Fort Wayne, Indiana Barbara Baekgaard and Pat Miller sat at a small table covered with many swatches of brightly colored fabrics being considered for the next product launch. The cottage industry business they had founded several years earlier had taken on a life of its own. From humble beginnings in the basement of Barb's home, they had proven both the feasibility and value of the market for attractive ladies' handbags and luggage. But as sales grew, so did issues with production capacity and quality to name a few. The two pondered the future. What financial resources and human resources would they need to scale up to the next level? How would growth affect the friendly, fun culture they had worked so hard to create?

Origins

Barbara Baekgaard was wrist deep in wallpaper glue one day in 1981 when the doorbell rang. Who could it be? She had only recently moved into her new home in the Wildwood Park neighborhood of Fort Wayne, Indiana. At the door were Patricia (Pat) Miller and her 5-year-old son, Jay. Pat had stopped in to welcome Barb and her family to the neighborhood. As Pat recalls:

I was the welcoming committee of one, and Barb answered the door. If you know anything about Barb, you'll know that she was redecorating—taking wall paper down and putting her own stamp on the house. She asked me if I knew how to hang wallpaper, and I said, no, and she asked, ‘How would you like to learn?’ That was the beginning of our first business, Up Your Wall, a wallpaper-hanging business.

We were good partners because she remembered every joke she's ever heard, and I was a good audience. She also liked to hang wallpaper around windows and doors, the more complicated stuff, while I enjoyed doing the straight walls.

The two women became fast friends and business partners, hanging wallpaper by day and raising their families by night. Up Your Wall, however, would be superseded within a year by another, more promising venture.

In March of 1982, the partners made a trip to Florida to celebrate the birthday of Barb's father. While waiting for a connecting flight in Atlanta's Hartsfield-Jackson Airport, they noticed that many passengers were carrying Land's End duffle bags and other utilitarian garment bags and luggage. Barb describes their observation:

While we were waiting for our plane, I looked around and realized that we weren't the only women with unattractive luggage. In fact, I didn't see one woman in the entire airport carrying anything that would be considered attractive. I knew that there was a look out there that was cute and trendy, but I didn't own any of it, probably because it was too expensive and not functional.

In fact, both Laura Ashley, known for its floral printed fabrics, and Pierre Deux, maker of French country-style handbags and accessories, targeted the high-end of the market with attractive products. Pat recalls that their Florida trip included a visit to a Pierre Deux retail store: “We loved that … it was part of our inspiration. There was nothing like that in this country.” However, neither of these potential competitors produced a duffle bag suitable for weekend or air travel. Barb and Pat discussed their luggage dilemma on the trip back to Fort Wayne. “We liked the shapes of the bags we saw,” recalls Barb, “but not their appearance.” The women wondered if they could make attractive but functional bags for everyday use and travel at a price that would appeal to a broader audience.

This case was prepared by Professor Angelo Santinelli and case writer Richard Luecke as a basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation. © Babson College 2010. All rights reserved.

The day after returning to Fort Wayne, Barb and Pat visited Joann Fabrics, a retail chain of fabric stores, where they purchased material with various patterns, stripes, and colors. They mixed and matched these in an effort to create a distinctive quilted cotton look of their own.

Once they had the designs they liked and cut out patterns, the team hired a woman who had done clothing alteration for their other home-based venture, running clothing trunk shows.1 She was paid for sewing the prototype bags Barb and Pat had designed. These initial prototypes included a duffle bag suitable for weekend travel, a smaller bag they called the “sport,” and a purse. There was enough fabric to make a dozen, which they hoped to sell at an upcoming trunk show. Says Pat:

We needed to do some market research and wanted to be certain that it was unbiased. We couldn't let friends who came to the trunk show know that we had developed these products—they might buy them simply because they were our friends. So, we had to come up with a brand name that didn't have either my name or Barb's name in it. We decided to use Barb's mother's name, Vera Bradley. My mother's name was Wilma Polito. That name didn't have a prayer of sticking as a brand, so we settled on Vera Bradley Designs.

The day of the trunk show was plagued by inclement weather, but attendance was high and the show was a success. All twelve of the prototype bags sold, and customers were asking for more.

Because the trunk sale attendees were generally middle-aged and older women, the two entrepreneurs looked for another segment in which to test the appeal of their products. Barbara had two daughters in college at the time, one at Michigan State and the other at Marymount College in New York, so they decided to extend their informal market research to college campuses. Barbara sent several bags to each daughter and asked them to find out what their friends thought of them. The response from both campuses was extremely enthusiastic.

With affirmation that their bags were potential winners, the ladies set out to purchase more material and commission the sewing of more bags. Each borrowed $250 from her husband, and with cash in hand they set off once again to Joann Fabrics.

The Founders

Barbara Baekgaard had attended Marymount College in New York and Barat College in Lake Forest, Illinois, where she studied sociology. Her father was in the gift candle business and he often took Barb to gift shows and other industry events. Her mother, after whom the company is named, had several small cottage businesses of her own. Barbara credits her mother for her work ethic, as well as her eye for design. “What I knew about business at that time I learned from them,” she says. “Things like finance were not even in the realm of my knowledge, but I was doing what I knew best—design.”

Barb's parents had bequeathed her other important traits: energy and unflappable optimism. “There are people who think they can, and people who think they can't. I'm the think you can type,” she says. “I am shocked when things don't go right for me. Just shocked.” Her fondest aphorisms reflect a deeply ingrained optimism: “Often wrong, but never in doubt.” “Good is the enemy of great—never settle for good.”

Like Barbara, Pat Miller had family members who influenced and shaped her attitudes toward business and customers. As a young girl she often worked in her grandfather's grocery store. “I learned a lot about business from working in that store—inventory control, bookkeeping, marketing, running the cash register, and dealing with customers,” she says. “I was always in the store and did a little of everything. And I knew that [in the future] I wanted to be connected with business.” She followed through on her intentions, earning a BS in business education from Indiana University, and then teaching business to high school students for six years.

The Early Years

With the success of their prototypes among trunk show attendees and college students, the founders knew that they were onto something of value. But would their bags appeal to a broader audience in a retail setting? The annual Chicago Gift Show, a major buyers-meet-sellers event, was coming up on the calendar in September 1982. It seemed a good place to test their products.

Barbara had attended various gift shows with her father, on behalf of his candle business. The Chicago Gift Show highlighted gift wares and home furnishings and was primarily attended by individuals who either owned or sold to gift shops and notions stores. Because handbags and luggage were not generally thought of as gifts, companies in that industry did not exhibit at the Chicago event, but favored other venues and trade shows where women's apparel accessories were typically featured. The founders, however, decided to try their luck in Chicago, thereby avoiding more competitive venues where standing out from the crowd would be a struggle. Says Barb:

I remember calling to rent booth space. They told me that they didn't have our category of product at the show and didn't know where to put us. When we showed up we found our space in the bowels of McCormick Place, where the show is held. But we took it in stride and set up a wonderful display of our products, with flowers and pretty fabrics.

During an evening reception for the event's hundreds of vendors, Barb chanced to meet Will Little, who ran the show. The two got along very well, and Little asked to see her booth. After getting a look at how nicely the two newcomers had decorated their exhibit, and its unfavorable location, Little took it upon himself to have their booth moved to a more strategically placed space.

The show was a success for the two women, who sold over $10,000 in product. It was then that they realized two things: They had something potentially big on their hands, and they needed to purchase much more fabric and outsource the sewing in order to tap that potential. But where would they get the cash?

Initial Financing

Their question was soon answered—and from an unanticipated source. Shortly after the Chicago Gift Show, Barb and her husband made a trip to nearby Michigan to visit one of his former work colleagues. Still bubbling over from her Gift Show success, Barb explained her new business venture to their host, who listened with interest. Later in the evening, the gentleman asked her to step into his home office, where he presented her with a check for $2,500 dollars. “I almost fell over,” Barbara recalls. “He said, ‘I love your enthusiasm. If you are successful, consider this a loan; if not, it's a gift.’”

A bank relationship soon followed. Back in Fort Wayne the two founders paid a visit to Franklin Bank, where they hoped to obtain a $2,000, 90-day loan for fabric purchasing. They walked in with sample products in hand and asked to see someone about a loan. The receptionist introduced them to a loan officer who listened with their plans with what both later described as undisguised condescension. “And where are you going to sell those bags?” he asked with a bemused chuckle. After a few more questions about the business, the loan officer unenthusiastically described the bank's terms and produced the proper documents, which Barb and Pat signed.

As they left the bank, Barb turned to Pat and asked what she thought about their experience with the loan officer. Pat was blunt and brief: “He didn't get it at all.” With that, the two made an about face, marched back into the bank, and demanded that they be assigned to another banker—someone who understood and believed in their business. The bank introduced them to Robert Marshall, who would be their banker and friend for many years to come. Marshall took a strong interest in the venture and would often drop in on their workplace to see how things were progressing and to offer business advice. When Marshall went to work for another bank, the Vera Bradley account followed him.

Neither partner had knowledge or experience in financing. Recognizing this weakness, they turned for help to the local office of SCORE (Service Corps of Retired Executives)2 and requested someone with financial expertise. SCORE introduced them to volunteer George Cook, a retired financial executive. His skills nicely complement those of the two entrepreneurs.

One of Cook's first initiatives was to show Barb and Pat how to analyze their cost of goods to ensure that they priced items in a way that would produce a healthy gross margin. He went on to study their production, distribution, and associated sales and marketing costs to understand what it would take to make a profit. Cook emphasized the importance of understanding costs and minimizing expenses in order to make the most of the venture's limited capital. Under his guidance, the company established sound bookkeeping and inventory procedures and produced monthly financial statements and inventory reports in order to control the business.

In the years that followed, the business would need more capital in order to finance its growing sales. That need would be met first by a cash infusion from the founders who mortgaged their homes to raise capital, and by a bank line of credit.

Production

Production at the company's “cottage industry” level involved cutting fabric into patterns, followed by sewing the cut pieces into finished products—both labor-intensive activities. Recognizing that their core skills were in design and sales, the partners decided to outsource sewing to people in the community who did it well. Barb was a good sewer but, as she said, “I shouldn't be in the basement sewing. I should be out selling.”

Working out of Barb's basement, the founders cut fabric, sometimes with the help of their children. All the materials needed to produce a bag—including zippers, thread, labels, and instructions—were then packaged into individual kits that freelance sewers would pick up and later return as finished goods for inspection. Outsourcing of manufacturing continued as revenues grew. “Our future was sales and design,” Barb asserted many years latter. “We wouldn't have been good at manufacturing.”

By 1986 the business had grown to the point that Vera Bradley needed more space. The next year it constructed a building with more than enough space for its current requirements, leasing out what it didn't need.

Brand Image

From the beginning, Vera Bradley bags had a distinctive look: vibrant colors, unusual patterns, and clever designs. “I've always thought that design was the engine that pulled our train,” Pat likes to say. She and Barb wanted their products to stand out and be identifiable as Vera Bradley, even when their labels were not visible. With that in mind, every newly introduced product had a unique design or pattern feature, yet maintained the Vera Bradley “look.” This distinctiveness reinforced the brand image and kept current customers coming back for more. However, every change represented a risk of being stuck with unsalable merchandise.

The founders' concern with the “look” of their products extended to the public's perceptions of Vera Bradley, the company. In their view, it was important for the business to look professional and larger than it actually was in those early days. They did not want customers or suppliers to think of Vera Bradley as a basement operation. With that in mind, Barbara instructed her children not to answer the phone during business hours. Meanwhile, Pat, with help from Barbara's daughter, Joanie, designed a striking and professional-looking letterhead and business cards. Joanie also lent her artistic skills the first company catalog (Exhibit 2.1). Product shipments used new boxes rather than reused boxes and packing material. According to Barb:

We didn't want people to know that we were working out of the basement. You have to look as though you are a strong, successful business. So everything sent out had to look as though we were in the most beautiful corporate setting around, and doing well.

Sales

The 1982 Chicago Gift Show gave the company some exposure to the distribution channel. Developing relationships and creating a network of repeat customers within that channel would require much more work. As with other functions of the nascent enterprise, the two founders began with a do-it-yourself approach. Whenever either of them was out and about they would look for local gift shops, walk in, introduce themselves and the company, show samples, and ask for an order. They also recruited friends and family as independent sales representatives: Barb's mother, sisters, college friends, friends of friends—they turned to people whom they knew and liked and asked if they would represent the company's products in their geographic areas. The first of these reps was Barb's college roommate, a resident of upscale Arlington, Virginia. She enlisted in 1983.

Sales representatives were responsible for developing a customer base of primarily gift stores in their geographic areas. Reps would take orders, but would not be paid commissions until sold items were paid for. The reasoning behind this compensation strategy originated in Barb's earlier gift trade experience. Many shop owners, she knew, were slow to pay. If reps were paid only after receivables were collected, they would naturally avoid store owners of dubious creditworthiness. That strategy also benefited cash flow at a time when cash was scarce.

EXHIBIT 2.1

From the first company catalog, circa 1985

Source: The Company with permission.

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In a matter of months, Vera Bradley had many independent representatives taking orders from gift shops in several states. Each rep had a direct or indirect relationship with one or both founders. And as their numbers grew, so did revenue: from a mere $11,000 dollars in 1982 to $503,000 dollars in 1985, to $4.8 million in 1990 (Exhibit 2.2). And the business community took notice. In 1985, Barb and Pat received the national “Entrepreneur of the Year Award” from Ernst & Young, LLC (see Exhibit 2.3).

Fiscal Yr 1982 4 months Fiscal Yr 1985 12 months Fiscal Yr 1990 12 months

Sales 11 503 4,757

Cost of Goods  7 289 2,311

Gross Profit  4 214 2,446

Selling/Admin Expenses  2 178 2,142

Income before other Inc/(Exp)  2  35

Interest income     23

Miscellaneous      5

Interest expense  (7)   (46)

State tax expense

Other income/(Expense)  (7)   (19)

Income before distribution  2  28    285

EXHIBIT 2.2 Early revenues and expenses ($000s)

Source: The Company with permission.

EXHIBIT 2.3

Barb and Pat's advice to entrepreneurs

Concentrate on what you do best.

Don't be satisfied with the status quo—innovate and practice continuous improvement.

Choose the right people to work with: vendors, bankers, and employees.

Networking is important; it's important when people like you and you like them.

Don't be afraid to take risks.

Take one day at a time.

Follow your passion and have fun!

Downs and Ups

In the beginning, Barbara and Pat did everything but the sewing themselves—even selling. They brought in employees only as they needed them. The founders recognized from day one of their association how their aptitudes and interests overlapped in some areas and complemented in others. They made the most of this as they divided their labors in managing their growing enterprise. As COO Jill Nichols, who joined the company as controller in 1989, observed their roles in those earlier years, “Barb focused on design—the creative side—and sales, while Pat was more concerned with operations. Pat's more oriented to processes, and Barb is more into the creative side.”

Like every enterprise, Vera Bradley experienced a number of setbacks and made its share of mistakes. Barb and Pat's natural optimism, however, led them to work through these stumbles without discouragement. In one case, Pat mistakenly placed an order for hundreds of 20-inch bag zippers when their design called for a 12-inch item. Rather than fight with the supplier over an exchange—and possibly lose credibility as a buyer—the two women decided to turn lemons into lemonade: They created a new bag design with a 20-inch zipper. In another case, Barb placed an ad in a direct mail catalog for a particular bag made from an off-the-shelf fabric. That fabric was then ordered from the manufacturer in anticipation ad-generated sales. “Sorry, that fabric has been discontinued,” the manufacturer replied. Since it was too late to pull the ad, Barb and Pat bit the bullet and ordered 2,000 yards of a special printing of the fabric in question, enough for some 650 bags. This special order was costly, but the customers were happy.

In some cases, the entrepreneurs caught lucky breaks and made the most of them. One of these has become a favorite tale of the founders, and a part of company lore. While exhibiting at a New York City gift show in 1989, a woman approached the company's booth just as the hall was closing. She asked Pat if Vera Bradley would consider doing a special collection. Pat suggested that they discuss it further. The unidentified woman said, “I'll give you a call,” and then disappeared into the crowd exiting the building. Moments later, Pat kicked herself for not getting the woman's card. “Who knew if she would ever call us?”

Not long thereafter, the woman phoned the company and asked if Pat and Barb would be in New York anytime soon. As it happened, both founders were heading to New York for yet another gift show, so the woman suggested that they have lunch at Tavern on the Green. Located in New York City's Central Park, Tavern of the Green was a popular tourist stop, and the second largest grossing restaurant in the country!

And so they met for lunch. After dining, the conversation turned to business. Barb and Pat assumed that their hostess was interested in products she had seen at the gift show, and were prepared to discuss an order, at which point Pat excused herself to go to the ladies room. When Pat returned, she found that their hostess had gone off momentarily to assist with a busload of tourists that had just pulled up. Barb leaned over and whispered her latest intelligence: The woman did not run the gift shop; she owned the entire place and wanted them to design a special collection of bags for Tavern on the Green! Their next meeting took place in the restaurateur's apartment at the Dakota on Central Park West, where the three began designing the collection. The eventual release of the Tavern on the Green pattern gave a boost and credibility to the Vera Bradley brand.

Sourcing a Key Input

Fabric was the key raw material of the business. As sales accelerated, the founders realized that purchasing fabric at retail prices would impair profitability. Retail fabric was generally priced at four and one-half times wholesale. They needed to establish relationships with fabric wholesalers, but had not yet realized that their purchase volumes were still too small to interest wholesale textile suppliers. Pat noticed that some of the bolts of cloth they were using were imprinted with their manufacturers' names and address. She created a list of these and sent letters to each one requesting a meeting. To her surprise, none responded.

One of the manufacturers, VIP, was located in New York City, not far from the college where Barb's daughter was enrolled. So, Pat suggested that Barb drop in on that company the next time she visited the campus, which she did. Without invitation, Barb showed up in VIP's lobby and introduced herself. Mistaking Barbara for a representative of the much larger company with a name similar to Vera, the receptionist whisked her off to meet the company's Vice President of Sales, Leo Driscoll. As the two talked shop, Leo realized that they weren't speaking the same language. Barb didn't appear to understand the standard terms of the trade.

He asked me at one point how many pieces I wanted and I responded, ‘As many as you can sell me.’ To me, a piece was a two foot swatch; [to people in the trade] a piece was 25 yards. Then he asked, ‘Who are you with again?’ and I said, ‘Vera Bradley.’ His next comment was, ‘How did you get in here?’

Leo wasn't interested in taking on a small customer like Vera Bradley, but he was amused and impressed by his guest's affirmative attitude. The two hit it off so well that he accepted her order for 500 yards of fabric—VIP's rock-bottom minimum order quantity.

Barbara attributes her success in this and similar encounters to advice received from her father many years earlier: “First, sell yourself, then your company, and then your product.” In the years that followed, Leo Driscoll became a friend and mentor to Vera Bradley, and his company was rewarded with larger and larger orders.

Culture

Barbara and Pat knew from the start that company culture would play a large role in their success and their own personal satisfaction. Because they thought of the company as a family, they hired family members, relatives, friends, and friends of friends who seemed to fit in with the Vera Bradley family—people whom Pat and Barb would enjoy spending time with: “nice people” who felt as passionate about the products as they did. “We focus less on the bottom line than on our culture, giving back [to the community], and having fun,” Barb says.

If you walk around this office, you'll see that people are laughing and having fun. Everyone is on even terms here. You never say, ‘She works for me.’ Instead, we work together. I'm insulted when someone says, ‘Barb is my boss.’ We're in this together. [For example], I had six of the girls over for dinner at my house last night. We had all been working late.

Growth and Challenges

By 1990, Vera Bradley bags were catching on in many parts of the country, and each semiannual new product launch was more successful than the previous one. The founders were happy with their progress and the fact that they were creating jobs in and around Fort Wayne. But they were barely beyond the level of a cottage business, and a number of hurdles stood between them and the larger enterprise they both envisioned:

Images The business had outgrown the current system of farming out manufacturing to independent sewers who showed up in increasing numbers at Barb's basement door. And the quality of their work was disturbingly variable.

Images Gift stores were their “bread and butter,” but these represented a small segment of the venues where women shopped.

Images Despite initial market testing success with college-age girls, the bulk of sales was going to 30- to 60-year-old women. Would it be possible to address a younger demographic without losing these committed customers?

Images Vera Bradley had to design its products around the off-the-shelf fabrics offered by VIP and other wholesalers—mixing and matching existing patterns to produce uniquely styled bags. Manufacturers needed a 9,000-yard order before they would print a special pattern, but the company's production had not yet reached that level. This was putting a constraint on Vera Bradley's number one capability: design.

Never short on confidence, Pat and Barb pondered each of these issues.