E.J. BRACH:

A MISADVENTURE IN CANDY LAND

An Economic and Social Analysis by

The Midwest Center for Labor Research

for the Garfield Austin Interfaith Action Network and the International Brotherhood of Teamsters, Local 738

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Forward

The Midwest Center for Labor Research was retained by the International Brotherhood of Teamsters Local 738, that represents production employees at E.J. Brach in Chicago, and the Garfield Austin Interfaith Action Network (GAIN), a coalition of community organizations and churches in the community that surrounds Brach, to produce this paper. MCLR has been studying E.J. Brach for five years. We were introduced to the problems and possibilities of the company following a request by GAIN to look into the reasons for lay-offs. Since that time, we have worked with the leadership of Teamster Local 738 and had the opportunity to interview production employees, ex-management personnel and others in the candy industry.

This paper was written by:

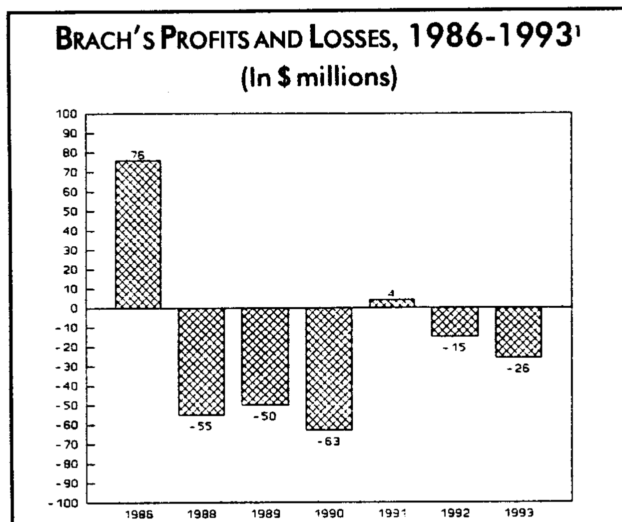
Dr. Robert Ginsburg, MCLR Research Director
Xiaochang Jin, MCLR Assistant Research Director
Sheila McCann, McCann and Associates

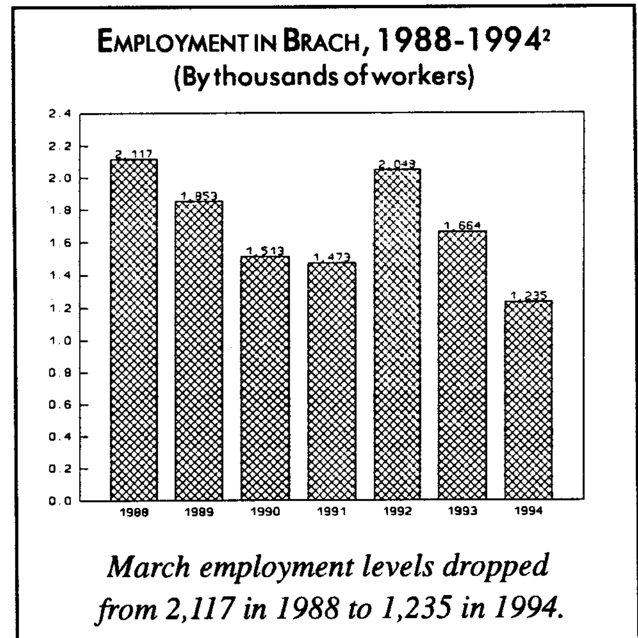
A MISADVENTURE IN CANDY LAND

An Economic and Social Analysis of E.J. Brach Candy

Since 1990, the specter of a shuttered E.J. Brach Candy plant has haunted the residents of Chicago's west side, Brach's production and salaried employees, as well as the civic and political leadership of the state of Illinois and the city of Chicago. It was in 1990 that Brach's parent company, Jacobs Suchard threatened to move production to Mexico or Canada and eliminate more than 2,100 jobs unless it received a designation as a Free Trade Zone (FTZ), which would have brought an exemption from imported sugar quotas (an exemption not enjoyed by most other U.S. confectioner companies.

Brach did not receive the exemption, and did not move out of its west side manufacturing facility. However, this incident focused attention on the wisdom of a business and marketing strategy, initiated with the purchase of the company in 1987, that quickly generated losses of $50 million in 1988 and to date could exceed $200 million.





March employment levels dropped from 2,117 in 1988 to 1,235 in 1994.

In addition, since 1987, the company has seen:

- ✓ **a loss of nearly 900 jobs, or 42% of the workforce**
- ✓ **9 different CEOs,**
- ✓ **a loss of key customers and market share,**
- ✓ **hostile labor/management relations,**
- ✓ **and a refusal or inability to communicate and work with a concerned local community.**

[1] The 1986 profits were reported by Financial Times, April 20, 1990. The 1988 losses were estimated by Hershey, a Brach's competitor, on the Brach's application for the Free Trade Zone. The 1989 losses were reported by Financial Times, June 25, 1991; and the 1990 figure was an estimate by Peter Rogers, then CEO, quoted by the Sun-Times on June 16, 1991. The 1991 number was provided by Peter Rogers, former CEO of Brach. The 1992 losses were reported by the Chicago Tribune, January 18, 1994. The 1993 losses were announced by Brach management at a March 13 union stewards meeting. No public data is available for 1987.

[2] The employment in Brach varies due to the seasonal change. All the figures listed reflect only the level of employment in March. Teamster Local 738 supplied these figures.

Particularly worrisome to Brach-watchers is the internal turmoil and misreading of the U.S. candy market that has typified Brach's leadership under Jacobs Suchard and C. J. Van Houten & Zoon Holding AG, its current parent company. This company was formed by Klaus Jacobs to run Brach and other companies not included in the purchase of Jacobs Suchard by Philip Morris.

A five year examination of Brach's operations, including a review of published corporate documents and interviews with customers, competitors, industry analysts and individuals knowledgeable of the company and its leadership shows why the business strategy implemented by its absentee Swiss owners was doomed to fail. If left to continue, the community will be left with an all-too-real scenario for the demise of the largest employer on the west side of Chicago. The impact on the neighborhood, the city of Chicago and state of Illinois would be substantial in terms of:

✓ **hard-core unemployment** with a loss of 7,000 jobs, with lost jobs in agriculture, wholesale trade and other sectors supplying corn syrup, milk and related services as well as consumer and service positions created by Brach employees' personal spending,

✓ **cost to government** of over $92 million due to lost government revenues from taxes and higher government expenditure for displaced workers,

Some industry insiders believe it is still possible to save the 90-year-old company. The fix will not be easy or quick. But it can be done with the cooperation of Brach Chairman Klaus Jacobs and President/Chief Executive Officer Kevin Martin; Brach employees; the Teamsters union and other labor leaders; industry, civic and community leaders; and the support of economic development leaders at the city, state and federal levels.

What follows is an analysis of Brach, its history, products, market niche, customers and the economic and social cost of its potential demise. Additionally, some alternatives are offered which could turn the company around, stem the tide of losses and regenerate the world's largest candy manufacturing facility.

I. Portrait of a Manufacturing Anchor for Chicago and a Sweet Success Story

E. J. Brach was founded in 1904 by Emil Brach, a German immigrant. He invested his life savings in a storefront candy store which he named "Brach's Palace of Sweets." Thanks to his innovative marketing strategies, the family business grew into an interstate enterprise with a weekly output that eventually reached 5.5 tons of candy. ("Economic Survey," Exhibit 4, E.J. Brach Application for Free Trade Zone Status.)

In 1921, ground was broken at 4656 W. Kinzie, its present location, for a plant with three floors. Subsequently, this plant has been expanded sixteen times to its current 2.2 million square feet. It is now the largest candy manufacturing plant in the world.

In 1966, American Home Products Corporation, the U.S. based conglomerate, purchased the company. During the more than twenty years E. J. Brach was operated by American Home Prod-

ucts, it grew to be one of the largest food companies in the U.S. In 1986, the year before its acquisition by Jacobs Suchard, the estimated pretax profits for the company were $75.6 million. (Financial Times, September 20, 1990.) It accounted for two-thirds of the U.S. market for bagged candy and seven percent of the $9 billion U.S. candy market. (Amy Feldman: "Arrogance Goeth Before A Fall," Forbes, September 30, 1991.)

Brach is now the largest candy manufacturing plant in the world.

The candy company's success was driven by its ability to provide grocery, drug store and discount retailers with a variety of products (starlight mints, candy corn, chocolate-covered raisins and nuts) and package sizes throughout the year and merchandising programs during the key holiday seasons of Valentine's Day, Easter, Halloween and Christmas. The company knew better than most how to sell penny candy by the pound. They were the first to individually wrap candy. They were the first to offer "Pick-A-Mix" candy sold by the pound in the grocery's produce department. They were the first to offer in-store pegboard displays, giving consumers a "billboard" of bagged products hung on pegs. They were the first to offer product in a variety of low and high margin bags and packages to meet drug store, convenience stores and discount customer requirements. The key to its success was, and is, a focus on selling everything a retailer needs. That means offering a variety of sizes and holiday programs that include a range of product from jelly eggs to chocolate bunnies and point of purchase merchandising displays designed to stimulate sales.

During its first 83 years, E. J. Brach was a stable and profitable company providing a strong employment base for the city of Chicago and the state of Illinois. In 1987, the company employed 3,700 workers, making it the sixth largest manufacturing company in the city of Chicago and the twenty-fourth largest manufacturer in the state of Illinois. (E.J. Brach's Application for Free Trade Zone Status, 1990)

II. Jacobs Suchard and Its Global Vision for E. J. Brach

Jacobs Suchard Limited, a Swiss chocolate and coffee conglomerate, purchased E. J. Brach in 1987 for $730 million. At the time, Swiss management saw the acquisition as an opportunity to achieve U.S. distribution for its European chocolate bars, such as Toblerone and Milka, as well as providing a launch into the Asian market. However, the purchase price was widely considered to be too high. (Merrill Goozner "Sales Tumble as U.S. Candy Market Grows", Chicago Tribune, Sunday, April 22, 1990).

At the time of the acquisition, Klaus Jacobs, president of Jacobs Suchard, identified specific goals for the company:

- ✓ Increase U.S. sales to 20 percent of Jacobs Suchard sales
- ✓ Expand its exports to European and other non-U.S. markets
- ✓ Focus on branded merchandise rather than bulk seasonal product ("Economic Survey," Exhibit 4, E.J. Brach's application for Free Trade Zone Status).

On the surface, many would characterize these goals as desirable. Most companies in the industry recognized the attractiveness of this vi-

sion of focusing on a limited, branded product. Companies with limited brands that enjoy high volumes such as The Wrigley Co., Mars, Nestle and Hershey earn high profit margins and to a large degree control the market. If Jacob were able to achieve this, he would have created a company that would be the envy of the consumer product world. In hindsight, the strategy Jacob employed to achieve these goals was doomed to failure from the outset. The problem, according to many industry analysts, was that the Swiss company misread and misunderstood the U.S. marketplace and Brach's customer base.

By the end of 1989, the company was in serious trouble. Corporate turmoil, in part due to a revolving door of senior management and misplaced energies, resulted in losses of $50 million on sales of $470 million. Former executives cited Jacobs Suchard's autocratic management style and inability to recognize the differences between American and European candy consumption habits. For example, Europeans consume more candy per capita than Americans and they consume it year round. In the U.S., candy is purchased on impulse and around four major candy holidays - Halloween, Christmas, Valentine's Day, and Easter.

III. What Else Went Wrong?

Under Jacobs Suchard, problems began to develop in all aspects of the company:

✓ **The Brach name,** which had a strong identity for quality bulk candy, was changed to Jacobs Suchard Inc., a name that few retailers or consumers recognized;

✓ **Product lines were reduced** from 1,700 to 400 to cut costs. This meant that rather than selling Starlight mints in 20 sizes, they would only be produced in six sizes. This makes sense only if you don't alienate the customers that were purchasing your products in the 14 other sizes. In Brach's case, drugstores could no longer sell a 9 1/2-ounce bag for a higher margin than the 7-ounce bag available at a discount store. (Amy Feldman, Forbes, September 30, 1991.)

✓ **Holiday promotional activities were drastically curtailed.** In early 1989, Ray Lalowski, the candy buyer for Walgreen's confronted E. J. Brach's new marketing executive at an industry trade show to talk about the upcoming Easter program only to find out there was none in place. "They didn't know which items they were going to have, they didn't know what the packaging would look like. We dumped them for the season and went to Farley (another Chicago producer)." (Merrill Goozner, "Sales Tumble As U.S. Candy Market Grows", Chicago Tribune, April 22, 1990.)

Other customers followed Walgreen's lead. Wal-Mart reduced its purchases of Brach candy from $26 million to approximately $6 to 8 million by 1990. If Brach's could not deliver what they wanted there were other candy companies who would. By the end of 1989 Jacobs Suchard's worldwide profits dropped by 10 percent to $216 million, on sales of $5.2 billion as a result of the decline of U.S. sales. (Amy Feldman, "Arrogance Goeth Before A Fall," Forbes, September 30, 1991.) What is especially ironic is that while Brach's was declining, industry sales grew 11 percent to $8.1 billion, according to Commerce Department figures.

In 1990, Phillip Morris purchased Jacobs Suchard for $3.8 billion, minus its U.S. subsidiary, E. J. Brach Corp. A holding company, C. J. Van Houten & Zoon Holding AG was formed by former Jacobs Suchard owner, Klaus Jacobs, to run Brach and other businesses. Following a failed attempt to reduce sugar costs through designation as a Free Trade Zone, Jacobs brought in Peter Rogers, a specialist in reviving financially troubled companies and an expert in the confectionery industry.

With the reduction in sales personnel came a reduction in loyalty to Brach candy.

The first move by this new management team was to attempt to restore the formula that had made the company a success before the acquisition. Rather than focusing on branded products, the company once again offered affordable confections produced in a wide variety of both product and package type, enabling the retailer to market the ideal size and mix for individual store and customer value. Rogers personally met with buyers representing every class of retail and promised to give them what they needed and delivered on that promise when product lines grew to 1,300. Rogers understood the U.S. marketplace and Brach's niche. His experience indicated that it would take patience and determination to restore customer loyalties. Holiday programs would be crucial for this effort. This strategy was initially successful. For example sales to Wal-Mart increased to nearly the level they were in 1987-88. The company posted a small, $4 million operating profit in 1991. ("Interview with Peter Rogers," MCLR, March 17, 1994.)

Published reports show that Brach lost between $18 million and $21 million last year.

Despite turning in the first profitable year since the takeover, disagreements with Jacobs on marketing and management strategies, particularly over commodity vs. branded products, led to Rogers departure in September 1992. This departure signaled the start of another turbulent period that saw three chief executive officers in just one year. There continues to be a high rate of turnover and dismissals within the sales and marketing department. With the re- focus on fewer, branded products, the company rationalized a smaller sales force.

The marketing strategies and personnel decisions have unfavorably affected Brach's customer base. As Brach reduced the number of products and options, some retailers discontinued orders. High profit margin branded products didn't sell as well in the drug store, convenience and mass merchandising outlets. With the reduction in sales personnel came a reduction in loyalty to Brach candy. Compounding this was the fact that as these sales personnel began to work for Brach's competitors they were able to bring customers with them.

The latest indicator of concern was the failure of Brach to have a presence at the American Wholesale Marketers show in February 1994 and the canceling of its booth at the Food Marketing Institute show in May where the supermarkets and grocery stores attending the show make up 80 percent of Brach's sales. And, the losses continue. Published reports show that Brach's lost between $18 million and $21 million last year. (Frederick Lowe, "Signs of Trouble Dogging E. J. Brach," Chicago Sun-Times. February 22, 1994.)

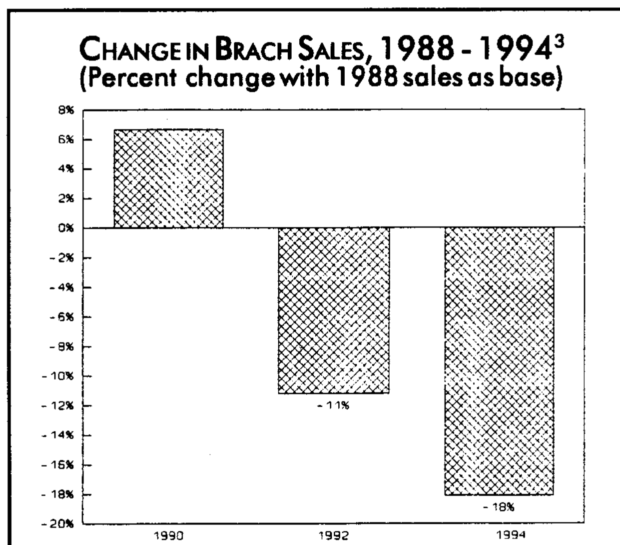
IV. The crisis at E.J. Brach: Economic Impact of a Failed Strategy

It is the opinion of many within the confectionery industry that the focus on high margin, branded products has had a negative effect on the company, its employees, vendors and supporting services. The only winners seem to be the competitors who are slowly picking up the customers discarded by Brach. One competitor said, "I hope the firm dies of leprosy instead of having a heart attack. That way we can slowly pick up their business." (Frederick H. Lowe, "Signs of Trouble Dogging E. J. Brach," Chicago Sun-Times, February 22, 1994.)

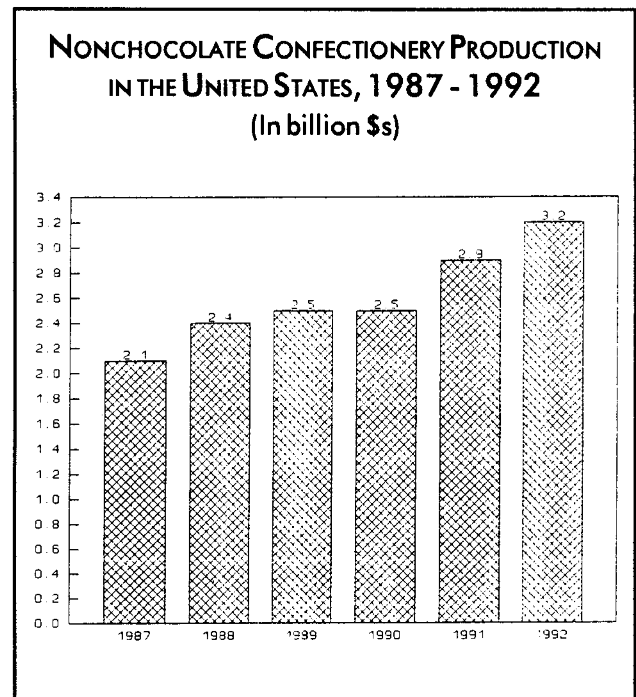
A review of the history of Brach under Swiss ownership reveals the following:

✓ The change in focus from commodity to branded products resulted in the **loss of business from several large accounts**, such as Walgreens, K-Mart, Wal-Mart and others representing millions of dollars of core sales;

✓ Prior to the take-over, Brach's revenues exceeded $640 million with profits of $60 million. In 1993, revenues were $400 million with a **loss of $26 million**;

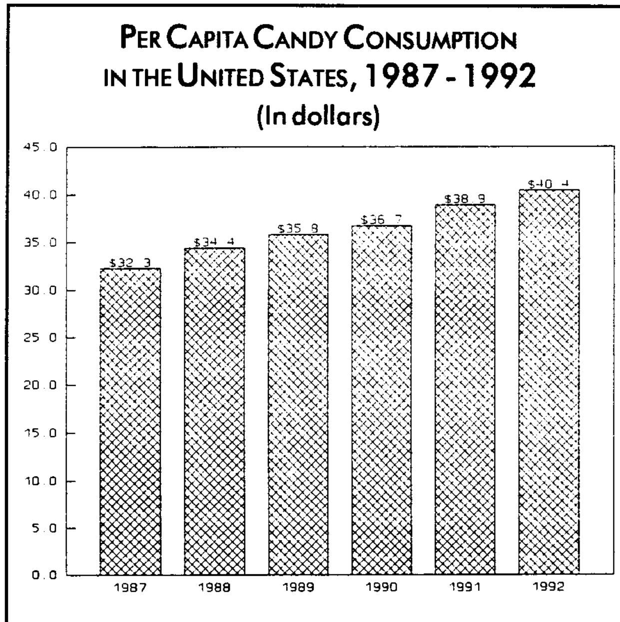


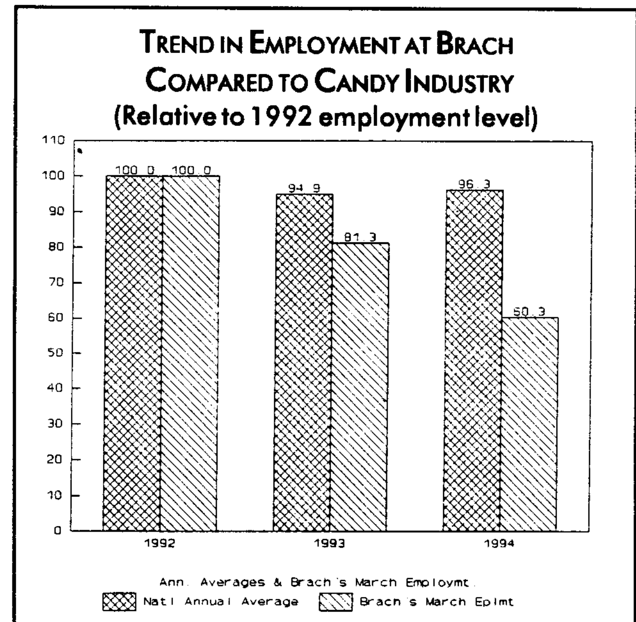
✓ Despite a 25% increase in candy consumption in the US since 1988, **production levels at E.J. Brach have dropped dramatically**. In 1994, the company will produce 36,000,000 lbs. less candy than the previous year and production is now approximately 320 million pounds per year according to Brach officials (Management presentation to E.J. Brach stewards on March 24, 1994);*This represents a 39% drop in sales volume since 1988 when Brach sold 460 million pounds of candy.* ("Economic Survey," Exhibit 4, Brach's FTZ application, p. 4; "Confectionery Products-Total sales," Department of Commerce).



[3] The 1988 sales were reported by Brach in its application for Free Trade Zone. Sales for 1990 were reported by Dun & Bradstreet, which quoted this figure from an interview with the Brach management. 1992 data was reported by Van Houten & Zoon Holding, AG, Annual Report. Van Houten & Zoon is the parent of Brach. 1994 sales estimate was provided by Brach management to E.J. Brach stewards, April 1994.

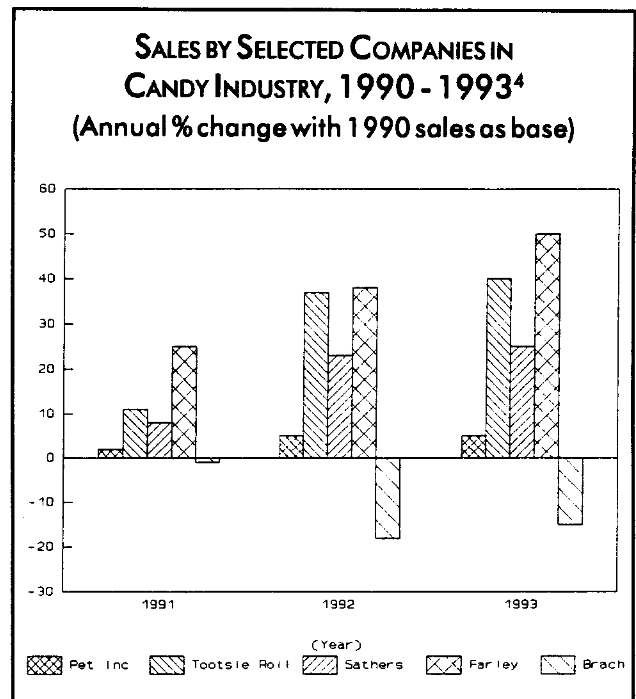
✓ **Brach sales and employment have declined** even as employment in the industry has remained constant:





V. Reasons for the Crisis: Is It Management or Is It Wages?

Current Brach management has argued that the financial problems at E.J. Brach are due to high labor costs that put them at a disadvantage in the industry. As is clear from the charts on employment in the candy industry and sales of selected companies (including both higher wage or unionized plants and lower-wage or non-unionized plants) Brach is going in a different direction than the rest of the industry. It was clear in 1990 in comments from other candy companies (include Hershey and Farley) that Brach's was "competitive with other US based companies in terms of its level of technology and its raw material costs [and it was] also clear that Brach's labor costs are comparable to confectionery industry standards, especially for a company of Brach's size...". (Comments by Hershey on FTZ Application).



[4] All the sales were reported by Dun & Bradstreet, except four figures. The 1991 Tootsie Roll's sales were reported by Chicago Tribune, Jan.23, 1992. The 1991 Sathers' sales were reported by Corporate Report, Minnesota, March 1992. The 1992 Brach's sales were reported by Annual Report of Van Houten & Zoon Holding AG, the holding company of Brach; and the 1993 Brach's sales were reported by Chicago Sun-Times, Feb. 22, 1994.

Brach was a profitable and efficient producer of candy in 1990 based on selling large volumes of candy. Labor costs have not increased significantly in the past 4 years. Modest wage increases have been offset by agreements by the workers to pay a larger share of the cost of benefits, including health care. What has changed is that Brach's management and marketing strategy has resulted in dramatically lower sales.

It appears that no amount of wage concession would be able to reverse the profit slide and save Brach's as long as the current marketing strategy remains in place.

Given this slide in revenues, production and employment, the question may be when, rather than if, the company announces the closing of the plant. It is important for the city and its elected officials, the workers and the candy industry to understand how the company got to such dire straits.

VI. Projected Impact of a Closure of the Brach Plant

All these signals point to the real possibility that the plant will be closed entirely or that production will no longer be possible at the current Chicago facility. It is both apparent and the view expressed by management that current production levels, well below 400 million pounds per year, make it impossible to efficiently operate a candy manufacturer in a 7-story, 2,000,000 square foot plant. In either case, a crisis in Chicago would result. Economic repercussions would be severe. A shutdown would be particularly devastating given the plant's high degree of integration with other sectors of the state's economy, especially its farm sector which supplies corn syrup and milk; and the plant's minority workforce which is projected to have a long average duration of unemployment. The cost to government in lost tax revenues and increased expenses for unemployment compensation and welfare assistance amounts to $92 million. The ripple effect on the state and local economy will result, ultimately, in the loss of another 4,700 jobs on top of the unemployed Brach workers. A summary of the impacts of a Brach closing is contained in the tables on the following page.

SUMMARY OF THE BRACH SOCIAL COST ANALYSIS

The study projects the impact of the loss of 2,048 E.J. Brach jobs, the number employed in 1992, many of whom are currently laid off. The calculations are for the first two years after dislocation.

The total cost to workers and taxpayers would be enormous.

✓ JOB LOSS

Direct **2,048 jobs**
Brach jobs lost

Indirect **4,723 jobs**
"Ripple effect" jobs lost in interrelated industries

Total Job Loss 6771 jobs

✓ EXTENDED UNEMPLOYMENT

Laid off workers still out of work after 1 year	**1,925 workers**
Workers still jobless after 2 years (when unemployment compensation runs out)	**1,129 workers**

✓ DEMOGRAPHICS OF THE BRACH WORKFORCE

35% of the workforce is female.
Women suffer longer periods of unemployment and get lower wages when they do find jobs.

25% of the workforce is black and 31% is Hispanic or Asian.
Same issues apply as when women are dislocated.

The average age of the workforce is 39.
Older workers suffer age discrimination, and more often have injuries or prior medical conditions that limit their opportunities.

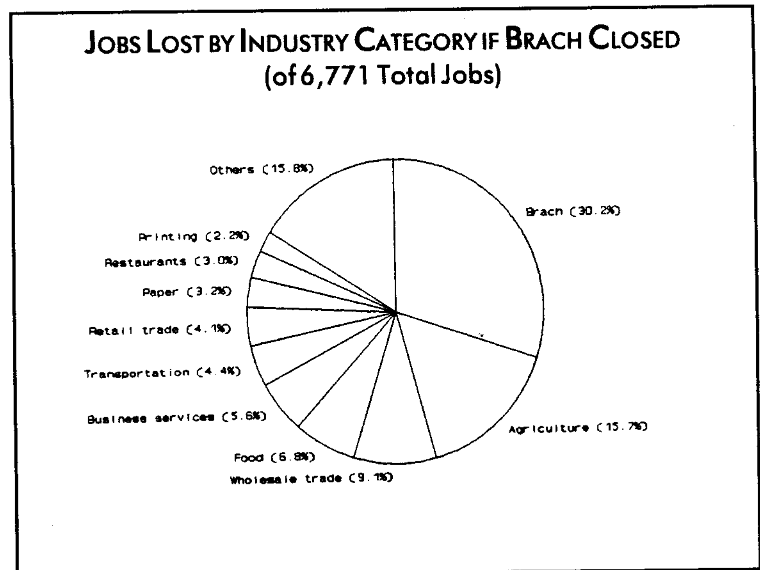
✓ COST TO THE GOVERNMENT

Illinois Tax revenues	**$3.9 million loss**
Indirect business taxes, including sales tax revenue	**$14.2 million loss**
Federal Income Tax revenues	**$19.4 million loss**
Social Security Tax revenues	**$19.8 million loss**
Property Tax revenues	**$2.4 million loss**
Unemployment compensation cost increase	**$28.6 million cost**
Welfare assistance cost increase (i.e., Food Stamps, AFDC & Medicaid)	**$3.2 million cost**
Total cost to the Government	**$91.6 million**

An Analysis of the "Ripple Effect"

Beyond the quantifiable loss to the city and state, losing nearly 7,000 jobs will rip the fabric of the west side community.

The study forecasts that **44.1 percent of the workforce would still be unemployed after 26 weeks**, when unemployment compensation runs out; **20.9 percent would still be out of work two years after the closing** with those workers age 55 and older especially vulnerable.



Jobs Lost by Industry Category if Brach Closed
(of 6,771 Total Jobs)

✓ Social Costs

Among the social costs to the community and the city are the following:

- ✓ increased crime rates
- ✓ increased instances of domestic violence
- ✓ increased stress-related health problems such as ulcers, high blood pressure, heart attacks, insomnia and mental health problems
- ✓ increased suicide
- ✓ increased drug and alcohol abuse and related health problems
- ✓ loss of participation in civic activities, such as church attendance, community involvement and voting

VII. Positive Options Available!

Clearly, it is in the best interests of the civic, political and business leadership to reverse the current decline that would bring about these devastating consequences to the social fabric and economic development of the community, the city and the state. There are several alternatives which could help save Brach and eventually realize the owner's goals of marketing branded products in the U.S. *See "Viable Alternatives" box at right.*

✓ VIABLE ALTERNATIVES

1. Current ownership will remain intact, but with a commitment to boost production and sales.

2. A joint venture between Mr. Jacobs, the employees, management and new investors. The manufacturing company would be jointly managed and owned. The venture would supply branded items that current management wants to sell and pay a royalty for the use of the Brach name, and the new company would sell to the markets that aren't being effectively serviced. Such a proposal has been made to Mr. Jacobs by representatives of Teamsters Local 738.

3. An outright sale of the company to its employees. Such a proposal has been made to Mr. Jacobs by representatives of Teamsters Local 738.

All of these options must be accompanied by a *verifiable* marketing, sales and management policy that builds on the business strategy employed prior to 1987, and on the talents of Brach's highly skilled production and management employees. This strategy will require patience. Even in a best case scenario, it will take several years, but ultimately customer loyalties and profits could be restored. At that time, the profits generated from this strategy could be applied to the introduction of branded products.

VIII. Recommendations

To ensure that every effort is taken to save this American candy company, it is imperative that a dialogue begin between the current owner and managers, the city and state economic development officials as well as representatives of the community and the Teamsters. This dialogue will allow interested parties to express their ideas and solutions to a problem that, if left unchecked, could spell disaster. Such a dialogue will provide the opportunity to reach a public/private solution that is a win-win for Klaus Jacobs, the city of Chicago, the state of Illinois, the west side community and the E. J. Brach workforce.