

Magic Muffin Company

Less than six months had passed since Meg Carter had opened the tiny shop fronting the Newport harbor. The small store, which Meg had named the Magic Muffin Company, sold a variety of freshly-baked muffins, soups, and natural beverages.

Meg was ecstatic that sales for the initial five months had been about \$145,000, considerably above Meg's initial expectations. As she thought about the company's tremendous progress to date, she had one primary concern: was it now to think about expanding to additional locations?

Background

Meg Carter, chef extraordinaire, had a prolific background in the food service industry. While in school, Meg had worked as a waitress, chef, hostess, and assistant manager of a local restaurant.

After graduation, she had accepted a position as an administrative assistant to a man who was expanding a chain of retail bakeries. Her duties included store layout, staffing, equipment planning, and supervision of new stores as they were being opened. This experience led her to think about opening a retail store of her own someday.

Meg worked for the bakery chain for several years. Although she was well paid, she began to feel that her job was losing some of its original challenge. Then, one day, while snacking on a stale muffin bought from a convenience store, she had an idea. Why not open a store to sell freshly baked muffins?

Meg thought about whether demand would exist for such a store. She noted the success of similar stores which sold freshly baked cookies, Mrs. Field's and David's Cookies in particular. If those stores could be successful, why not a muffin shop? Besides, muffins were much healthier items and the nation was becoming increasingly obsessed with diet and nutrition. Meg became convinced that a store where customers could get warm, fresh muffins would really flourish.

Over the next several weeks, she thought about what it would take to open such a store and where it should be located.

Early Decisions

A number of factors crossed Meg's mind as she thought about how and where to open her new muffin store. First, she thought it would be important to open the store in a location which drew a large amount of foot traffic. Muffins, she felt, were somewhat of an impulse purchase so it might be necessary to grab the consumer off the street and into the store.

Second, Meg was concerned about the amount of money that it would take to get the store off the ground. Her salary of \$60,000 annually had enabled her to save a fair amount of money over the past few years. However, she didn't want to risk it all in one investment. She believed that it would be wise to limit the amount of store space that she rented and keep the interior furnishings simple. Once the concept was proven to be successful, she could always upgrade the store's atmosphere and image.

Third, Meg believed that a limited menu was all that was needed. Mrs. Fields and David's Cookies had apparently proven that a retail baked goods store didn't need a large and varied menu and Meg thought that operations would be much simpler if her new store kept menu choices to a minimum. Meg decided that she would sell only muffins, soups, and beverages in her new store. About six varieties of muffins would be available on any given day along with two soups, coffee, tea, and a line of naturally-flavored soft drinks. Meg felt that the soups were needed to offer lunch customers a more balanced meal although she didn't expect that soup and beverage sales combined would amount to more than 30% of the store's total revenues.

Finally, Meg thought about her managerial skills and the amount of time she was prepared to devote to a new business. She was convinced that she had the expertise needed to start and run the business but was more concerned about the time issue. Meg decided that she wasn't ready to spend 100 hour weeks, 52 weeks a year starting a new business but she did not mind a concentrated effort getting the store off the ground.

Balancing all these factors, Meg had an idea. Why not open the store in a resort area where there would be lots of traffic over a limited season? The more she thought about this approach, the more sense it made.

Newport, Rhode Island

A Rhode Island native, Meg was convinced that Newport would be an ideal location for her new business. Long a playground for the wealthy, Newport attracted a great number of affluent individuals during the summer months. In fact, the population nearly quadrupled from 29,560 year-round residents to about 112,000 each summer.

The shopping district of Newport was somewhat spread out but, for the most part, was located at the base of Newport harbor. There, a number of trendy restaurants and boutiques catered to the many tourists and yachtsmen who visited the town. Visitors went to Newport for its unique charm and to see the grandeur of the numerous mansions built by wealthy 19th century industrialists.

An additional attraction Newport had once offered was the America's Cup sail boat race. This event, which took place every three years, had drawn over a quarter of a million visitors to Newport during May and June for more than 40 years. But, with San Diego Yacht Club skipper

Dennis Connor's victory over a strong New Zealand crew in 1986, the America's Cup races were moved to California. This move had a severe effect on property values in the area and had a temporary effect on business but, overall, most of the area businesses had recovered and adjusted reasonably well.

Meg drove to Newport one day to review the competitive situation her new company would face. While there were over 30 restaurants along the Newport harbor, there were only two small stores which sold muffins. One of those stores was a convenience store which charged 79 cents for a muffin and the other was a local bakery which charged 59 cents. Neither of them positioned muffins as a primary product of the business. Meg estimated that combined these two stores probably sold only \$ 20,000 worth of muffins a year.

During her visit, Meg also looked for a suitable store front from which to operate her business. There were a number of sites available in the town but Meg found one small space which looked particularly attractive. She took down the number of the landlord posted on the window and decided to call when she returned home.

A Store is Born

Meg called the landlord about the store. He informed her that the store comprised about 450 square feet of space and was commercially zoned. He couldn't see any reason why the town would not allow a bakery or restaurant on the premises. He informed Meg that he wanted \$1,000 per month for rent along with an override of 3% of sales above \$250,000 per year. He indicated that he would be flexible about the term of the lease. Meg asked him if he would consider a one year lease with two three-year renewal options. While the landlord at first balked at this proposal, he quickly changed his mind when Meg conveyed her enthusiasm in the concept. Without further thought, Meg told the landlord that she would rent the store.

Meg then contacted suppliers of equipment and raw materials. She also spoke to town officials about the permits she would need. Since the store she had rented was very small, Meg wanted permission to put some tables and chairs out on the sidewalk for her customers. Working at a breakneck pace, she was ready to open the store after only two and a half months. The town gave her the permits she needed and allowed her to put tables on the street on a trial basis. Total start-up costs to this point had come to about \$ 135,000.

Nearly from the start, the store was successful. Town residents and visitors were drawn to the store by its location and out of curiosity. What they found was a long counter in a small, cramped, and relatively simple space. But what they also found were delicious, warm muffins.

The Magic Muffin Company quickly became a trendy place to go for freshly baked muffins and hearty soups. Customers frequently had to wait 10 minutes or more to be served. Nevertheless, many of the town's residents and visitors became regulars who befriended Meg and encouraged her to share her concept (and muffins!) with the world. Many offered to help her finance additional locations if she would consider expanding.

Meg concentrated on running the store during the summer but when October came, she closed the store until the following May. During the fall, she reflected on her recent experiences. The store had been quite successful (see Exhibit I.) Why not expand to additional locations within her state? Developing another store might be just what she needed to keep herself busy during the winter months ahead.

Expansion Ahead

Meg was encouraged by her many customers who urged her to expand. Since the business was obviously a success, why shouldn't she consider branching out to other locations? If one or two additional stores were also successful, Meg figured that she could franchise Magic Muffins and go nationwide. Within several years, she might even be able to go public or sell out to a big food conglomerate.

Meg's obvious choice for the first additional location was Providence, the capitol of the state. It didn't take much for Meg to research the area: she had lived there most of her life.

Providence was a small city of approximately 156,000 people. There were several prime retail locations including a major shopping mall called 'The Arcade' and East Providence, a small, cozy, charming collection of shops at the foot of Brown University.

Meg thought about the city and decided to open her next store in East Providence. Rent in that area was steep, about \$ 50 per square foot annually, and she would need to rent more space than she had in Newport, but a store near Brown would be an excellent showplace for the company. Investors could visit it, feel the unique charm of the area, and would probably want to participate in the company's future growth.

Meg also thought about the new store's image. A simple, basic decor might work for the Newport area but it definitely would not do for East Providence. Besides, if the company planned on expanding nationally, it would need a very polished and attractive interior design.

Meg contacted a design firm which proposed several interior designs ranging in cost from \$150,000 to \$650,000 per store in finish work. The company provided Meg with sketches showing each option and Meg felt that the more expensive option provided an extremely attractive look.

Finally, Meg reviewed the proposed start-up costs (\$675,000) and expenses (Exhibit II) for the new store. She was prepared to invest every penny she had in the new store (nearly \$700,000). After that, she would permit her customers to invest in the company to fund the expansion or franchising of future locations.

While Meg was able to estimate start-up costs and operating expenses fairly well, there were several areas Meg was uncertain how to handle. She wasn't sure if the prices she had

charged in the Newport area (sixty-five cents per muffin) were appropriate in East Providence. She was also uncertain how to project revenues for the new store. Finally, she sensed that some advertising might be necessary to introduce the store and to continue to draw customers over the full year.

Meg had collected some information about the food industry and the Providence area (Exhibit III) but she wasn't sure what to do with it. She sat down to review the data she had collected and to think about the various decisions she had to make.

"I know I'm on to something big here," Meg would say to her friends. "All trends point to muffins becoming the next healthy snack. If I can only establish the company early, I can play a major role in what could be the next major food industry success."

Exhibit I
Magic Muffin Company

Newport Store
Income Statement
May – Sept

Revenues	
- muffins	\$ 101,150
- soups	8,500
- beverages	<u>34,850</u>
sub-total	\$ 144,500
Cost of Goods Sold	
- muffins	25,300
- soups	5,525
- beverages	<u>12,200</u>
sub-total	\$ 43,025
Gross Profit	\$ 101,475
Expenses	
Rent	5,900
Utilities	3,200
Salaries	9,600
Payroll Taxes	1,200
Paper Supplies	6,800
Cleaning Supplies	1,500
Permits	1,375
Insurance	6,000
Depreciation	<u>3,100</u>
sub-total	\$ 38,675
Net Profit Before Tax	\$ 62,800
Taxes on Income	<u>18,800</u>
Net Profit After Tax	\$ 44,000

(Note: Net profit figure is before owner's draw.)

**Exhibit II
Magic Muffin Company**

Estimated New Store Expenses

Rent	\$ 60,000
Utilities	9,000
Salaries	70,000
Payroll Taxes	8,400
Permits	1,375
Insurance	12,000

(Note: All other expenses are variable.)

**Exhibit III
Magic Muffin Company**

Industry Observations

U.S. Retail Sales (in millions)	2000	1990
- Donuts	\$ 2,500	\$ 2,620
- Muffins	720	418
- Other baked goods	6,920	6,720
U.S. Population (in millions)	240	236

East Providence Area

- Approximately 43,000 live within a 5-mile radius of the major shopping area. Of that amount, 6,500 are students at Brown University.
- In addition to the above, some 50,000 workers travel to the area each business day. On the weekends, it is estimated that about 30,000 people who live outside a 5-mile radius shop in the area.
- There is one restaurant and two bakeries already in the area which sell muffins. The restaurant is a 24 hr. pancake house. Muffin prices range from fifty to seventy-five cents.
- Meg estimates that about \$ 40,000 worth of muffins are sold in the area each year.