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Corporate Forces Endangered the Twinkie, but May Save It

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Snack cake aficionados rejoice, the Twinkie will live.

Its demise nearly came at the hands of corporate America's machinations. Its survival, however, depends on some of those same machinations. In the end, it was the extreme outcome of a liquidation in bankruptcy that made the 83-year-old brand salvageable.

The history of the cream-filled snack illustrates a number of the forces that have driven American capitalism over the last hundred years. Its first owner, Continental Baking Company, bought companies left and right in the 1920s, including the Taggart Baking Company, maker of Wonder bread, in 1925.

But the Twinkie was an in-house invention. It was created in 1930 by an executive working at Continental Baking who was looking for a product to sell after strawberry season ended, when the factory line for cream-filled strawberry shortcake sat empty. The yellowish, cream-filled Twinkie was a hit and the company quickly expanded.

Continental Baking continued its acquisition spree and by 1968 it was a motley assortment of baking brands that fed on America's tastes for sweet and easy food. It was then acquired by Harold Geneen's ITT, a conglomerate that sold not only Twinkies but also munitions. There, the brand sat for 16 years until Continental Baking was sold in 1984 for $475 million to Ralston Purina.

By then the baking business had entered a slow growth phase as inflation in baked goods, which had allowed the company continually to raise prices, subsided. Ralston Purina was unable to produce growth in the brands and ended up selling the bakery for about $400 million in 1995 to Interstate Bakeries.

Interstate Bakeries became the largest bakery in the country, but the sentiment around the deal was aptly expressed by a food industry analyst, who said at the time that Ralston Purina's sale "basically allows them to get rid of a dog."

Interstate Bakeries was itself a mongrel of many brands put together by serial acquisitions. Unfortunately, Interstate turned out to be better at acquiring companies than managing them. The brands had been passed around often and in the traveling it appears management never could get a more coherent vision for the company other than acquiring yet more unhealthy brands and leaving them to languish.

Then, at the turn of the millennium, the company was hit by a double blow: a taste for health and less carbohydrates among consumers and a botched attempt to put an additive in its breads to give them longer shelf life. You can tell that something is wrong with a food company when its strategy to save itself is to make its food last weeks longer.

It was also not the time to lack vision. The company's historically high labor and food costs could no longer be covered up by rising prices. Consumers demanded ever cheaper snack food prices.

The company entered bankruptcy in 2004. More than four years later, it emerged, now owned by Ripplewood, which put up $130 million to acquire it. It was then that the company rebranded itself as Hostess Brands.

Despite the company's cost reductions, and its lowering the employee head count by about 10,000, that was still not enough. The company had more than $800 million in debt coming out of bankruptcy, which was actually over $150 million more than it started with. Not to mention that it had spent $170 million on advisers during bankruptcy.

Indeed, people close to Hostess also say that Ripplewood's plan was yet another merger: to sell the company to the Sara Lee Corporation. But when Sara Lee sold its bakery operations to Grupo Bimbo, there was no Plan B.

The company filed for bankruptcy again in 2012. It lost $341 million in the previous fiscal year, according to Standard & Poor's Capital IQ. And management, which had gone through six chief executives in a decade, had been unable to execute a turnaround plan.

When the Bakery, Confectionery, Tobacco Workers and Grain Millers International Union drew a line in the sand in November and said it would rather risk liquidation, it was over.

It was a principled position that the brands would do better with a fresh start and new management. Hostess filed a plan to liquidate the company and fire almost all its 18,000 employees.

The news spread that the Twinkie had finally met its match, along with Wonder bread, the Devil Dog and all the other products. It was then that the mechanisms of corporate America were put in motion to revive Hostess.

Hostess's investment banks went to work and lined up potential bidders. In fact, they didn't have to do much, as the announcement of the company's liquidation and the publicity that followed brought in more than 80 bidders in a few days. It also led to a quick run on Twinkies and other Hostess brands.

The interest came as a surprise to Hostess. Its executives - fearing that liquidation would destroy everything - had worked hard with the Teamsters union for a plan to save the company, only to be frustrated by the bakers union at the last minute. But liquidation has proved to be the Twinkie's savior.

Instead of trying to work out a compromise by reorganizing in bankruptcy, the company used the bankruptcy process to escape all its past burdensome debts. Freed of 394 union contracts, more than $2 billion in pension liabilities and any need to retain factories, the value of the Twinkie was reduced solely to what people were willing to pay for the brand. News of the Twinkies demise was the best thing that ever could have happened to the company.

Two private equity firms, C. Dean Metropoulos & Company and Apollo Global Management, have agreed to pay $410 million to buy the Hostess business, including Twinkies. And Flowers Foods has agreed to buy Wonder and Hostess's other bread businesses for $360 million. Even Drake's will survive; McKee Foods has agreed to pay $27.5 million for the business.

These are so-called stalking horse bids. In bankruptcy there is an open auction of the liquidated business, which in this case is expected to occur in bankruptcy court in February and March, when others will bid.

All told, it appears that the sale of Hostess may reap over a billion dollars, almost twice what the creditors initially expected if it had not been liquidated. In other words, the liquidation of Hostess has made the company worth more.

There's a lesson here. While corporate machinations and passing along brands can damage them, the clean bill of liquidation allowed corporate America to re-evaluate the Twinkie.

Sure, there will be future battles as Hostess's old unions struggle to have their employees rehired and new management tries to restart the company. And nothing can heal the wounds of the employees who have lost savings and pensions as well as jobs.

But the brands will now come under better management and, we can hope, more capable owners who can turn to reviving these businesses. In other words, while extreme finance was the cause of Hostess's demise, it may very well now be the Twinkie's savior.