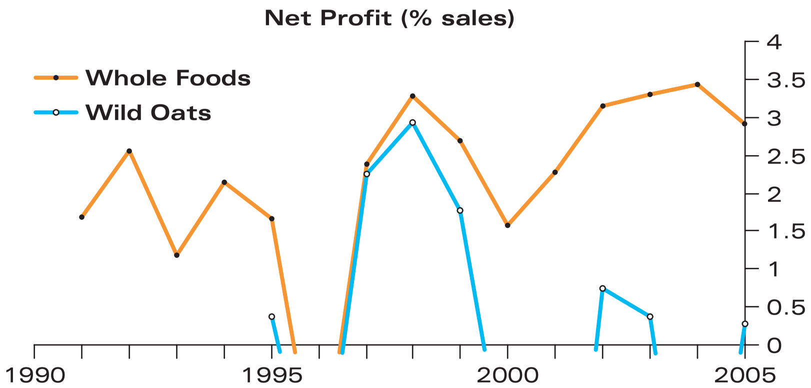

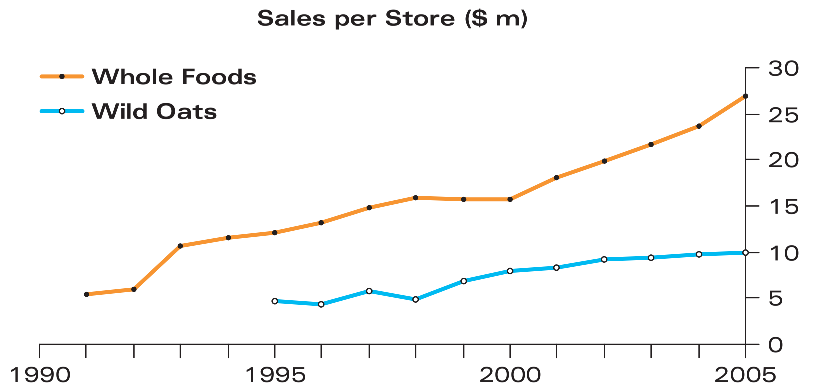

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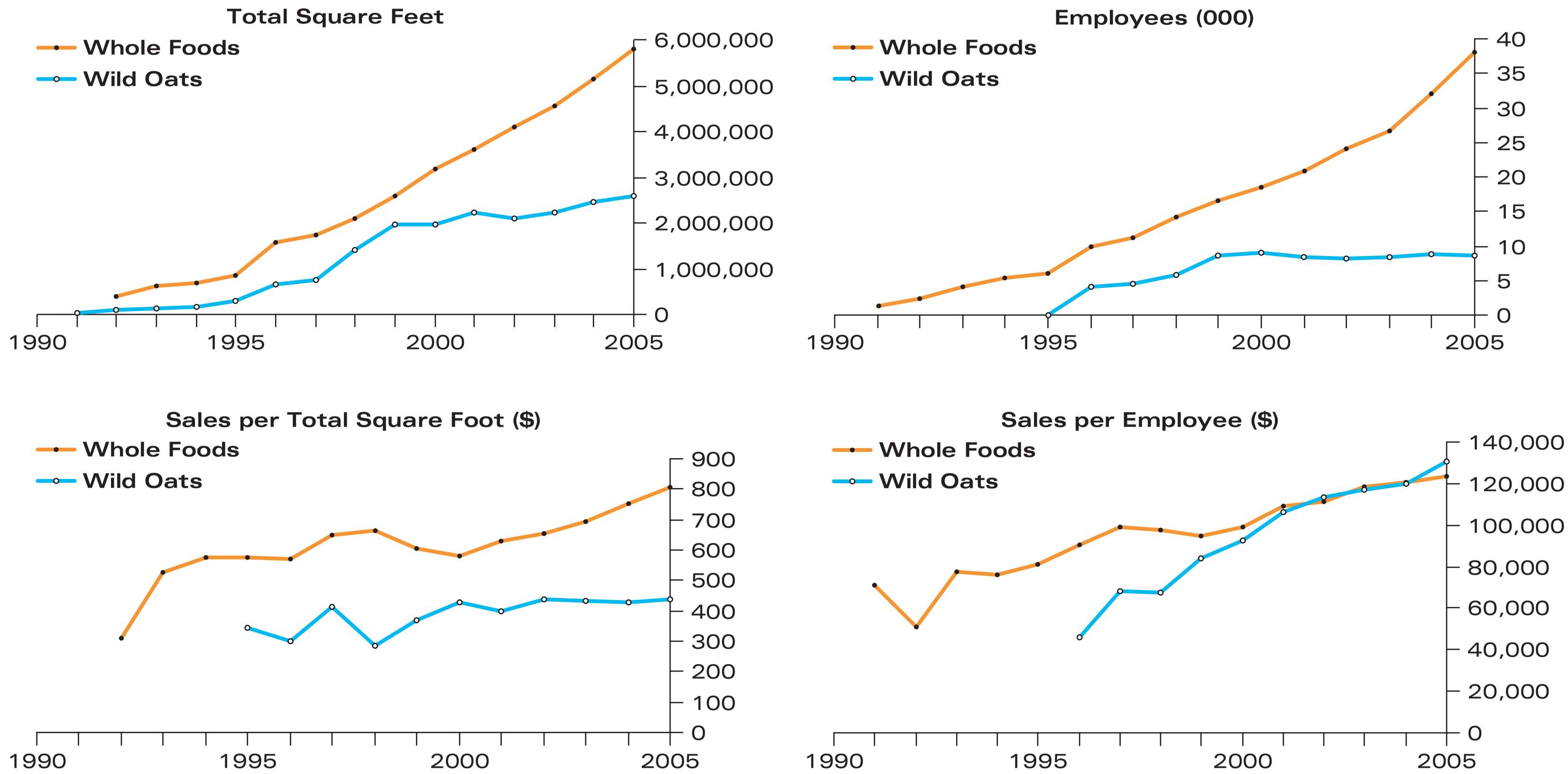

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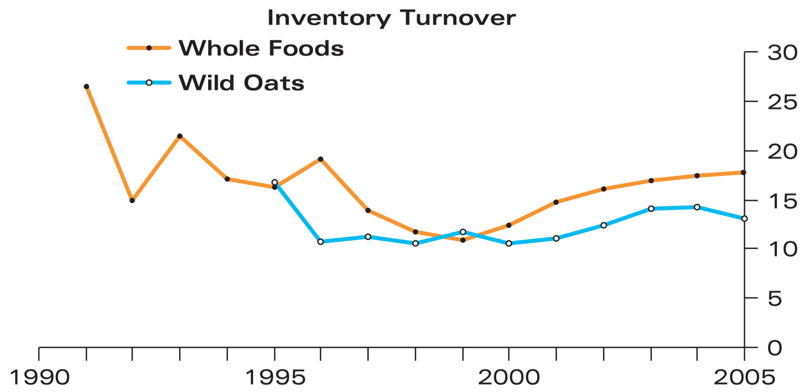

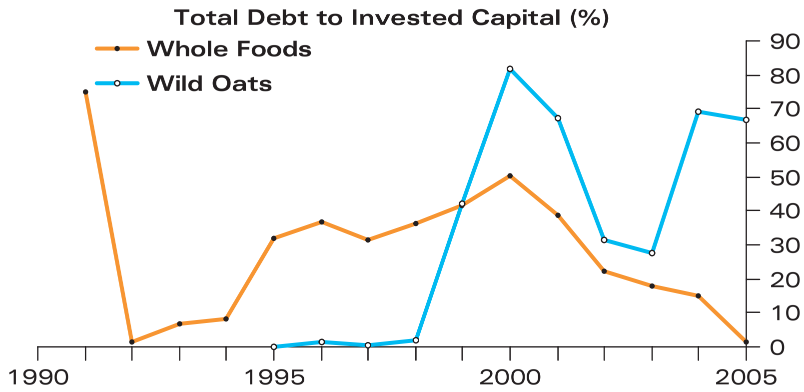

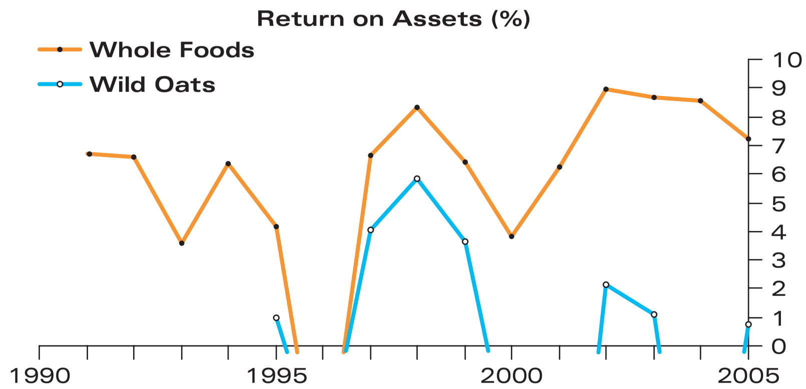

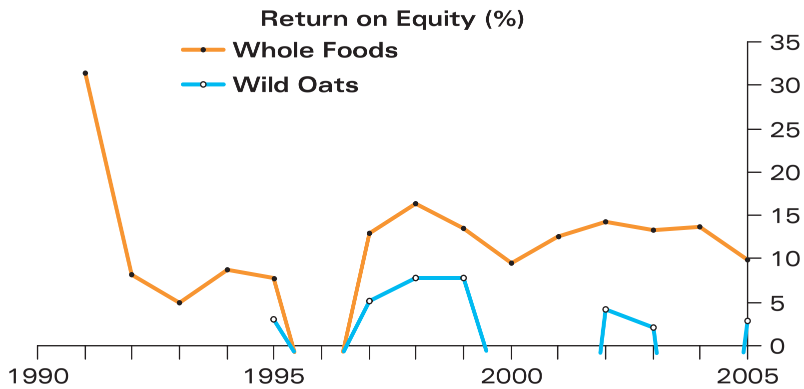

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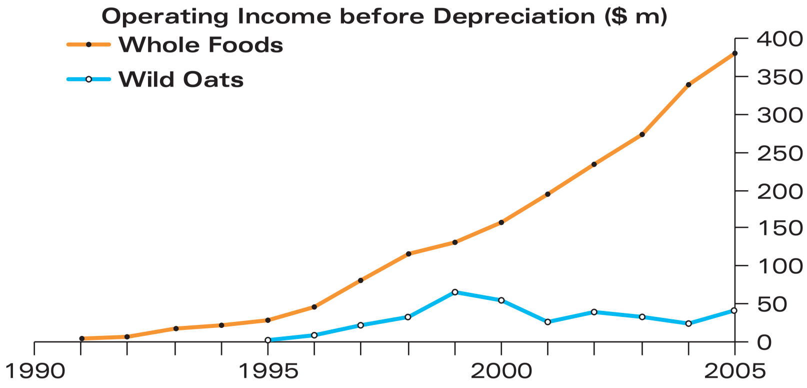

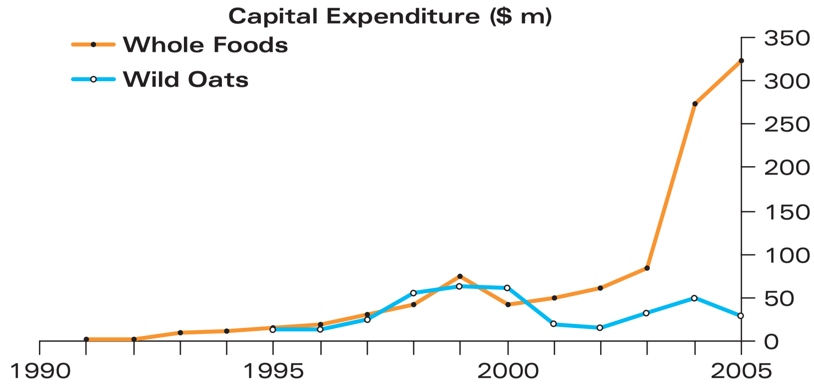

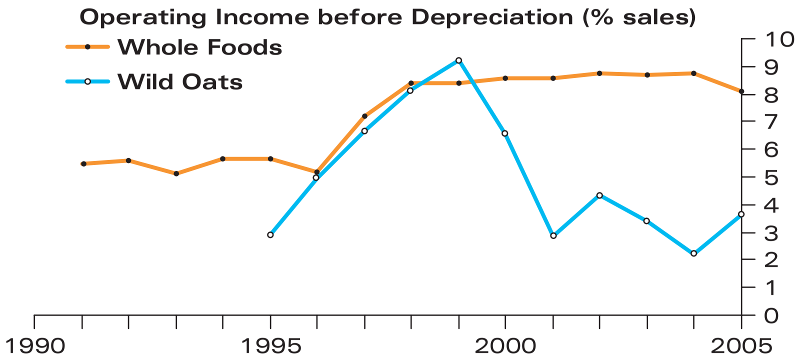

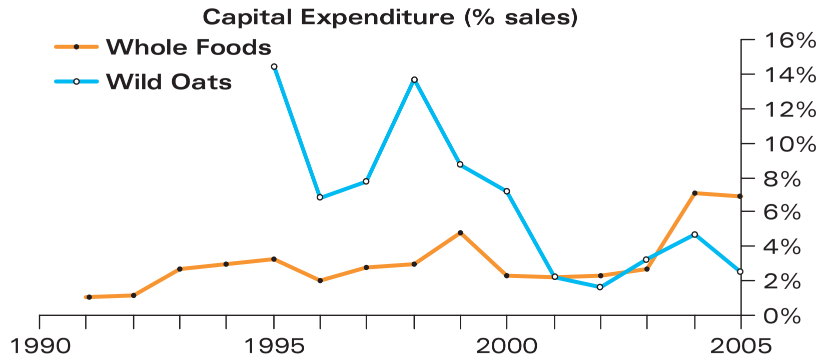

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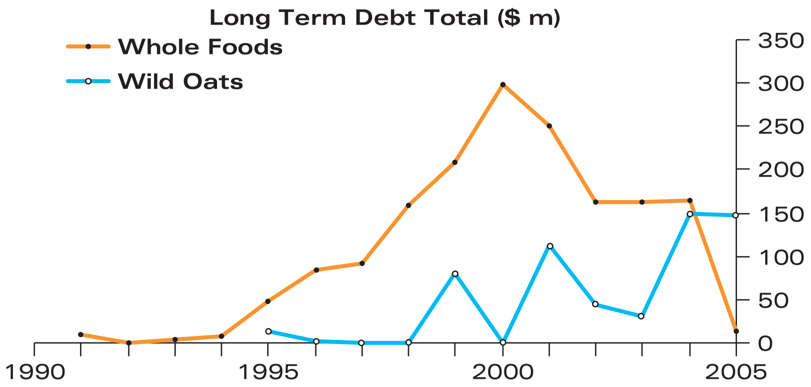

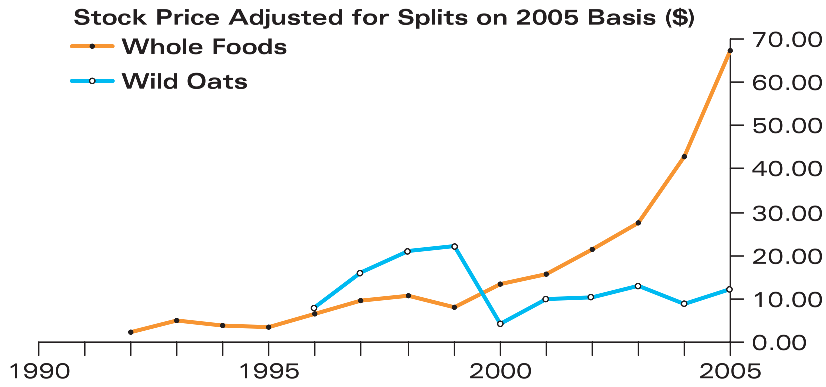

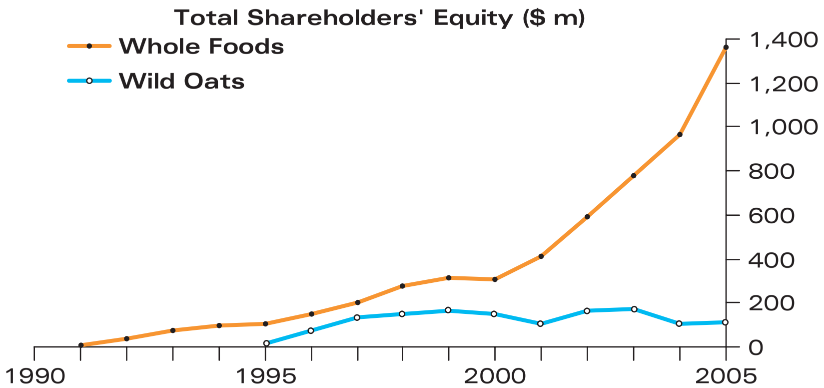

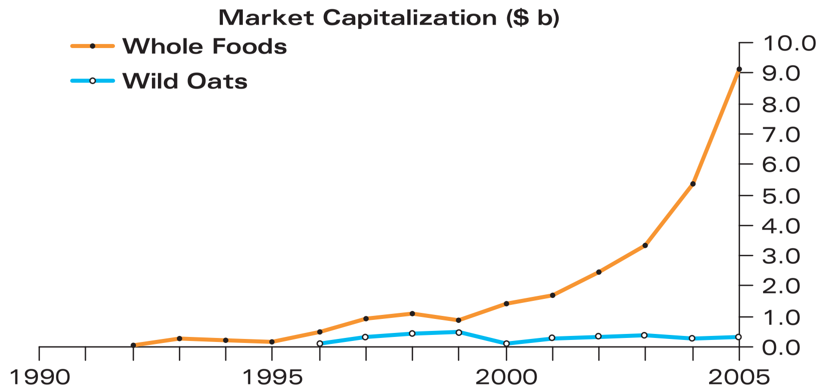

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