Ethical brands

Turn on, tune in, sell out

In the past decade, multinationals have gobbled up ethical brands – with huge benefits to both parties, argues Jon Entine

In the early 1980s, Gary Hirshberg, then an environmental activist and author of a book on wind-powered water pumps, launched with a friend a school in New Hampshire to teach sustainable agriculture. Reflecting the values of many young people of his generation, the pair wanted to change the world. They owned a few Jersey cows and a recipe for a great-tasting yogurt that they sold to help raise funds. But the homemade organic treat was so well received they soon changed their working model. They realised they could serve the environment better by running a yogurt farm than by teaching other farmers. They founded Stonyfield Farm, now the biggest organic yogurt maker in the US.

But being a hit in New England, an oasis for maturing hippies, was one thing; going mainstream was another. Hirshberg, who gradually assumed management control, failed to attract institutional investors in the late 1980s and 1990s even as sales steadily grew. Big business and venture firms were sceptical about the prospects for what they suspected was a fad – organic and natural products. They doubted whether it could evolve into an enduring business.

"I had a great company," Hirshberg jokes. "I just had no supply and no demand."

We know how that story turned out for Stonyfield and the array of entrepreneurial companies that folded social ideals into their operating DNA. The list of such companies snapped up by or forming partnerships with global conglomerates is staggering. Among the best known: chocolatier Green & Black's, now owned by Cadbury; cosmetic companies Body Shop and Aveda swallowed by L'Oréal and Estée Lauder respectively; Tom's of Maine toothpaste owned by Colgate-Palmolive; lip balm maker Burt's Bees acquired by Clorox; and PJ Smoothies snapped up by PepsiCo.

Are ethical firms and their founders turning their backs on "capitalism with a conscience"?

That's just the tip of the natural products iceberg. The biggest boom has come in the organic products sector. Growth in retail sales has been 25% or more annually since 1990, according to the US agriculture department. Although rising fuel and food prices are nibbling at growth rates, the organics market is expected to reach $24bn in sales in the US this year and more than twice that worldwide, and it is forecast to continue expanding at 20% a year.

The turning point came in the late 1990s, when for the first time more organic food was bought in conventional supermarkets than in other venues. The big boys took notice. Mars snapped up control of the UK's first and fastest growing organic dairy, Rachel's Organic, only to sell it to Dean Foods, the US food multinational, which had gobbled up Horizon organic dairy products.

As demand rocketed, food giants such as General Mills, Heinz, Coca-Cola and Kraft invaded the organics market en masse. Tyson, Dole and other mega-businesses rolled out organic lines, and investment firms, including Lion Capital in the UK and Solera Capital in the US, went on acquiring binges. Even working-class-focused big box stores, such as Wal-Mart, have found tremendous growth by expanding into organics.

Good, bad and ugly

It is easy to understand why smaller, growing concerns are tempting targets for global food firms. Multinationals, bloated with cash, know it is cheaper and reduces the steepness of the learning curve in entering hot market segments to buy going businesses rather than innovating. And many of the small firms they are chasing have hit a wall of sorts, strapped by cash-flow and distribution challenges. To scale up, they need to sell out, trading authenticity for ubiquity. It is globalism at its best and worst: corporate Darwinism, with hippie entrepreneurialism an inevitable victim.

But the controversy has not centred on economics. It is focused on values. Are ethical firms and their founders turning their backs on "capitalism with a conscience" – the very principles they claim motivated them to start their businesses in the first place? Can socially responsible businesses hope to transfer their social values into the mega-corporations that are swallowing them up? What are the pros and cons of this trend?

"The corporate takeover of organics can be seen as both a success and a failure for the organic movement," says Phil Howard, assistant professor in the department of community, agriculture, recreation and resource studies at Michigan State University, who has produced an instructive series of graphics illustrating the takeover bonanza.

"On the one hand, the acreage devoted to organic production, without synthetic pesticides, increases every year to meet the market demand. On the other hand, some of the ideals of the organic movement, which were in large part a response to industrial agriculture, have fallen by the wayside. Organic increasingly resembles the global, industrial agriculture system it was created to combat."

Despite obvious benefits – spreading the gospel of green to a wider audience – the acquisition boom has not gone down well with many organic purists and some socially responsible business activists. "Is Your Organic Food Really Organic?" asks the US-based Organic Consumers Association website. Another headline foretells a dire future. "Now large corporations … are moving to … seize control. For the sake of the earth and our health we must stop them."

The "small is always beautiful and best" crowd reflexively assumes that big business is intrinsically less ethical, with lower quality standards, than supposedly well-meaning entrepreneurial firms. That's a dubious claim. The romance of "natural business" pictured on websites, discussed in rapturous articles in green business journals, and extolled in Harvard and London Business School case studies – idealistic entrepreneurs travelling the world for exotic natural ingredients; farmers hand-milking cows and mixing yogurt in the barn; ranch hands picking fruit fresh from the trees; chickens and pigs cavorting in spacious outdoor pens – was always as much image as practice.

Human nature and competitive business realities have pushed many self-proclaimed socially responsible companies to cut corners on the progressive practices that were so easy to execute when they were start-ups. By the time many were acquired, they had achieved iconic status based in part on a muddled history of good intentions that had hardened into legend.

Body Shop: rumours persist despite roaring success

Once considered pure as the driven snow, Bert's Bees, a "Maine-based company", has long sourced its beeswax in Ethiopia, shipped at great environmental expense to its anti-union factory in North Carolina.

Anita Roddick took the name and marketing concept of Body Shop from two American entrepreneurs who opened their stores in San Francisco six years before. Questions were also raised about her early stories of sourcing natural ingredients in distant locales.

The "small is always beautiful and best" crowd reflexively assumes that big business is intrinsically less ethical

Natural juice company Odwalla hit trouble after its founder, Gene Stelpenpohl, cut corners in its production processes to meet booming demand, leading to an e-coli outbreak in batches of juice made from apples that had fallen into natural fertiliser – dung – that resulted in dozens of injuries and one death in 1997. The list goes on and on.

Even the most ethical of companies compromise their stated intentions, with many practices falling below the everyday standards of "evil" corporations. "Everyone talks about how environmentally progressive our business is. That's bull," Gene Kahn, founder of Cascadian Farm, now owned by General Mills, told me shortly before he sold out. "The conventional food industry, for all its faults, has higher levels of consumer disclosure and ethics than organics. In theory, organics creates an enormous opportunity to live our lives as caretakers," he said. "It doesn't necessarily guarantee that."

Exchange of values

Ben & Jerry's was one of the first start-ups to catch the natural and organic wave. Floated on the stock market in 1983, it had a market value of $150m by 1999, when acquirers came calling. Devotees of the ice cream and its campaigning philosophy manoeuvred to scuttle the deal, setting up a website and circulating petitions warning that big business wanted to "skin the company alive and use its gentle lambskin brand identity to fool unsuspecting consumers into purchasing their soulless profit-driven products".

But in 2000, when Unilever offered three times its floundering stock price, Ben & Jerry's founders – Ben Cohen and Jerry Greenfield – had little choice but to heed their fiduciary duty to their shareholders

Ben Cohen: not a happy seller

and sell. "We didn't feel great about it from the start and throughout," Greenfield recently told the Guardian newspaper. "It was extremely difficult, heart-wrenching. It was a horrible experience for me and I can probably say it was horrible for Ben too." Cohen has washed his hands of the company and moved on to other ventures.

Takeovers are looked upon sceptically in the close-knit ethical investing community. "We're not really excited to see these acquisitions occur," says Kevin Ranney, managing partner and director of research at Jantzi Research, the Canadian social research organisation. "The reality is that what Ben & Jerry's was all about is now buried deeply within a massive corporate structure, and it has relatively little impact on anyone's assessment of Unilever."

Many people believe the quality of the ice cream has fallen, as Ben & Jerry's now uses high fructose corn syrup – made in a complex industrial process where starch is extracted from corn and converted with acids or enzymes into glucose and fructose. Greenfield complains that the company is a clone of its giant owner. "It feels different to have our manufacturing staff report to Unilever," he has said. "They are not our people any more."

But maybe that is not such a bad thing. Ben & Jerry's may no longer be autonomous, but it operates with an unusual degree of freedom in an otherwise button-downed multinational corporation and has continued to use its marketing leverage to promote social initiatives. Unilever has also dramatically streamlined operations, revived an eroding brand, and moved to rationalise franchise operations. It is arguable that without the intervention of Unilever or another corporate white knight, today Ben & Jerry's values would be mostly symbolic, talked about in the past tense.

Ben & Jerry's struggles mirror the fate of another greying brand, Body Shop, which went into a long decline in the early 1990s, beset by dated store designs, rebellions by money-losing franchisees, and fierce competition from nimble competitors with higher quality products. L'Oréal came to the rescue with its takeover in 2006, accelerating the buyouts of disgruntled franchisees, refreshing the stores, radically overhauling the product line, and running the business with a professionalism that had been sorely lacking.

In both cases, the founders had in effect made their companies vulnerable to takeover through years of bungling and mismanagement, lackadaisically responding to an increasingly competitive marketplace that overwhelmed the expertise of the mediocre executives they had vetted. They were better entrepreneurs than business leaders. At least in these two instances, there

Buyouts revive the commitment of struggling ethical pioneers to social causes

was indeed a transfer of values; the buyouts revived the commitment of these struggling ethical pioneers to social causes.

Preserving ethics

Despite grumbles, many of the recent takeovers have gone relatively smoothly. By most accounts, Cadbury's acquisition of Green & Black's has been a classic win-win. One of the organic chocolate firm's founders, Craig Sams, still runs the business. Its new owners have toed the line on its ethical trade deals and brought the organisational discipline and distribution savvy that has sent revenues soaring, up almost 50%, while competitors are running flat.

Did Sams want to stay independent? He could not have done even if he had wanted to, he says. "It's one of the things that all small companies come up against," Sams says. "You are doing really well but whenever others see that you have done something clever they all come after you. Supermarkets launch their own brands; wholesalers knock you off. The market becomes fragmented and diluted and other people mop up. So, instead we took in cash to invest in the brand."

In his 1993 book, The Soul of Business, Tom's of Maine founder Tom Chappell says he had rejected suitors "because I didn't want to become them". But facing the same competitive reality that prompted Sams to sell, Chappell brokered a majority stake in 2006 to Colgate-Palmolive, a company not known for its high ethical standards. "We're going to do business as we have done business," his wife, Kate, declared shortly after the deal was sealed. Holding firm, Tom remained chief executive and the Chappells were given guarantees on a range of operational practices and social commitments, some of which they believe are progressively influencing Colgate's operations.

Stonyfield Farm is widely recognised as the model for an enlightened sell-out. By 2001, it had blossomed into a $78m business. But many of its 300 socially committed shareholders were eager to cash out after years of capital infusions. Gary Hirshberg looked into going public or offering shares directly to customers, but neither structure offered what he was looking for: a way to meet his obligations to shareholders while maintaining operational oversight of his creation. He then had talks with 20-odd companies proposing what everyone said was impossible: to sell a majority stake but retain total control.

In what became a breakthrough agreement – it is known today in ethical marketing and merger and acquisition circles as the "Stonyfield deal" – Hirshberg persuaded Danone to buy 40% (it later raised its stake to 80%), but leave Hirshberg as chief executive with no interference from the parent company.

Hirshberg recalls with some humour being interviewed, along with Danone chief executive Franck Riboud, by a Wall Street Journal reporter the day the deal was announced.

"He peppered us with all the usual questions," Hirshberg says. "He asked about return on investment, return on equity. But Riboud cut him short, he just stopped him." Hirshberg assumes a thick French accent as he recalls: "'We expect this will be very good for our shareholders, a very good investment,' Riboud said to the reporter. 'But that's not why we did this. Stonyfield represents an ethic that we, Danone, have to learn and develop if we hope to compete in the 21st century.'"

"He got it," Hirshberg says, who believes that both companies have benefited from the partnership. Since the acquisition, Danone has taken positions in three new organic ventures, increased its sustainability reporting, created a carbon footprint accounting structure for its drinks business and pioneered an anaerobic biogas digester water treatment plant that Hirshberg championed over the objections of some Danone engineers.

Enlightenment dispenser

"You need an enlightened and intellectually flexible acquirer if you want to preserve your values," he says. It has taken adapting by both sides. "There are special expenses to running a socially responsible business, using higher quality ingredients and committing to social causes. But because we've never compromised on our values, we've retained a strong bond of loyalty with consumers. This is not the 'advertising model' of a typical business. As a result, selling costs are also far, far, lower."

He adds: "But I had a responsibility too. For this to work for Danone, I had to deliver on finances. We've done that."

Since the deal, Stonyfield's revenue has grown more than fourfold. And both partners could not be more pleased.

Can you really scale up, sell out, and still preserve your reputation as a socially responsible business? Even visionary leaders such as Hirshberg and Riboud, who have structured their partnership to preserve Stonyfield's ethical identity, face challenges in the years ahead as sales and market share grow. As Hirshberg acknowledges, emotion, even more than rationality, drives brand loyalty. The moment you take your special, authentic, limited-edition products and turn them into mass-market commodities you risk alienating the very customers who carried you to success. That's the next challenge for ethical brands now operating under the umbrella of major companies. ■

> ***"You need an enlightened and intellectually flexible acquirer if you want to preserve your values"***
> *Gary Hishberg, Stonyfield Farm*