INTRODUCTION

Herr Foods Inc. (http://www.herrfoods.com/) is a regional snack food company in the mid Atlantic and Northeast producing and distributing over 350 sku items under their name with potato chips representing over 50% of their revenue. Daryl Thomas, vice president of marketing for Herr Foods Inc. (Herr’s), was driving to his office pondering the challenges that Herr Foods would have to address in the near future, especially with regard to a more health sensitive selection of snack foods. One of the lead stories on last night’s (1/12/2005) evening news highlighted a report on the government’s new Federal Diet Guidelines published by the Agriculture and Health and Human Services Departments. One of the major recommendations was for Americans to slash their calorie intake and increase their exercise to 30 to 90 minutes a day. They advised people to lose weight but gave few specifics on how to do it.

The new dietary guidelines updated the food pyramid for the first time in 12 years. While most people were aware of the food pyramid, few seemed to follow it as evidenced by the increasing number of overweight and obese individuals.

The new guidelines promoted whole grains such as whole wheat bread versus refined foods like white bread or bagels. They also promoted more vegetables and fruit. Fewer calories, but not necessarily limiting carbohydrates, plus more physical activity were the keys to controlling body weight.

A committee of 13 scientists and doctors had spent nearly a year reviewing Americans’ diet and health. They said people practiced sedentary lifestyles and made poor food choices, leading many to exceed the calories they needed even as they failed to get enough nutrition. People needed to choose their fats and carbohydrates wisely and severely restrict trans fat that could clog arteries. It was also important for people to reduce the amount of salt to about 1 teaspoon per day as salt was linked to high blood pressure.

This news announcement further reinforced what seemed to be coming from many different sources — the importance of a healthy lifestyle and proper eating. The fast-food industry had especially come under fire even with threats of lawsuits claiming that fast-food companies were responsible for individual illnesses and weight problems.

Daryl reflected on how Herr’s had been in business for almost 60 years and how much times had changed. When
Herr’s first started potato chip operations, many people had much more physically demanding jobs. Children did not have television or video games and spent more time involved in physical activities. He had recently heard that children may spend 5 hours a day in a sedentary activity after sitting all day at school. Much had also been learned over the last 60 years about healthy foods and preparation practices.

Daryl understood that change was critical for the long-term viability of a business. Jim Herr, founder of the company, often said, “A company standing still will eventually go backward.” Daryl wanted to review how Herr’s had changed in light of increasing revelations regarding lifestyle and eating habits. The fast-food industry was already receiving some condemnation for products they serve, and he was well aware of changes they had made to maintain market share and customer satisfaction. Could the snack-food industry be far behind?

If the term “junk food” came up, Daryl suspected that — after hamburger and fries — many people would think “potato chips.” Given that potato chips represented a significant portion of the production and profit of Herr Foods, Daryl thought it might be worthwhile to review how the company was responding to this changing environment. Being proactive to national trends and consumer concerns might also provide a new business opportunity. Promoting healthier snack foods could increase market share, especially in the health-awareness market. Specifically, Daryl needed to consider a decision to recommend a more health sensitive selection of snack foods.

**COMPANY HISTORY**

In 1946, Jim Herr purchased Verna’s Potato Chips company in Lancaster, Pennsylvania, for $1,750. The company consisted of two iron kettles (each holding 100 pounds of lard), a three-potato slicer, a peeler that held 10 pounds of potatoes, and a 1938 Dodge panel truck. At 21 years old and with a $1,750 loan, Jim soon became a distributor of potato chips in a wax paper bag to small grocery stores and other food outlets in southeastern Pennsylvania.

He and his wife, Miriam, worked long hours in front of the hot kettles perfecting their recipes and product quality. Building a customer base was equally difficult as there were similar operations selling essentially the same potato chip-type products in the Pennsylvania and Maryland area.

In 1951, a fire destroyed the entire operation. Jim, a religious man, believed God would lead them to a new location. Soon, they purchased a small farm in Nottingham — ideally located near his mission church where his family was active and closer to their distribution area. With all of his available resources and help from the local bank, Jim reestablished Herr’s and expanded the scope of its operations.

Nottingham — located in the southwest corner of Chester County about 50 miles southwest of Philadelphia and 50 miles north of Baltimore — was a great location. Even though it was in a rural area, nearly 50% of America’s population lived within a 500-mile radius. The county itself had one of the highest per-capita incomes in the state and was one of the fastest growing counties in the Philadelphia area. Jim found that the people practiced good moral and ethical standards, were religious, and provided a dependable and stable work force.

Jim and Mimi’s faith and commitment to fair and ethical business practices paid off over the years. Jim was a man of his word, and a simple handshake often closed many complicated agreements between customers and suppliers. Jim always made good on his promises and never forfeited on a debt obligation. If someone was unethical in their business practice with him, he showed compassion and was not vindictive. This was not a sign of weakness, but an effort to reflect his Christian testimony in all areas of his business.

Herr Foods grew and prospered with 1,500+ loyal employees and over 350 sku product line classifications. Herr’s operated in a 10-state region between Massachusetts, Ohio, and Virginia with 23 distribution centers and its own fleet of vehicles to distribute its products to retailers. Revenues approached $200 million per year for this family-owned business, with potato chips accounting for about 50% of revenues.

The same values that Jim practiced in running the business were still evident as the second generation had taken over ownership and operation of the business. Jim’s three sons, Jim, Ed, and Gene; his daughters, June and Martha; and his son-in-law, Daryl, were all active in the business and espouse the same strong Christian values and beliefs. Son Jim stated, “I’ve basically agreed with my father’s philosophy of running the company (and its mission) to maintain a culture of integrity, fairness, and opportunity; to stress quality products and service; and to continue the growth of the company.”

**CORPORATE CULTURE AND PHILOSOPHY**

Jim Herr had always been a deeply religious man and believed that the corporate culture and philosophy should be grounded in Christian values and ethics. Maintaining
the highest levels of integrity, reputation, and excellence of Herr Foods in the eyes of customers, employees, suppliers, and other stakeholders was critical. Therefore, every significant decision top management made must be subject to something similar to a “What would Jesus do?” criteria:

- Is the action in the best interest of all parties concerned?
- If not, what additional actions, if any, will be needed?
- Are we being a good steward of our resources — both financial and otherwise?
- Does this action meet the highest ethical and integrity standards?

For this decision on more health sensitive snacks, there were several critical concerns some of which were company integrity and reputation, product quality, potential compliance regulations, emerging and/or maturing market segments, and media visibility. Daryl knows the importance of being sensitive to the market and the desires of all stakeholders and he wants the company to remain in a more proactive versus reactive mode.

**PRODUCTS AND PRODUCTION**

Given that there were 30 snack-food companies in Pennsylvania alone — along with the large national companies like Frito Lay and Nabisco — any level of success and growing market share was quite an accomplishment for Herr’s. In addition to the extensive potato-chip product line, the company produced pretzels, tortilla/corn chips, popcorn, and cheese curls. Each line offered a variety of products with varying sodium, fat, nutrient content, and packaging. The company also distributed complementary product lines like salsas, dips, meat snacks, and an assortment of other items.

The pretzel production system was highly automated. Three hundred pounds of dough were produced every 8 minutes and fed onto four different conveyer lines. The operation ran continuously from Monday morning through Friday noon. On Friday afternoon, the equipment was cleaned. After the dough — either plain or sour — was blended into 10-pound sections it went through a pretzel die to form its shape. Depending upon the pretzel, 600 to 2,000 pounds per hour were baked in each of four ovens.

The tortilla/corn line produced both corn and tortilla chips. Two lines ran continuously at a rate of about 2,000 pounds of product per hour. The corn was soaked for 8 to 10 hours and then cooked for 2 minutes to a lumpy, creamed corn texture. The product was cut on a sheeter to the desired shape and then sent to a fryer for 15 seconds. The hot chip was then sent through a tumbler where seasoning was applied. One day per week, onion rings were produced in this assembly area. Onion rings were actually dehydrated potato flakes fried with onion seasoning applied.

Cheese curls and popcorn represent smaller product lines. Corn meal was used to produce cheese curls and extractors were used to remove moisture and apply seasoning. The product was baked for 1 minute to give it a puff texture and about 1,000 pounds were produced per hour. Popcorn products used a yellow gourmet kernel that was air popped. A tumbler removed small and un-popped kernels leaving the large hot kernels, which were seasoned.

The potato chip line was the biggest operation. Sixteen to twenty tractor trailer loads of potatoes arrived every day with 50,000 pounds of potatoes per truck. Each truck was hydraulically lifted to a 45-degree angle to dump the potatoes. It took 4 pounds of potatoes to make 1 pound of potato chips.

Potatoes were dropped into a washer where they were scrubbed and sent by water flume to three slicers. Potatoes were sliced at 24 slices per inch in less than 1 second. The potatoes then went to the vegetable oil vats where they were cooked between 3 and 5 minutes at around 325° F. Around 56,000 pounds of potatoes per hour were processed through five fryer ovens 16 hours a day. Afterward, they were dried and salted.

The chips were transported on a conveyer belt moving at 60 miles per hour where they passed under an opti-sort electronic sensor that identified chips that were either overcooked or green. The defective chips were blown off the belt. Various different stages along the conveyer size the chips before they reach a packing machine, with smaller chips going to the smaller packages.

The tortilla chips, popcorn, cheese curls, and potato chips were packaged by weight using a bucket process to accumulate the product. The product dropped into a waiting bag. Fourteen million bags of potato chips of various sizes were produced per month along with a similar quantity of other products. The production process was almost entirely automated until the bags were placed in cartons and inspected.

Cartons of all the product lines go into the warehouse where they were stacked by type. The entire warehouse inventory rotates out on a first-in-first-out basis three times per week, which was critical for a freshness-sensitive product that had about a 10-week shelf life.
Pretzels were the only remaining labor-intensive product line with only a partially automated packing function. Currently, individuals packed containers for many of the final pretzel products. Herr’s was considering automating this process and cross-training existing employees into other jobs.

**MARKETING**

Brand and product marketing was a constant challenge. Herr’s had to compete not only with the large national companies like Frito Lay, but also with over 30 regional snack food companies like Utz, Wise, and Snyder’s of Hanover. The multitude of companies and proliferation of products had made competition in the northeast and mid Atlantic areas, where Herr’s operates, especially complex.

Herr’s was constantly considering new product lines and distribution and promotion strategies. With shelf space at retail outlets a premium, sales representatives must continuously work on building relationships with retail customers. Daryl thought about possible sources of competitive advantage in this area. Because of Herr’s integrity and honesty, customers’ trust in them had grown, making it easier for Herr’s representatives to work with their clientele.

For example, Herr’s had over 350 products, and given that snack packages tend to be bulky, sustaining shelf space at retailers was a major challenge. Fortunately, based on their continued relationship, retailers had maintained an interest in stocking Herr’s products, but the question of capacity was a constant consideration.

Herr’s was not alone as each producer in the snack food industry continued to solicit retailers for more and better shelf space for their individual brands as each expanded their product line based on new market trends. Thus, Herr’s accounted for the competitive moves made by other snack-food distributors which were trying to capture the same shelf space. Other distributors also represented quality products and the retailers were interested in the product mix from all suppliers that met the highest percent of customer preferences and delivered the greatest profits.

**CONSUMER ISSUES**

To make matters more difficult, diversities had an impact on the snack-food industry. Customer preferences included more ethnic foods, hot foods, spicy foods, organic, and health foods. The issue for manufacturers was to try to forecast how long the various interests would continue and what each would command in terms of market share over the long run. Most companies, including Herr’s, would have to choose carefully which segment niches to target and invest in product development. Some of the product variations could be easily produced with different seasoning or changing of ingredients, so it was possible to participate, as Herr’s was doing, in some of the specialty markets. Other requirements, like low fat, were more difficult because eliminating certain ingredients could drastically change the taste. Additionally, with any new product there may be the potential for new equipment and other capital investment demands. Finally, consumers may refuse to buy new products even if they were healthier.

The health concerns related to snack foods required a different marketing strategy. Realistically, many snack-food products may never be perceived as healthy. While some consumers think a potato chip was not especially good for you, they overlook the fact that it was not that much different than a baked potato with butter and salt. The potato was a vegetable that consumers find very nutritional, but very few people eat the potato plain. The potato could be seasoned to taste with everything from butter and salt to any number of toppings from sour cream to chili. The potato chip product was essentially replicating that baked potato process to suit individual taste and behavior of consumers.

To make healthier snacks, Herr’s had been experimenting by incorporating alternative elements during production to meet a variety of diet needs and consumer interests. The selection of cooking oils that used trans fat-free oil or low levels of cholesterol had always been a practice. However, it was essentially impossible to eliminate all forms of saturated fat and sodium in the production process and still maintain the taste that consumer’s desired. If Herr’s really wanted to produce only healthy snacks following some strict nutritional standards, over half of the product lines may be discontinued, significantly cutting revenue and profit potential. Many consumers would still want the previous products — healthy or not — and would just purchase a competitor’s products sitting a few feet away on the shelf. Manufacturers simply could not forecast what percent of the market’s consumer would strictly purchase foods for health reasons. Generally speaking, the low fat varieties of snack foods have not generated a strong consumer preference. In addition, many people eat snacks as a stress reliever, and potato chips were one of the most popular foods that consumers desired as a means of stress reduction.

The Snack Food Association had worked closely with other organizations like the American Council for Fitness
and Nutrition to develop healthy lifestyles with balanced diets that include snack foods. When consumed in proper proportions and in conjunction with appropriate daily activity, some snack foods may help regulate blood sugar and give individuals more sustainable energy. Snack foods were also “fun foods” to relieve stress and tension and provide pleasure.

**PRODUCT RESEARCH AND DEVELOPMENT**

Daryl met with Phil Bernas, the vice president of manufacturing, who was familiar with much of the new product development and efforts made by Herr’s to respond to nutritional concerns. Phil supported a company position they felt was in line with the Food and Drug Administration: it was not “good and bad food” but “good and bad diets” and a principle of “all things in moderation.” Phil believed that the media focus would be more on diets than on individual foods.

Phil pointed out that the potato chip was high in Vitamin C, potassium, and fiber. A 1-once bag of chips provided over 13% of the daily Vitamin C requirement for children and 7% of the recommended daily allowance of iron. (See Exhibit 1.)

Because of health concerns, Herr’s had been proactive in product research and development. About eight years earlier, they developed Rave, a product line using Olean—a indigestible fat with no calories. The product line was discontinued after two years because of lack of sales. Phil believed there was minimal customer satisfaction. The body actually craves calories, and consumers seemed to need some fats to gain calories. Olean was also a very expensive product at about five times the cost of vegetable oil. The products had to sell at a 25 to 30% premium over other similar products and also had a different texture and taste.

Herr’s had also looked into a soy product called Crisp—a high protein snack with moderate levels of carbohydrates and low fat. The product was a mixture of soy, corn, and potato and looked like a rice cake. However, the cost was about double that for the typical snack-food product. Consumers perceived pretzels as a healthy snack-food alternative. Herr’s was very active in the pretzel market with several varieties including a wheat pretzel. The problem with pretzels was the high level of carbohydrates—around 98%—and many current fad diets were down on carbs.

Herr’s, through a partnership with another snack food company, had been distributing power bars which were high in soy and low in carbohydrates and other similar items. For Herr’s to produce those products on their own would represent a significantly different production line and process. The partnership seemed to be a much more efficient way to penetrate this market.

Within existing lines, Phil indicated that reduced-fat potato chips might be an alternative along with low-salt varieties. It would be a matter of customer preferences. If a product line could not support itself, it generally did not get produced. The marketing issue always needed to be considered. With well over 200 different items and limited shelf space in most stores, there were only so many varieties of products that could be sold.

The type of oil used in the cooking process was also critical. Jim Herr switched from lard to cottonseed oil many years ago, and that had remained the vegetable oil of choice. Production people had found cottonseed oil to be low in saturated fat, with relatively good frying properties. This oil was reasonably inexpensive. The oil was about 30% of the material cost of a potato chip with the other 70% representing the cost of the potato. Also, about 35% of the final product was oil. Initially, about 70 to 80% of the potato was water. The cooking process reduced the water content to about 1 to 2%.

The research and development department determined the specs for each product, and they were closely monitored by the Quality Assurance Department. If problems persisted, team meetings were called to review situations. Appropriate changes were made to maintain high product quality.

Phil and Daryl were both aware that 40 to 50 prototypes were produced every month and of that maybe four to six major new items may be introduced in a year. Herr’s also considered distributing about four new products per year through joint ventures, but generally every new product led to the elimination of an existing product as they had reached the maximum number of products they could fit on to their current allocation of shelf space or within their plan-o-grams.

Phil generally believed that the health-food and diet markets still had not found a level of stability. First, it was low fat, then low carbs, then high protein, next low sugar, and maybe next low salt. If Herr’s tried to become a major player in either of these arenas it may just end up “chasing rabbits.” It was not that difficult to create a healthier product; the trick may be to create market share to justify the fixed cost and develop staying power. The product had to taste good and, for most snack foods, should be crunchy.
MARKET RESEARCH

While Daryl was discussing the issue of nutrition with key staff, he asked his administrative assistant, Christina McGinty, to conduct some additional market research to try to determine the extent of this health-food movement and emphasis on diet and exercise by various influential groups and agencies.

Christina recalled hearing about a study of obesity trends in certain women which was started in 1985. Twenty years ago, around 10% of the population was 30 or more pounds overweight. The study was repeated about seven years later and around 12% of the population was 30 or more pounds overweight. In 2002 data was collected from all 50 states, and 20% of the population was overweight by 30 or more pounds.

A study by the New England Journal of Medicine in 2003 showed that snack foods comprised 10% of the total calories of adults regardless of their classification, from underweight, to optimal body mass index, to overweight, and finally obese body mass index. The study showed a very similar food mix between underweight and obese individuals.4

A Harvard study on childhood obesity of 14,000 American children came to a conclusion that snack foods and soda were not linked to obesity. While snack foods may have had low nutritional value, they were not an important independent determinant of weight gain among children. The study helped to reinforce a growing understanding that the lack of physical activity could be a more critical cause of childhood obesity.5

In a joint 2004 study by the United Health Foundation, the American Public Health Association, and Partnership for Prevention, 18 personal, community, and public health factors were used to measure the health of Americans. The study concluded that there had been a 17.5% improvement in overall health in the last 15 years but that the rate of improvement had slowed significantly. The rate of improvement was about 1.5% per year in the early 1990s, but that rate had slowed to less than 1% in recent years. A 25% reduction in the number of smokers since 1990 from 29.5% to 22% may have been the biggest factor in improved health.6

There was a general feeling that most consumers believed the food industry was not primarily responsible for the health problems faced by obese people. People had choices regarding where and what they ate. There was a feeling the food industry should not be legally responsible for the health problems of consumers who chose to eat at quick-service restaurants on a regular basis.

A very recent article by Food Processing stated that the message from analysts was make healthier products. However, the article contended that maybe food companies were being made the “scapegoat.” The article contended that consumers were more worried about vanity than health when it came to obesity. Additionally, there could be a number of other more relevant factors causing obesity such as the reduction in smoking, stress, safety and security concerns, and a sedentary lifestyle.7

The snack-food industry grew by about 2.0% in 2002 and 3.6% in 2003. People in their 60s and 70s were considered light users, middle-aged (40s and 50s) who grew up on snack foods were heavy users, and youth were heavy users. Snack food consumption by teens was nearly six times higher than just five years ago.

While lunch had always been a prime target for snack foods with salty snacks as a favorite lunch item, dinner was becoming a much more popular time for snacks as well. Snacking was perceived as healthier probably as a result of the advertising emphasis on healthy snack foods. While natural products were gaining increased interest, taste was still a primary determinate for food preference.

Diets still attracted a lot of attention, from low carb, low sugar, low fat to high protein, but the trend seemed to fluctuate. The interest in low fat seemed to peak in the late 1990s, and the low-carb diet increased attention. In 2003 and 2004 more than 600 new low-carb products were introduced into the market. The biggest growth in low-carb products was in snack bars up 61% and salted snacks up 21%. The target market for organic and natural snacks seemed to be the female aged 25 to 44.

CASE CONCLUSION

The importance of diet and nutrition in peoples lives was gaining increased awareness by the public and rightly so. There were several ways a healthier lifestyle could be achieved from eating habits to exercise routines. Regardless of any positive or negative publicity related to nutrition issues, Herr’s was going to be influenced by changes in consumer behavior. An excellent company needed to anticipate changes, know how they might impact operations, and respond accordingly. Daryl felt he had a good understanding of the nutrition situation; the key decision was if the company should introduce more health sensitive snack foods. Daryl needed to think of ideas and present feasible alternatives to top management.
Herr Foods Inc lends itself to an open-ended or directed discussion format in a classroom setting. Since healthy eating and obesity have recently gained considerable attention in the public spotlight, this case study may lend itself to a variety of presentation formats including role playing, a debate format, videos, on-line dialogue, web based research, or panel discussion. Essentially everyone consumes some amount of fast food and snack foods on a regular basis, and has an opinion on healthy eating and over eating. Side issues related to this case are almost unlimited including:

- parents of an obese child
- school lunch programs
- health insurance issues
- potential lawsuits
- sedentary lifestyles
- the importance of exercise

While this case focuses on the snack food industry, certainly the fast food industry is receiving the greatest exposure regarding healthy eating and obesity. Nationally known companies have taken actions in both directions when it comes to promoting its product lines from supersize portions to healthy choices. A secondary objective of this case could be to branch off into other industries or related issues to examine the extent of this dilemma on the public conscious. The instructor could use any number of presentation approaches to expand this topic and the related discussion. The movie/documentary Super Size Me could be an excellent introduction to the presentation of this case.

Some or all of the suggested questions listed below can be used depending on the issues being addressed. The suggested questions also do not represent an all inclusive list, as many others can be added at the discretion of the instructor. In addition to the questions below, a comprehensive set of teaching notes with suggested answers is available from the author.

1. How should Daryl Thomas address the issue of health concerns of snack foods?

2. Consider the feasibility of the decision of more health sensitive snack foods from a business policy and corporate culture and ethics perspective. Identify the critical issues which could impact this decision process.

3. Should Herr Food’s develop a more health sensitive selection of snack foods?

4. What kind of a contingency plan, if any, should Herr Foods develop to answer critics or public sentiment if there is a backlash against the company concerning the health food issue?
ENDNOTES


