

Food & BEVERAGE INNOVATORS

On June 17, 2015, the San Francisco Business Times held a forum to discuss the sustaining strength and continuing innovation in food and beverage manufacturing in the Bay Area with a group of executives from local F&B businesses. The conversation was hosted by the accounting firm Sensiba San Filippo LLP and moderated by San Francisco Business Times publisher Mary Huss.

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Matthew Jacobs
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Introduction by Karen Burns: Today's program is all about innovation. In business, innovation is hard. You have to take risks if you are going to innovate. I challenge you to assess your own teams, and determine whether you have the right players and the right products to win. If you do, you will set yourself apart from the competition.

Technology impacts the way we think about food and our food habits. Look at all the kids on their mobile devices and the increase in obesity, lack of exercise, unhealthy snacks. Think about the social evolution, from stay-at-home moms making dinners to families working to survive to make a living to needing things to be instant, a lot of dining out, a lot of immediate need to have things. Technology influenced all of that. It enhanced our foods.

Now we have a new generation that says, "Maybe some of those enhancements weren't exactly healthy for us." We are now seeing a shift to healthy convenience food because it still needs to be quick. We now see companies like Blue Apron, and today we are going to hear from Munchery.

Specialty food also is on the rise. The Specialty Food Association recently published a report indicating that since 2012 specialty food has increased 22 percent and is now a \$109 billion dollar industry. Compare that to all food categories which have just risen a mere two percent. Retailers have had to evolve. What once was a shelf dedicated to specialty food became an aisle, and aisles have become entire stores. Now over 80 percent of specialty food is sold through mainstream stores. Manufacturers have also had to evolve. 94 percent now offer some kind of all natural food product. 57 percent offer non GMO alternatives. And 55 percent say they are planning for gluten free products in 2015.

Q: What are some of the challenges to manufacturing in the Bay Area?

Todd Masonis: It's difficult. It's very expensive. For the new factory, I think we could have put it somewhere else, but we live here. San Francisco has a really interesting chocolate history. It's not enough just to have a building. So we are going to do even more classes and more education and more tours. We hope to do a chocolate salon maybe even a dessert bar and so find uses and revenue streams for the space instead of pure manufacturing.

Nicolas Bernadi: We have food production, with culinary talent, and how do we scale that? How do we make a hundred thousand high quality meals every single day in every city we are in without compromising great food? That's the first business challenges. The second is the technology challenge because we have a big technology platform for the food business and the delivery business. We have 800 employees now and operate in four cities: San Francisco; Seattle; Los Angeles and New York. In each city we have our own quality kitchen, our own chef, culinary talent, people working with local farmers.

How do we not compromise and yet be very affordable? We believe affordability is key.

On the delivery side, we have our own drivers who are employees, not contractors. In traditional restaurants you have an easy connection to customers. Our choices as a food company are limited to a cell phone, computer and delivery drivers. So for us it's very critical to treat our delivery drivers extremely well. They eat our food, have access to benefits.

Quick and fresh is the highest rising category in the sector of specialty foods. Energy bars are up 20 percent, refrigerated dips 19 percent, and refrigerated pasta, 17 percent. These statistics demonstrate the significance of specialty food and the significance of how those companies have had to innovate.

I'll give you an example of how we have had to innovate at Sensiba San Filippo. As a CPA firm, and advisor to food and beverage companies, we had a model that was very similar to most service providers which was an eat what you kill compensation model. We found that if we wanted to do something new, we had to stop doing something old. So what we decided is to get really good at our technical discipline and to focus by industry sector and get really, really good at that as well.

I lead our manufacturing distribution practice with a subsector specialty around food and beverage, and the leaders in our firm took it to another level. We said, "Customers want to work with people who make their lives better. What else can you do besides offer what everybody else offers?" So we started the East Bay Manufacturing Group. It's an organization that's dedicated to food and beverage executives, helping them to come together and learn and share their best practices.

Essentially, innovation is hard and it's scary, but it is necessary if you want to survive and thrive. Determine what your competitive advantage is, continually work to refine it and redesign it, and if you do, you will have better customers and better margins, and you might even be champion of your chosen niche.

Matthew Jacobs: We have a pilot factory in South San Francisco, but most of our manufacturing is in Peoria, Illinois, where we have repurposed an old Pabst Blue Ribbon brewery. We are growing micro algae in large stainless steel vats.

Q: Do you feel pressure to be acquired by the big national companies versus fighting it out alone for market share and shelf space?

Jon Sebastiani: Every time I raised capital via private equity, there were strings attached to that capital and that capital diluted our own interest. So when Hershey approached us in October of last year, I was amazed that this iconic company would be interested in Krave. And as the founder, I really wanted the brand to survive and succeed for the rest of my lifetime. And it happened very quickly. They did their research. They knew they wanted it.

Chris Cuvelier: As an entrepreneur, you've got to be out in front. You've got to be innovating. And I think that a lot of the big companies realized they don't innovate well. As Jon mentioned, the food business is extremely capital-intensive. We have raised well north of \$10 million and we have lines of credit in place. We learned early on, if there's capital available, go get it, because what you don't want to be in a situation of needing capital and having to go back and get it.

Helen Russell: You see a lot of money being floated around. Blue Bottle just got \$70 million. A lot of people have approached us to give us money. We all have different synergies, but we all have to innovate. So you have got to have gluten-free; you have to have Fair Trade; you have to have organic; you have to have a story; you have to have a reason to be because we all have a very, very high expectations, especially in the Bay Area. It's a big responsibility to take money unless you really do have an exit plan. Right? But when I think about Starbucks, I think about publicly traded beige scones buying La Boulange, an incredible brand that everybody loved and now dumbing down that brand again and now giving it up. So we've decided not to go that route.

Q: How do you establish yourself in a competitive field? How do you scale your products while still connecting with customers?

Nicolas Bernadi: It starts with the product. Our food has to be amazing and has to be affordable. There are three major cost drivers: ingredients, labor and real estate. In terms of ingredients, we have such a scale now that we have very strong purchasing power. In terms of labor, we are able to use a lot of different technology for cooking, like ovens that are super-small that can measure the cooking of every single piece of salmon and cook pieces one at a time. And we don't have prime real estate — we don't need to be able to be on Pine Street or Polk Street.

Todd Masonis: We haven't spent any money on marketing, but we have spent money on trying to educate people. We offer an introduction to chocolate: we teach people how to make chocolate at home, we take customers to Belize for a week. If we sell wholesale, every case comes with a sample bar that's

unwrapped and the person at the store that is going to sell it eats it.

Matthew Jacobs: There is demand for new tools that can help fix what is in some ways is a broken diet. We create solutions from micro-algae to create healthier and more sustainable products. The irony is not lost on me that we are here talking about food innovation and our ingredient is actually the oldest food ingredient on earth. Micro-algae is the precursor to all plant life.

Q: Your products depend on ingredients under environmental threats. How do you manage supply risks like that?

Helen Russell: It's about relationships for us. We have been traveling to the farmer's gate, whether it be in Guatemala, Kenya, Rwanda or Nicaragua, meeting with our farmers, negotiating with our prices. We do micro-credit loans to some of our farms. And climate change in the coffee lands is very, very real. Because we buy coffee so high up the mountain, we buy the top percent that's available and we are insulated just a little bit.

Todd Masonis: If we don't get good beans, we are not going to have good chocolate. It's very easy to see why the farmer chooses the more-robust, lower-flavor bean. Everyone is optimizing for a yield. No one is optimizing for flavor. So we and others are finding ways to pay farmers for a good price for really good beans and getting them excited.

Chris Cuvelier: Brazil, we went really deep in the supply chain when we first got there. So we've gotten scale in a year where the exchange rate is not in our favor. Our coconut water comes out of Thailand. We are considering setting up a separate company to buy in Thai baht. It will be much more stable than buying by the dollar.

Q: Tell us about some innovations in branding and how you established your brands.

Jon Sebastiani: There were three companies in U.S. meats in our category: Jack Links, Con Ag Foods and their Slim Jim brand, and Oberto. And they were doing the same thing. We didn't even want our brand to be in the same sentence as their brands. We wanted to put our brand with Pop Chips and Chobani and Kind Bar and Cliff Bar. Jillian Michaels signed on with Krave as a partner. We also work with Meb Keflezighi, who most recently won the Boston marathon. So the brand is important to establish health first, product second.

Helen Russell: We chose the Bengal tiger as our icon because of the power and grace and because we were committed to save that tiger. In Mill Valley, we have two stores and we have a huge cycling community. Cyclists love coffee. And we work with team Mikes Bikes. We sponsor the women's team and we take our coffee to all their events.

Matthew Jacobs: We realized with algae being a new ingredient, it's important that our customers and the manufacturers really understand it. Consumers are increasingly savvy. They want to know: How are ingredients are made? Where do they come from? What are the health advantages?

Read the complete transcript at www.ssflp.com

Q: What might we see from your company in the near future?

Matthew Jacobs: Algae is the hero of the story here and we will continue to do new product introductions. Our products will get out into more store shelves and really have the benefit for people to experience, enjoy and actually arrive at that nutrition benefit.

Chris Cuvelier: We are innovating in a few different places right now. We have a couple different coconut water flavors, and we have chocolate-covered fruit coming out right now.

Helen Russell: We are celebrating our 20th anniversary right now, and we are layering our company with the next generation. Being in the retail space has driven our wholesale. Unless you have a retail space and coffee to experience the brand, you can't continue to grow wholesale. If you go into our stores you will see coffee brewing equipment, you will see single serve. We are going to do more with food service because that is how we are going to grow our business. We are in Google. We are in Twitter. We are in LinkedIn.

After seven years we bought a coffee farm in Panama named Sophia. We were one of the first roasters in the US to own our own farm in Panama, and we will have our first harvest this year.

Jon Sebastiani: Krave is going to stretch the brand into the \$10 billion bar space. So we will launch a meat bar in early incorporating fruits and vegetable and grains and basically the proposition is going to be twice the protein with a third of the sugar of a Cliff Bar and half the carbohydrates.

8 Resources for talent

- 1 East Bay Manufacturing Group / SFMade
- 2 Manufacturing Extension Partnerships (MEPs) - Manex
- 3 Design it - Build it - Ship it
- 4 Economic Development Agencies
- 5 Workforce Development Agencies / WIBs
- 6 Employment Training Panel (ETP)
- 7 Community Colleges
- 8 National Labs