

KRISPY KREME: A STRATEGIC ANALYSIS

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I. ABSTRACT:

Krispy Kreme has fallen on hard times as result of poor leadership throughout its infrastructure. After the company first went public in 2000, Wall Street was amazed with the impressive performance and consistent profits the company produced quarter after quarter. The desire to be the best and not let the investors down resulted in numerous ethical oversights and judgment shortfalls. By the end of 2004, many of Krispy Kreme's accounting scandals began to proliferate. The severe nature of many of these scandals made it nearly impossible to keep them out of the public eye and it became clear that Krispy Kreme was in a great deal of trouble, both legally and financially. In 2008 when this once great company was at its lowest point, it became clear that change was necessary if the company was going to survive. This paper analyzes the shortcomings of Krispy Kreme Doughnuts and proposes a strategic plan for turning things around and establishing a viable long-term plan.

II. Introduction

Krispy Kreme opened its doors in 1937 when Vernon Rudolph purchased the secret recipe for yeast-raised doughnuts. By the 1960's, Krispy Kreme had become very well known throughout much of the southeastern United States. Revival and upward expansion were paramount in the 80's and 90's. This resurgence that Krispy Kreme experienced was due to a renewed focus on a hot doughnut along with rapid growth outside of the southeastern United States. Since its quaint beginnings, Krispy Kreme has grown to be a multi-national and multi million-dollar corporation with quite a history along the way [3].

The purpose of Krispy Kreme, just like any other for-profit corporation, is to increase assets and instill loyalty in its consumer base. Krispy Kreme strives to be the leading choice of consumers for specialty baked goods and beverages. Krispy Kreme seeks to maintain its loyal customer base and attract new customers in both current and developing markets with its commitment to quality and consistency in its doughnuts, other baked goods, and beverages. Krispy Kreme's life cycle has followed that of many great corporations in the past. It began with a long period of steady growth followed by a period of rapid expansion until reaching its maturity and beginning to decline [4].

Krispy Kreme has three primary revenue generating segments, which are company stores, franchises, and the Krispy Kreme Supply Chain. Company Stores have been the basis of their operations; they include on-premises sales and off-premises sales, which are usually the factory stores. The on-premises sales are where you can find the "HOT" doughnut signs, all kinds of drinks, memorabilia, a seating area if you have time to sit down and enjoy your break, and the drive thru window when you just want a doughnut to go [4]. The on-premises sales are also, where community organizations can go to get the "fundraiser" doughnuts to raise money for their cause. The off-premise sales are mostly done in the large Company factory stores which have the capacity to make up 10,000 dozen doughnuts a day and supply the

convenience stores, grocery stores and other institutional accounts. The Company Stores represent \$326,199,000 that accounts for 70.7% of their total revenues in 2007, which is down 18% from 2006 [4]. It is important to note that direct operating expenses associated with generating this revenue account for 88.9% of the total revenues generated by company stores. In the end, company stores brought in 50.27% of net operating income in 2007.

Krispy Kreme Franchises are formatted in the same manner company stores are in respect to their on and off premises sales but of course the owners of these Franchises pay fees and royalties [4]. Under the franchises, Krispy Kreme does not generate a significant amount of total revenues, only bringing in 4.6% of total revenues at \$21,075,000 in 2007, which is up 14.6% from 2006 [4]. For Franchises; however, direct operating expenses only account for 21.8% of revenues. As a result, franchises are still able to bring in 22.94% of Krispy Kreme's total net operating income.

The Krispy Kreme Supply Chain is the main distribution channel for all the things needed for any store to operate. It provides the ingredients for the doughnuts, all the equipment needed, all beverages served, and all other store needs such as signs, display cases, and even the uniforms all employees wear. Krispy Kreme has pride in their distribution processes and strives to make it better by adding key suppliers to reduce their cost and making it more convenient for stores worldwide. The Supply Chain revenues went down from \$126,517,000 in 2006 to \$113,921,000 in 2007, thereby accounting for 24.7% of total revenues [4]. The direct operating expenses associated with generating this revenue account for 83.1% of it, which means that the Supply Chain was responsible for 26.79% of net operating income.

III. SWOT Analysis

Krispy Kreme has the potential to become a powerhouse in the United States again. Through the use of a S.W.O.T. analysis, Krispy Kreme can identify its internal strengths, internal weaknesses, external opportunities, and external threats [6]. One of Krispy Kreme's most powerful internal strengths has been their logistics program since having placed a renewed focus on it in recent years. Their program, MyKrispyKreme, has allowed the company to lower their transit and turnover times [3]. This has helped the company lower its waste levels caused by overproduction. Brand recognition is another strength that Krispy Kreme possesses. Their logo and doughnuts can be spotted by both sight and smell from far away. When consumers are able to witness the doughnuts being made fresh and are able to sample them, it allows for a hands-on grass-root campaign style. The smell and taste of this product has helped to make their doughnuts iconic. This recognition helps Krispy Kreme remain visible and therefore it is a productive strength for the company.

Although Krispy Kreme has many internal strengths that have gotten it to where it is today, they have many weaknesses within the company that are hurting its overall profitability. Since the consumer health craze began in the 90's and hit its peak in recent years, consumer perception of Krispy Kreme has become somewhat of a joke about obese children and a diabetic nation. Further, the lack of variety has increased exposure to changes in demand, thereby exposing the company too much greater risk. Krispy Kreme has made steps to cater to the more health conscious public in the United States; however, their national ad campaign does not adequately penetrate the market resulting in low consumer awareness. Between 2006 and 2007, Krispy Kreme closed 48 franchises and 9 company stores [4]. This can be attributed to the weaknesses and shortfalls of the screening and selection process when granting franchises and opening stores.

Even with so many weaknesses impacting the profitability and longevity of Krispy Kreme, the company still has many opportunities now as well as in the future that could potentially turn things around for the company. The global economy of today provides many avenues for expansion and diversification. The

primary reason for this is that demand trends differ greatly across different demographic regions. In many Asian and Eastern European countries, the value of sweet commodities is increasing at a fairly rapid rate while the market in the United States is stagnant. Here in the US, the education sector is another powerful opportunity for growth. They have the potential to further capitalize on brand recognition through affiliation with the local schools and their communities.

The fast food industry is a threat to Krispy Kreme. Krispy Kreme has primarily been perceived as a breakfast store due to the traditionally high demand of doughnuts and more recently, coffee. As a result, Krispy Kreme's sales tend to be the highest during breakfast hours. Other companies like McDonalds and Burger King have started entering the market and developing a similar selection with even more choices available at lower prices causing Krispy Kreme to lose part of its niche market. Krispy Kreme's biggest competitor is Dunkin' Donuts. This company has over 7,000 stores within the US and 30 countries worldwide. They have implemented an execution strategy stressing beverages over the carb-laden doughnut [2]. They still offer 25 varieties of doughnuts compared to Krispy Kreme's 20 [3]. Offering greater variety in the food they sell along with aggressive expansion makes Dunkin' Donuts a formidable competitor.

Other sources of competition are from Starbucks and Tim Hortons. Krispy Kreme has been trying to add more products to go along with its doughnut. Expansion into the coffee and coffee-like beverages has caused Starbucks Corporation to become a primary competitor with over 12,000 stores that offer many drinks and pastries that can be found at Krispy Kreme [7]. Tim Hortons has become a viable threat to Krispy Kreme since merging with Wendy's in 1995, and thereby greatly increasing their opportunities to expand into the United States market [8]. Tim Hortons currently has over 3,000 locations in the Canada and the northern United States with a strong foundation as a coffee and doughnut shop.

IV. Short-term and Long-term Goals

In order for Krispy Kreme to remain competitive and increase profitably in the future, they have established many short and long-term goals. One of their goals is to hold senior officers accountable by conforming to the Sarbanes-Oxley Act [4]. They are interested in increasing inventory turnover and creating a more efficient supply chain. Krispy Kreme is also working on improving the quality of the franchise store operations. They are developing and implementing a more beneficial international growth strategy through their use of political risk assessments. Finally, Krispy Kreme would like to alter their customer's preferences and perception from a negative connotation to one that is more amicable [4].

The most important aspect of goal setting for a corporation in Krispy Kreme's position is the way in which they approach it. The best approach would be to set S.M.A.R.T. goals—goals that are specific, measurable, attainable, realistic, and timely [1]. It is clear that the company already has a laundry list of goals that sound promising; however, simply listing the goals without a SMART approach often ends with poor or inefficient results. By quickly conforming to the Sarbanes-Oxley Act, Krispy Kreme can more efficiently reach many of its goals while positioning it to attack others [4]. Had Krispy Kreme implemented SMART goals and similar protocol of that put forth in the Sarbanes-Oxley Act as early as 2000, the company could have avoided the substantial loss of market share and could still be experiencing strong growth today [1].

V. Assessment

By combining the SWOT analysis with SMART goals we get the USED analysis. Under a USED analysis, management would be able to implement a four step strategic plan by using each strength, stopping each weakness, exploiting each opportunity, and defending against each threat [6]. This would allow them to reach their short-term and long-term goals in a timely and efficient manner. While their logistics programs have improved substantially in recent years, becoming lackadaisical is not an option. The first step in the strategic plan will be to hone in and focus on improving the supply chain and making it more efficient. A key component to this step is improving the relationship with the wholesalers and the communication between the strategic business units throughout the company's infrastructure [5].

The next step in this plan is to focus in on brand recognition. The Krispy Kreme trademark is arguably the most valuable asset the company has and therefore should be protected and improved upon. In order to do this the company needs to focus on improving consumer perception of their products via a more penetrating national ad campaign. It is clear that the vast majority of health conscious consumers in the United States have a negative perception associated with Krispy Kreme. To combat this negative stigma surround the company name, increasing research and development towards meeting the needs of the consumers is paramount. Another way to further capitalize off of the brand recognition would be to more aggressively reach out to the local schools and communities. This grass-root approach is one of the most cost effective and profitable advertising approaches available for enhancing market penetration.

The third step is aimed at expansion into foreign markets and providing a safer and more diverse investment opportunity to the shareholders. This can be accomplished by first developing a better screening process for company stores and franchises thereby decreasing the high turnover rate that is currently hindering the company. Next, the focus would be on international expansion. To ensure a smooth entrance into these developing markets, it is of utmost importance to have an effective political risk assessment plan in place. This means that Krispy Kreme would have to invest in gathering research aimed at identifying weaknesses as well as opportunities that will play a major role in the success of this endeavor.

The fourth and final step is aimed at effectively recognizing and handling competition. It is clear that Krispy Kreme has a great deal of competition in its market. The best approach to handling this competition is to understand the nature of its competition. Since many of the fast food restaurants will focus on offering better prices and have the resources to do so competitively, Krispy Kreme would have to focus on offering value to the consumers in another way. This can be accomplished by specializing in quality and customer service over lower prices. Their other major competitors are those that have major market share in the same avenues of service such as Starbucks and Duncan' Donuts. To remain competitive with these companies, Krispy Kreme would have to focus on establishing their niche market and meeting the needs of their specific customer base. Increasing research and development in areas such as new product development would be necessary to get the competitive edge in the health foods market over their primary competitors.

VI. Conclusion

Funding these additional expenses is necessary and feasible in order to regain profitability and to continue to expand globally. The company can generate the funds by starting a new aggressive marketing approach to investors emphasizing a total restructuring of the company that will turn things around in regards to profitability, consumer awareness, and the management within the company's infrastructure. If Krispy

Kreme effectively manages its resources and implements this four-step approach to transforming the company into a profitable entity, it will be able to not only increase market share but also resume a long period of steady upward expansion within the next three years. At that point, the company can begin to repurchases shares of stock and increase the earnings per share. It is, however, of utmost importance that the company continues to fund research and development and update their strategic business plan regularly to ensure that they remain ahead of the competition in order to prevent another substantial loss in consumer wealth and market share.

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