

500

HORMEL: COMPANY PROFILE

REVENUES

PROFITS

EMPLOYEES

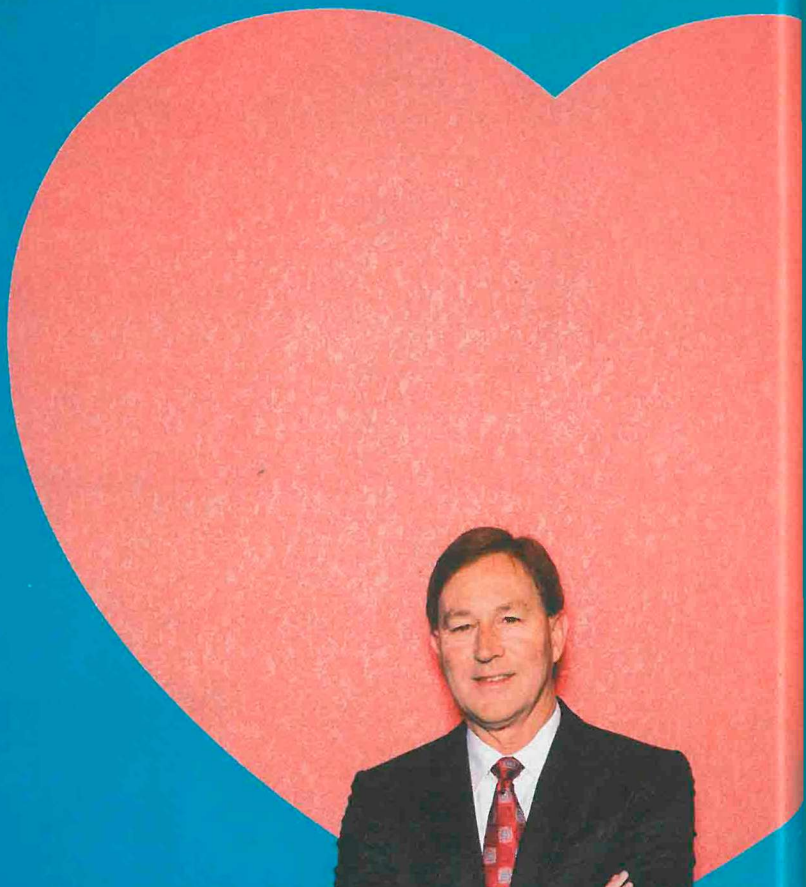
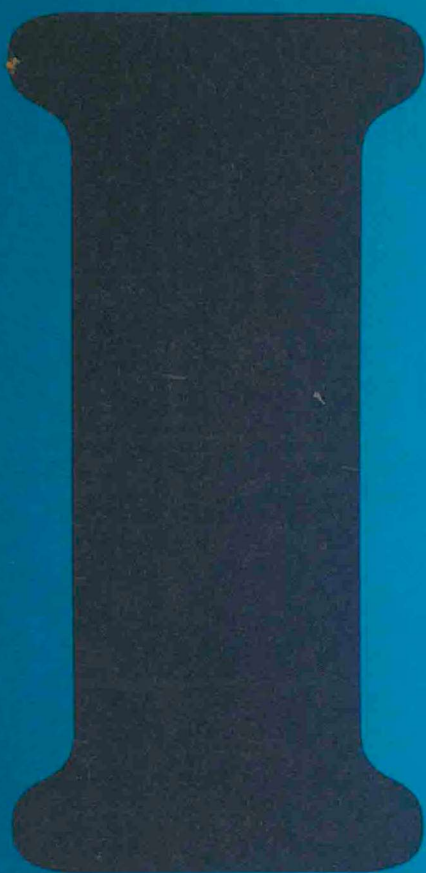
TOTAL RETURN TO SHAREHOLDERS  
(2005-2015 ANNUAL RATE)

\$9.3 BILLION

\$686 MILLION

20,700

19.2%



# HORMEL'S NEW RECIPE FOR SUCCESS

PHOTOGRAPH BY ACKERMAN + GRUBER



**CAN-DO EXECUTIVE**  
HORMEL CEO JEFF ETTINGER  
INSIDE THE NEWLY OPENED SPAM  
MUSEUM NEAR THE COMPANY'S  
HEADQUARTERS IN AUSTIN, MINN.



As it celebrates its 125th birthday, the old-school maker of processed meats is riding a wave of growth driven by product innovation and boldly moving into the world of organic food and healthy snacks. BY KEN OTTERBOURG





**The cornfields come right up to the edge of Austin, Minn., which is the hometown of Hormel Foods and one of just a handful of small places left in America that a very big company still calls home. Nearly everything in Austin owes its existence to Hormel. They are bound together, and mostly at ease with their isolation and the fact that much of what people take for granted in the rest of the country has either not yet arrived or has already left. There are no Uber drivers. No Starbucks and no Toyota dealer. The Target closed last year. Staples, the year before. The only Airbnb option is a fifth-wheel trailer.**





**SMOOTH OPERATOR** JARS OF SKIPPY PEANUT BUTTER ROLL DOWN THE LINE AT A FACTORY IN LITTLE ROCK. HORMEL BOUGHT SKIPPY IN 2013. SINCE THE END OF 2013, THE NO. 2 PEANUT BUTTER BRAND'S U.S. MARKET SHARE HAS GROWN FROM 16.6% TO 18.6%.

Hormel's best-known product is Spam. It's easy to joke about a company built on meat that comes in a can, but it turns out that Hormel is having the last laugh. For the past 10 years, it has been on a tear. Revenue has increased from \$5.4 billion to \$9.3 billion, boosting its ranking in the *Fortune* 500 by nearly 100 spots, to No. 304 this year. Earnings have more than doubled, the dividend has almost quadrupled, and the stock has returned roughly 400%. The growth has

been fueled by a flood of new products: everything from peanut-butter snacks to single-serve turkey sticks to a food-service burger made with chicken, quinoa, and, yes, kale. All were developed in Austin—proof that innovation is defined by people, not zip codes.

But Hormel's success is also a story of acquisition and the persistent colonization of new food worlds. In the past five years, the old-school meat producer has paid more than \$2.3 billion to acquire a portfolio of brands that sell organic food, ethnic food, and health(ier) food. They include Wholly Guacamole, Muscle Milk, Skippy peanut butter, and Applegate Farms. In May it agreed to buy Justin's, the ultrahip nut-butter company, for \$286 million.

There's no tofu Spam on the horizon (phew!), but Hormel is rolling out a pea-based protein shake and experimenting with the online sale of bespoke hams. Not to worry, the mainstream processed meats that add so much to Hormel's bottom line—and our waistlines—aren't going away. So what we're witnessing is a company in full embrace of the cognitive dissonance of our collective diets, where we eat like a vegan at lunch and snack like a carnivore on the drive home. It is a familiar story across Big Food, as companies invest in the eating habits of the emerging America—one that is more diverse, more pressed for time, and more concerned about ingredients and the ethics of food production. By that narrative, it's not that Hormel has a better recipe than its peers. But it may have better cooks.

**H**ORMEL TURNS 125 THIS YEAR. And it is by nature an incremental company—a place of evolutionary rather than revolutionary change. In this context, many of its recent deals seem more like sensible experiments than strategic shifts. But if there were any questions about Hormel's direction and its appetite, they were answered two years ago. Hillshire Farms was on the market. On paper, the two companies were a nice fit, with Hillshire's strength in deli, sausage, and hot dogs complementing Hormel's clout in bacon, turkey, and grocery. Hormel, however, didn't bite.

Why pass? Price was a factor. (Tyson Foods ended up buying Hillshire for \$7.7 billion.) But there was something else as well. Jeff Ettinger, Hormel's direct and self-effacing chairman and CEO, says the company's reluctance to move on the deal underscored a critical pivot in thinking: Hillshire was just more of the same. "We felt that Hillshire was a mainstream processed-meat company," he says. "We really preferred to put our bets on some of those newer spaces."

Applegate Farms fit that bill. Its vision is to "Change the Meat We Eat," and it's not always clear if Applegate is a meat company that advocates agricultural issues or an NGO that happens to sell cold cuts. Since its founding in 1987, it has built a passionate following among consumers willing to pay extra for an all-natural hot dog. Stephen McDonnell, Applegate's founder, is still a leading voice challenging the livestock industry's default use of antibiotics and a supporter of greater labeling of GMO ingredients. Hormel



remains on opposite sides of these issues.

McDonnell, who is now 61, suffered a stroke in December 2013, and by March of the next year he had retained Goldman Sachs to help him sell the company. McDonnell, who has never before spoken publicly about the process, says he and the team from Goldman interviewed representatives from nearly every major meat company in the world. There was lots of interest.

Hormel gained the inside track through a decidedly Midwestern, old-fashioned approach. "Jeff reached out directly on his own," recounts McDonnell. "And he was the only one that did this, and he said, 'Could we have dinner?'"

They met in New York City, at Maialino, part of Danny Meyer's restaurant empire. There was no real business talk, just conversation about values and vision. But for McDonnell, it sealed the deal. "I said from the beginning that I was going to look into somebody's eyes, and I was going to trust them, and Jeff was that guy."

## EXPANDING ITS MENU

In the past five years, Hormel has made a series of acquisitions that move beyond its processed-meat heritage. — K.O.

The Applegate deal was announced on May 26, 2015, with Hormel paying \$774 million for a company with roughly \$340 million in sales. Unlike Hormel, Applegate owns no farms or processing plants. From bird to nugget, it's all done through third parties. What the company did have was a groovy office in Bridgewater, N.J., filled with designer chairs, folk art, and a bunch of employees who had some serious concerns about what the new owners—referred to tongue in cheek as "Hormellians"—would demand.

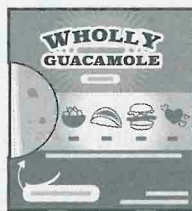
Gina Asoudegan is the senior director of mission at Applegate, charged with working with environmental and animal-welfare groups across a wide range of issues. "It was hard for me in the beginning to believe that Hormel, the makers of Spam, would somehow be okay with the mission and the things that I want this company to do in terms of raising the bar on animal welfare and things like that," she says. "I wrestled with that. I'm not going to lie."

But she said she came around after a trip to Austin. She heard the meat managers at Hormel talk about the need to clean up labels and remove ingredients to better reach millennials. What she realized was that it didn't have to be about Applegate selling out. Maybe Hormel was buying in, and moving—albeit slowly—toward a different, perhaps more enlightened, model of food production.

Not surprisingly, all this corporate kumbaya is at times met with a side order of skepticism. Applegate's social media team still spends lots of time assuring customers that nothing has changed and that Applegate operates independently. That's not quite true, of course, although company officials insist that Applegate is actually trying to be more assertive on food-production issues because the competition in the organic-meat business has gotten stiffer, and the company's activism is a core attribute of the brand.

### FRESHERIZED FOODS

**Year: 2011**  
**Price: Undisclosed**  
Hormel bought the maker of Wholly Guacamole and Wholly Salsa through its MegaMex 50/50 joint venture with Mexico City-based Herdez del Fuerte. In filings, Hormel said it invested \$61 million as its share.



### SKIPPY PEANUT BUTTER

**Year: 2013**  
**Price: \$707 million**  
The No. 2 peanut butter brand was bought from Unilever in two separate deals. [The business unit in China was sold separately.] Under Hormel, Skippy has developed new products like its P.B. Bites snackables.



### CYTOSPORT

**Year: 2014**  
**Price: \$420 million**  
Founded by the father-and-son team of Greg and Michael Pickett in 1998, the Benicia, Calif., company makes Muscle Milk protein-supplement powders and bodybuilding beverages that are favorites among workout-aholics.



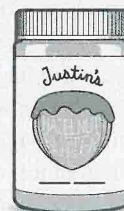
### APPLEGATE FARMS

**Year: 2015**  
**Price: \$774 million**  
The New Jersey organic and natural meat company with a vision to "Change the Meat We Eat" opposes overuse of livestock antibiotics and advocates better GMO labeling—putting it in opposition to its new parent.



### JUSTIN'S

**Year: 2016**  
**Price: \$286 million**  
Hormel paid nearly three times sales for its most recent acquisition, the ultrahip, Boulder-based maker of "naturally delicious" nut butters and healthy snacks founded by vegetarian entrepreneur Justin Gold in 2004.





**M**IDSIZE COMPANIES that make healthy food are prime targets for acquisition by the majors. "The 'better for you' category is a high-velocity area in terms of deals," says Rodney Clark, a founder with the M&A firm Aspect Consumer Partners. "It's driven by corporate competition. Underpinning it all is that consumers have gotten smarter and are looking at labels. For the companies with the older, more traditional, less healthy brands, the question is, How do we continue to connect with consumers? It's hard for them to disrupt themselves."

Justin's has revenues of less than \$100 million. The steep price Hormel is paying—nearly three times sales—reflects the strong growth in the specialty-nut category and also the challenges Hormel would have faced building its own business off the Skippy's franchise.

The food business is incredibly transparent. The market-research companies can slice and dice checkout data, so it's hard for a boutique company to fly under the radar. Prices for deals have increased in recent years, as private equity also chases those businesses. Hormel's pitch is based not just on dollars upfront but also on showing respect for the owners and a promise to grow the acquired company after the ink dries.

Justin Gold, the founder and majority owner of Justin's, said that Hormel's team approached him late last year. One of the first things he did was to reach out to McDonnell and the owners of Muscle Milk about their experiences under Hormel. In both deals, the existing management and headquarters were largely kept intact. And neither brand carries any labeling acknowledging Hormel's ownership.

"These guys have a credibility for doing what they say they are going to do," says Gold. "The founders are very happy with the way that Hormel has grown their business."

“

**WE'RE NOT AS POOR OR AS OLD AS PEOPLE THINK WE ARE," SAYS A HORMEL EXEC ABOUT THE STILL-ROBUST MARKET FOR SPAM.**

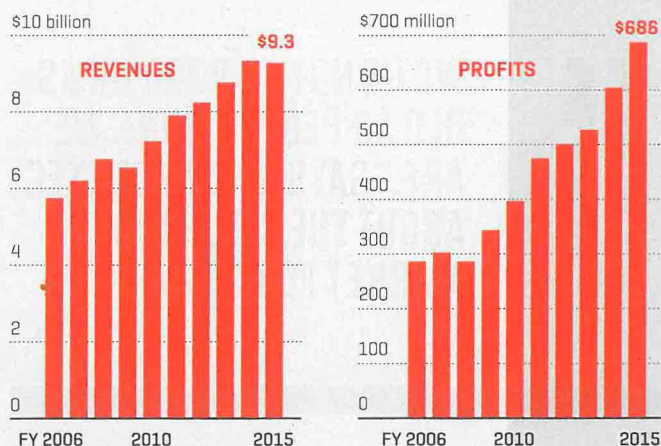
**A**T HORMEL'S LOW-SLUNG corporate offices next to the rumble of Interstate 90, the receptionist shows up before 6 a.m. Most employees are there by 7, a nod to the company's meatpacking roots. Hormel's leadership team averages 26 years with the company. It is overwhelmingly white and male—far less diverse than the company's overall workforce, its board of directors, or its customer base. It's an issue that Ettinger says he is working on, but one that is made more difficult by Austin's location and Hormel's propensity to promote from within.

Ettinger came to Hormel in 1989 as an attorney and then transferred to product management. He started out with canned chili and eventually led Hormel's Jennie-O turkey business. In 2005 he emerged as CEO, and a few years later the Hormel team ramped up its bolt-on acquisition strategy.

Hormel has five divisions: grocery products, including a joint venture with Herdez del Fuerte that is the largest seller of Mexican food in the U.S.; refrigerated meats, which are nearly half the company; Jennie-O, which has bounced back from the crippling impact of avian influenza last year; specialty foods; and international. Running in the background, primarily in refrigerated meats, is a billion-dollar food-service operation, which provides everything from precooked ribs and the guacamole at Subway to the toppings that go on all those pizzas sold at Casey's General Stores across rural America. Unlike many of its competitors, Hormel rarely uses food brokers. Its sales force is on the ground, and the insights from customers speed the development of new products, both for retail and the trade.

Take bacon. Americans love it. Many food-service operators hate it. The cleanup after a breakfast shift is a nightmare, and it's easy for a small distraction during the cooking to lead to an overdone tray. These are what kitchen managers call pain points. So Hormel spent five years creating a machine that churns out fully cooked bacon that can be reheated on-site and has the proper taste and texture—delivering the right amount of chewing delight, known to food scientists as jaw stress. The patent is pending, and it has been an enormous success for institutional customers.





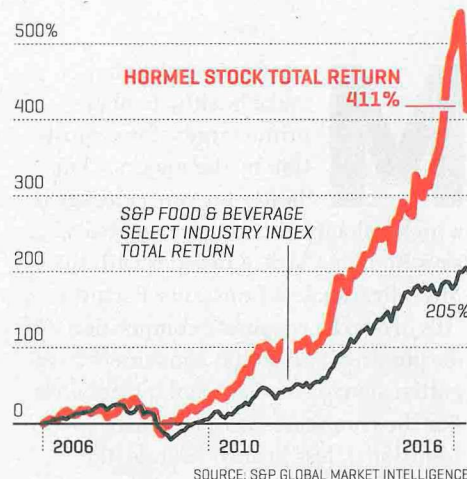
### PACKING ON THE PROFITS

Hormel has more than doubled its earnings in the past decade on strong sales growth, and its shareholders have benefited.

And then there is Hormel's entry into the peanut-butter wars. Peanut butter is now a two-jar competition between Skippy and Jif, which is made by J.M. Smucker and has twice Skippy's U.S. market share. (Skippy leads internationally.) Peanut butter is one of those products that are in almost every household. And the brand you grow up with often ends up being the one you grow old with.

Hormel's tactic here hasn't been so much to win the category but rather to change it—finding new uses for peanut butter. Soon after buying Skippy, Ettinger challenged his development team to take the product out of the jar, and to do it quickly. The result? Skippy P.B. Bites, marble-size munchies, launched last year. Its target consumer: boys and girls who arrive home from school “hangry,” i.e., so hungry they're angry. Sales are good, but the key takeaway is that nearly half the shoppers who buy the snacks for their kids are Jif loyalists. That said, Skippy's market-share gains are coming mostly at the expense of smaller brands, not Jif. But the Hormellians are hopeful.

For sulky teenagers who have outgrown Oscar Mayer's still mighty Lunchables empire, Hormel has developed REV, which is a piece of meat and a piece of cheese wrapped around flavored flatbread. No condiments. No lettuce or pickles. To say it is dry is an understatement. But that



SOURCE: S&P GLOBAL MARKET INTELLIGENCE

misses the point. It's designed to be eaten with one hand while the other hand keeps texting. REV, already a \$50 million business, was developed in part from the work of Hormel's in-house anthropologist, Tanya Rodriguez. She visited university campuses and noticed how many students didn't put down the phone even during meals. “The table has become more of an irrelevant symbol, more of an archetype,” she says.

**T**HE NEW SPAM MUSEUM opened in April in the heart of downtown Austin. The gift shop notwithstanding, it is less cheesy than you might expect. There was a time not that long ago when Hormel took Spam very seriously—perhaps too seriously. In 1995, for example, it sued Jim Henson Productions over trademark infringement for a boar named “Spa'am” who makes a cameo in the film *Muppet Treasure Island*. Hormel claimed the character's lack of cleanliness reflected poorly on its products. The court sided with Miss Piggy. An appellate judge later wrote, “The district court found no evidence that Spa'am was unhygienic. At worst, he might be described as ‘untidy.’”

Nicole Behne is a marketing director in Hormel's grocery products division, in charge of selling Spam, Mary

Kitchen Hash, and Dinty Moore stews. None of those products has quite had a PBR or Old Spice hipster-revival moment, but Behne is ever the optimist. She's trying to tie Dinty Moore to so-called "lumbersexuals"—young men who wear flannel but don't wield an ax.

The Spam you buy today is made to last for three years. Behne describes it as a shelf-stable and functional product, which sounds more like a paperweight than something you might want to put in your mouth. Spam typically occupies some of the worst real estate at the supermarket. But it is still a brand with estimated sales of \$300 million and one that's growing about 3% each year. "We're not as poor or as old as people think we are," says Behne. Spam's newest line extension is Spam Mezclita, a combination of Spam and processed cheese now sold only in Puerto Rico. A version targeted toward Mexican-Americans didn't catch on and is being discontinued. Ditto for Spam Snacks, dried morsels that came in a pouch.

Overseas, Spam's prospects are stronger. Because of restrictions on the importing of meat products, most foreign Spam sales (upwards of \$500 million) are through licensing agreements. South Koreans consume a staggering \$175 million of Spam each year, much of it in a spicy noodle-and-kimchi dish called Troop Stew, which is a staple across the country.

The great frontier is China. In late 2014 the Chinese government imposed for the second time a ban on Spam imports. Since last spring, the country has been officially Spam-free. That will change at the end of 2016, when Hormel opens up a factory in Jiaying, adding to its existing production of processed meats in China. Unlike the Koreans or the Filipinos, the Chinese aren't Spam-crazy—yet. "The rising middle class is where the opportunity is," said Larry Vorpahl, the president of Hormel Foods International. "Just like everybody else, they need convenience. Pre-cooked and flavored, ready to go—that's the market where disposable income is going to be."

**H**ORMEL'S FLAGSHIP FACTORY, where it makes much of its Spam, sits halfway between the company headquarters and the new museum. Last year, Hormel found itself in an unflattering spotlight when workers at the contract slaughterhouse inside the factory were filmed hitting animals with paddles, among other apparent violations. The USDA issued no fine, but the incident underscores an important point. Despite all the branding and clever marketing, Hormel is at its core a company that starts with animals entering through one door and meat leaving through another. It is often hard and demanding work, built around processing 1,300 hogs an hour. In 2007 the complex came under scrutiny after public-health investigators identified a cluster of neurological disease among employees who worked on or near the brain-harvesting station.

Richard Morgan is the president of Local 9 of the United Food and Commercial Workers Union in Austin, representing 1,500 Hormel employees and another 1,000 at Quality Pork Processors, the subcontractor on the slaughter side of the sprawling factory that was brought in on the heels of a protracted and at-times violent strike in 1985 that made national headlines.

"These are the toughest jobs in the world," Morgan says. The union signed a new five-year contract with Hormel last year after taking two strike authorization votes. It is the best contract Morgan can recall, and yet hourly wages increased only 2%, from \$16.90 to \$17.30. That's one indication of Hormel's drive to squeeze costs, boost profits, and achieve its goals of 10% earnings growth on 5% revenue growth. Another indication: its fight to avoid paying workers for their time putting on protective clothing at a factory in Wisconsin. (The state's supreme court sided with the workers.)

Morgan has other long-term worries. He's concerned about where the next generation of meatpacking employees is going to come from. His new members are mostly immigrants—from Latin America,



Asia, and Africa—who are for now willing to endure the pace, the stress, and the cold of the packinghouse. Hormel pushes hard, says Morgan, but he also recognizes it as better than its peers. It's a stable company that has few layoffs. And there is still a profit-sharing program that, come the holidays, can mean several hundred dollars in a worker's paycheck.

**H**ORMEL'S STABILITY is not simply because people today reliably eat bacon and chili, or because tomorrow they're going to switch to almond butter and microwavable vegetarian meals. It's more fundamental than that. Just under 49% of Hormel's stock, worth around \$9 billion at current prices, is controlled by the Austin-based Hormel Foundation, located in the basement of a squat office building kitty-corner from the museum. The foundation owns 5% outright—and gets that stake's \$16 million in dividends—but it also votes the shares of trusts established for the grandsons of George Hormel. Eventually, all those shares and their dividends will revert to the foundation.

Ettinger sits on the foundation's board, and he says the arrangement protects Hormel and lets it manage for the long term. Activist investors don't bother with the company because there's not a plausible end-game. He's quick to add that activists also tend not to bother companies that are performing well.

Jon Feeney, an analyst with Athlos Research, puts it this way: "Jeff Ettinger doesn't lose sleep over whether some bigger company is going to outmaneuver him and buy him—and that's by design, and it's a fundamentally correct way to do business."

According to its most recent tax return, the foundation gave away more than \$22 million in 2014 to local groups, principally the City of Austin and its public schools, the local community college, and the Hormel Institute, an affiliate of the University of Minnesota that is a leader in cancer research. Its most recent expansion

**HIGH-SPEED SNACKING**  
HORMEL DEVELOPED REV, A NEW LINE OF ON-THE-GO MEALS, WITH INPUT FROM ITS HOUSE ANTHROPOLOGIST, WHO NOTICED THAT TODAY'S STUDENTS DON'T PUT DOWN THEIR PHONES DURING MEALS.



includes a \$5 million microscope with near-atomic resolution.

"Oh, my gosh," says Bonnie Rietz, a former mayor of Austin who is the foundation's vice chair. "We are so lucky to have this. It's an amazing setup." She says the foundation's resources have kept the schools well-funded, paid for college scholarships, and poured millions into the institute. The latest project is working with a developer on an apartment complex for the institute's expected wave of new researchers, encouraging them to live in Austin rather than Rochester, some 40 miles away.

Hormel's early starting times discourage that commute. Instead, nearly all of the company's top executives are huddled in the same neighborhood of split-levels on Austin's west side. Their kids go to the same schools as the kids whose parents work in the factory, and they often pray at the same churches. Two months ago, Ettinger and Jim Snee, Hormel's president and Ettinger's heir apparent, worked the check-in table at a dinner before Austin High's prom. Each has a senior at the school.

All of this can sound bit hokey, but perhaps that's just the cynicism from the coasts talking. "When it's all said and done, Austin and Hormel are inextricably linked," says Snee. "You really get to know each other beyond just the workplace. For me personally, I think there is incredible value in that. You know who the individuals are, you know how they work, and you know what it takes to get things done."

And even in such a small town, that kind of thinking can sometimes lead to big results. **B**