

NGFN Food Hub Collaboration

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FOOD HUB BENCHMARKING STUDY

REPORT ON FINDINGS **2013**

W WALLACE CENTER
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 FARM CREDIT EAST

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 morse marketing connections, llc
making connections to build sustainable food systems

INTRODUCTION & BACKGROUND

DEFINITION AND KEY CHARACTERISTICS OF REGIONAL FOOD HUBS

A regional food hub is a business or organization that actively manages the aggregation, distribution, and marketing of source-identified products primarily from local and regional producers to strengthen their ability to satisfy wholesale, retail, and institutional demand. “Source-identified” means that, to some extent, the stories of the food, the producer, production methods or the location—stay with the product. One distinguishing characteristic of a food hub, as compared to a conventional produce wholesaler, is that food hubs typically have an explicit mission. By design, many food hubs prioritize strengthening producer capacity and increasing their access to markets. For additional information and resources on food hubs and their impacts on producers, communities, consumers and more, please refer to the Regional Food Hub Resource Guide and the 2013 National Food Hub Survey (both developed through the NGFN Food Hub Collaboration, and available at <http://foodhub.info>).

Although the definition of a food hub includes “business or organization”, the majority of food hubs are operated as businesses, regardless of tax filing status. Even the nonprofit food hubs are striving (and in many cases succeeding) to support all of the core functions of aggregation, distribution, and marketing, with revenue generated through sales or services. It is understanding the sustainable profitability of food hubs that motivates this benchmarking study.

Though hubs share many features, they represent a diversity of business models. Some sell exclusively wholesale to businesses, others only to retail consumers, and yet others to a combination of both. Some act more as brokers, others have significant infrastructure; some operate packing lines, while others require producers to pack and grade their own product, etc.

BENCHMARKING STUDIES

A typical benchmarking study collects historical financial results from similar businesses, as well as operational measures such as how many miles were driven by delivery trucks, or how many full time worker equivalents were employed. This information is compared to peers in the study, and then analyzed to determine a range of performance. The value of benchmarking rests in its ability to give the big picture of the sector being studied, as well as very detailed information about how each participant in the sector might be able to improve financial and operational performance.

BENCHMARKING FOOD HUBS

In the area of local foods there is a tremendous lack of data. Part of the reason for this is that USDA and other data collectors have traditionally focused on *what* farm product was being sold, such as grains, eggs, beef, or watermelons. Understanding local and regional food systems requires a shift to be able to track sales, volume, price, and other activity in the marketing channel we call local and regional foods.

Understanding how this market sector works is important not just to farmers and food hub operators, but also to lenders, investors, and even savvy grant makers, who need to understand where the risks are for each business function in the value chain, and for the sector as a whole. Many predict that consumer driven demand for local foods will continue to grow in economic significance for farmers and in cultural significance to communities.

METHODS

PARTICIPANTS

Approximately 60 hubs were invited to participate in the study. Full data submissions were received from 18 food hubs, however only 15 of those hubs were included in the benchmark numbers for a variety of reasons, including insufficient detail to allow comparison of financial or operational details.

DATA COLLECTED

- 2011 & 2012 Balance Sheets
- 2012 Income Statement
- 2012 Statement of Cash Flows
- Questionnaire Responses (see Appendix B)

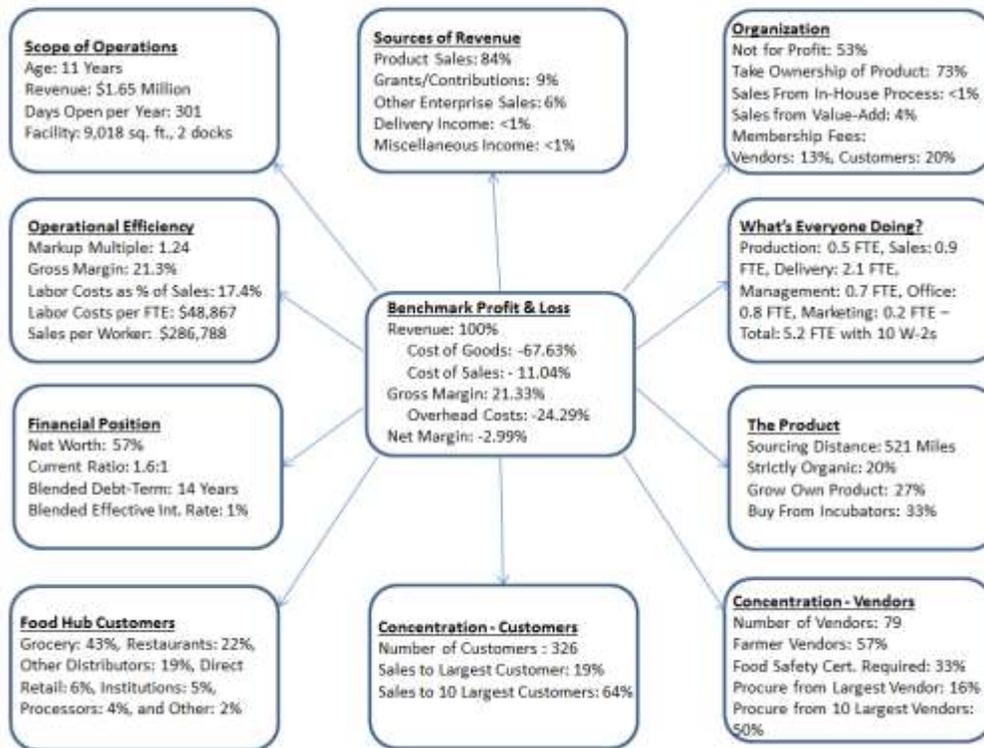
DATA SUMMARY

The data was collected from the participating hubs May – July 2013, and covered the 2012 fiscal year. There were a number of different product mixes and revenue streams; however hubs were compared across the industry rather than disaggregated into sub-groups. Overall, the information received was detailed and well organized.



FINDINGS

Benchmarking a Food Hub



Benchmarking study averages overview

*All of the figures are an average of the respondents; for the more complete view of the financial metrics, please see Appendix A for the range of these numbers. Because of the small sample size, the range of results is more descriptive than the average of results.

SCOPE OF OPERATIONS

Scope of Operations	
Age of Food Hubs	11 Years
Revenue	\$1.65 Million
Amount of Days in Operation	301 Days
Facilities	
Square Footage	9,018 Feet
Number of Loading Docks	2 Docks
Delivery Fleet (Annual Miles Driven)	54,011 Miles



Food hubs often approach their markets differently. Some are seasonal and others operate year round, often depending on the growing season in the area. Food hub operators must decide whether or not it’s necessary to shut down during slow months to conserve expenses or try to maintain sales in order to offset ongoing overhead costs.

THE PRODUCT

The Product	
Sourcing Distance (Miles)	521 Miles
Strictly Organic	20%
Grow Some of Own Product	27%
Buy From Own Incubator Farms	33%

Many food hubs source local products. However, the functional definition of local varies depending on factors such as the time of travel for delivery, distance in miles, state boundaries, etc. While a definition of local based strictly on distance may be restrictive, we found that the average sourcing distance for food hubs is 521 miles. Additional factors that affect sourcing distance can include the product mix or goals of the food hub. For instance, if the food hub will only sell organic products, their sourcing distance may need to increase in order to gather certified product. In this study, we found that 20% of hubs are strictly organic. Other hubs we studied (27%) grow some of their own product rather than procuring everything from vendors. This entails additional farm labor and operating costs, not to mention agricultural production risks. Similarly, several food hubs have a community-based education mission, and they have developed programs to teach beginning farmers how to produce and market their agricultural products. These are considered incubator farms, and 33% of the hubs we studied operate farms as part of their business model.

ORGANIZATION AND OPERATIONS

Organization and Operation	
"Not for Profit" Status	53%
Take Ownership of Product	73%
Sales From In-House Processing	<1%
Sales From Value-Added Products	4%
Membership Fees Charged	
To Vendors	13%
To Customers	20%

We found many variations in organizational structure. The majority of the food hubs in the study (53%) consider themselves Not for Profit, and file within section 501(c)3 of the federal tax code. Almost three fourths of the hubs in the study take ownership of the product during the



course of the value chain. Many of these hubs put their own brand on the product to establish a marketplace identity that connotes a certain expectation of location-specific freshness and quality.

Although there has been significant attention paid to incorporating processing as a revenue stream at food hubs, this study revealed that less than 1% of sales comes from in-house processing (such as turning tomatoes into salsa). Similarly, the hubs that do track their sales of value-added product (i.e. salsa bought from a farmer and re-sold) make up only 4% of the hub’s sales. These are typically products with a higher mark-up and longer shelf life. Resale of value-added products purchased from farmers or other local vendors may serve to expand product lines and maintain sales through seasons when fewer farm products are available.

A significant minority of hubs in the study charge membership fees to their customers and vendors, 20% and 13%, respectively. Such membership fees increase revenue, but may ultimately reduce access to new or smaller customers.

SOURCES OF REVENUE

Sources of Revenue	
Product Sales	83.78%
Grants/Contributions	8.99%
Other Enterprises	6.35%
Delivery/Trucking Income	0.75%
Miscellaneous Income	0.13%

For the purposes of this study, product sales include all items bought and then re-sold. Sources of revenue are heavily weighted towards products sales at 83.78% of income. With income from grants and contributions at 8.99%, it appears that most revenue is from sales rather than dependence on outside contributions or private/government grants. Few food hubs charge for delivery, as reflected by delivery/trucking income at 0.75% of all income. It is not clear if such charges are based on a specific analysis of actual delivery costs. Other enterprise income (6.35%), and miscellaneous income (0.13%), make up the remainder of the revenue channels measured.

FINANCIAL POSITION

Financial Position	
Net Worth	57%
Current Ratio	1.6:1
Blended Debt Term	14 Years
Blended Effective Interest Rate	1%

*** Current ratio = current assets / current liabilities**

The overall financial position for the hubs is relatively positive. The average Net Worth for a hub in the study is strong at 57%, meaning that for every \$100 in assets utilized by the food hub, 57% are owned outright by food hubs and 43% were obtained through borrowing. Current ratio indicates a company’s capacity to pay its short-term obligations over the next 12 months. The current ratio (current assets divided by current liabilities) of 1.6:1 reflects the strong net worth of food hubs in the study.

The blended effective interest rate (the interest rate if each separate loan the company owes were theoretically combined into one big loan) of 1% is unusually low, likely because funding has come from direct investment by owners or philanthropy. If financing were coming from conventional lending sources, market interest rates would result in a higher blended interest rate. Furthermore, the blended debt term (the weighted average length of time to pay off all loans) of 14 years is slightly higher than expected. However with an effective interest rate of only 1%, a longer debt term is less of a concern.

LABOR EXPENSES IN FULL TIME EQUIVALENTS (FTE)

Labor Expenses in Full Time Equivalents (FTE)	
Employee Role	Paid FTE
Production/Growing	0.5
Sales	0.9
Delivery/Distribution	2.1
Management	0.7
Office/IT	0.8
Marketing	0.2
Total	5.2
Number of W-2s Issued	10

Labor is often one of a distribution business’ biggest expenses. In addition to looking at the total dollars spent on labor, we examined dollars spent on tasks to allow a higher degree of comparison based on the efficiency of labor. Since labor is a substantial portion of operating costs, it is all too often the first thing cut in a cost-conscious environment. By closer tracking of the labor cost for particular tasks, we can identify potential improvements in labor efficiency. For example, considering labor efficiency it may be more effective to invest in a forklift versus using hand trucks, or modifying the warehouse design to reduce material flow bottlenecks or load re-palletizing. Such spending on equipment to reduce labor costs could be shown to pay for itself quickly where task-oriented labor use is known.

Food hubs average five full time equivalent workers (FTEs). The amount of labor devoted to each role was divided into the following categories: production/growing, sales, delivery/distribution, management, office/IT, and marketing. Delivery/Distribution is by far the

most time consuming work with over 2 FTEs allocated to it, with the remaining categories all using under 1 FTE. Ten W-2s were issued for each hub, which means that together ten individuals perform the work equivalent to 5.2 full time workers. Therefore, many workers are likely seasonal or were part-time.

We used FTEs (total hours worked divided by 2,040 hours per full time employee) in this study in order to compare labor effort across the different sizes of work forces of hubs. Establishing the number of paid FTEs, we evened out the effects of full time, part time, seasonal, double time people, etc. Note that this approach does not account for volunteer labor, yet almost all of the food hubs use volunteer labor but do not track it. This is a significant gap in labor utilization and cost information. For the food hubs, it is important to know how much volunteer labor is used, and in what categories, because if the “free” labor were unavailable there would be no indication of its replacement cost in wages. Substitution of volunteer labor with paid labor may not be economically justifiable, but current data makes this difficult to ascertain.

FOOD HUB CUSTOMERS

Food Hub Customers	
Type of Customer	% of Sales
Grocery/Food Stores	43.25%
Restaurants and Caterers	21.52%
Other Distributors	18.81%
Direct Retail	6.13%
Institutions (Schools, Government)	4.51%
Processors	3.74%
Other	2.04%
Total	100.00%

One of the most important decisions for food hub operators is determining to whom they are going to sell their products. For food hubs in this study, the most common choice is grocery/food stores, making up over 43% followed by restaurants and caterers (21.5%), other distributors (18.8%), and direct retail or storefront (6.1%). In aggregate, these same four customer types make up almost 85% of all food hub sales to customers. This isn’t necessarily bad, however one has to recognize these four types of customers serve markets with very competitive pricing. Therefore, it may be difficult for food hubs to sell high-margin products, and indeed prices are likely to decrease. Many of the items sold are perishable products, which can create a move-the-product-sell-at-a-loss situation that results in very thin margins and low-markups.

CONCENTRATION - CUSTOMERS

Concentration - Customers	
Number of Customers	326
Product Sales to Largest Customer	19%
Product Sales to Largest 10 Customers	64%

Product sales to the largest customer make up 19% of total sales, and products sold to the largest 10 customers make up 64% of total sales. This degree of sales concentration represents a moderate risk to the average food hub business, where the loss (or non-payment) of the biggest account would have an immediate adverse impact on cash flow. Where there is such concentration, developing and maintaining close customer relationships is an essential business practice that should be reinforced by robust credit policies to assure quick payment from customers and having pre-arranged access to working capital as risk mitigation strategies.

CONCENTRATION – VENDORS

Concentration - Vendors	
Number of Vendors	79
Farmer Vendors	57%
Food Safety Certification Required	33%
Purchases with Largest Vendor	16%
Purchases with 10 Largest Vendors	50%

Similar to our review of the revenue streams, we also analyzed where those product sales are sourced. The number of vendors (79) and specifically farmer vendors (57%) is expected in the context of the food hub business model. Food hubs are only relying on their largest vendor for 16% of their product, slightly less concentration than on the sales side of the business. This study did not assess the reliability of food hub suppliers' farms, but it is refreshing to see that these food hubs are diversifying risk through the number of suppliers. Only 33% of food hubs in the study require a specific food safety certification of their vendors.

BENCHMARK PROFIT AND LOSS

Benchmark Profit & Loss	
Revenue	100.00%
Cost of Goods	-67.63%
Cost of Sales	-11.04%
Gross Margin	21.33%
Overhead Costs	-24.29%
Net Margin	-2.99%



Of great importance to this benchmarking study are the profit and loss benchmarks for the food hubs. Unfortunately, the average results showing losses is likely a consequence of a small sample size. Further analysis to reveal more detail and better understand why hubs in certain regions were performing similarly could not be done as it would tend to breach confidentiality by allowing identification of individual study participants. Nevertheless, these data are from real businesses doing real work, so despite the small sample size they are substantial and meaningful. Profit and loss was examined on a weighted average basis using percentage of sales rather than whole dollars, which allows comparison across all food hubs in the study.

It is significant to note that the range is up to 22% profit, demonstrating the potential of the food hub model. However, there is an inherently high amount of overhead cost in order to keep a food hub operating such as investment in the principal plant, warehouse, and transportation/delivery fleet. Improved margins and doing more with less are obvious but not necessarily implementable strategies to increase overall profitability. It is typical of a high volume, low margin business that overhead costs need to be spread over a large amount of sales.

For every sales dollar of revenue of the hub, around 68 cents is spent on the Cost of Goods Sold (COGS), meaning the expense of procuring the product that is re-sold. Another 11 cents of each dollar are spent on organization, packaging and delivery of that product, referred to as the Cost of Sales, or the expenses incurred to sell products including commissions, marketing costs, and delivery costs. Thus, 21 cents of every dollar of sales are left over to cover the overhead of the business (called the Gross Margin, or total sales minus variable expenses). This includes depreciation, a non-cash expense that is charged to reflect the fact that plant and equipment wear out over time and are therefore worth less as an owned asset if they were to be sold. As alluded to earlier, these overhead costs are significant, at 24 cents of every dollar of sales, and so minimization of overhead needs to be treated as a major area of improvement for food hub financial performance (Overhead Costs are those expenses incurred regardless of sales volume including salaries, rent/mortgage, utilities, and insurance). This leaves a final net margin for our limited sample of food hubs that is negative, or represents a net loss.

OPERATIONAL EFFICIENCY

Operational Efficiency	
Markup Multiple	1.24
Gross Margin	21.30%
Labor Costs as a Percent of Sales	17.40%
Labor Costs per Paid FTE	\$48,867
Sales per Worker Equivalent	\$286,788

We have reviewed the overall sales, costs, vendors, customers, and how those affect the income statement, but what about the operational efficiency of these hubs? The markup multiple of the hubs is 1.24, with a Gross Margin of 21.3%. The Markup Multiple is a comparison of the cost of the product to the price at which it is sold. For example, a tomato purchased for \$1.00 is being sold by food hub study participants for \$1.24. And this is an aggregate of all products, in the whole business, so compares revenue for all products to the cost of all products (even those that are not sold). The labor cost as a percentage of sales is 17.4% (not including volunteers), with labor costs per paid FTE at \$48,867 and sales per worker equivalent at \$286,788.

Typically, in a retail environment, you aim to have a Markup Multiple close to 1.6. As a general rule, wholesalers usually get about 1.5 on average, depending on the product. The more perishable the product, the less of a markup is usually possible. If your markup is on the low side, there are 3 places you can start to examine: 1) appropriate sales pricing; 2) appropriate purchase pricing; and 3) sales shrinkage (goods purchased but not sold, such as samples, spoilage, etc.). No matter what, the revenue received should cover the cost of all expenses and then some. Raising or lowering the price is not always the easiest decision.

FINAL THOUGHTS

Establishing a baseline level of financial performance and operational trends of food hub businesses was the primary goal of this study. Although reporting was constrained by the small number of food hubs studied, valuable information was gathered and the survey instrument and methodology was validated. The need for more information about food hubs and their role in local food systems was confirmed by this study, and has provided the impetus to repeat an expanded study in 2014.

Food hubs are an emerging sector, and as such, partners, investors, entrepreneurs, and lenders need actionable information to support the sound financial and operational planning necessary for sustainability.

COLLABORATION

This study was conducted by Farm Credit East, Morse Marketing Connections, Farm Credit Council, and Wallace Center at Winrock International.



APPENDIX A: RANGE OF FOOD HUB BENCHMARKS

Net Margin		Gross Margin	
33rd %	1%	33rd %	24%
Median	5%	Median	30%
67th %	14%	67th %	43%
Average	-3%	Average	21%
Total Sales		Sales per Employee (FTE)	
33rd %	\$824,573	33rd %	\$104,086
Median	\$1,102,579	Median	\$257,573
67th %	\$1,460,148	67th %	\$301,441
Average	\$1,653,780	Average	\$286,788
Cost of Goods Sold		Total Overhead Costs	
33rd %	\$409,333	33rd %	\$167,072
Median	\$626,492	Median	\$278,889
67th %	\$918,690	67th %	\$624,632
Average	\$1,260,780	Average	\$444,533
Number of Customers		Number of Vendors	
33rd %	130	33rd %	45
Median	173	Median	80
67th %	300	67th %	85
Average	326	Average	79
Facility Size (Square Feet)		Sourcing (Number of Miles)	
33rd %	2,500	33rd %	75
Median	4,000	Median	250
67th %	7,285	67th %	300
Average	9,018	Average	521

*In these charts the data are broken down into percentiles to show the range of the numbers. Because of the small sample size, the range of results is more descriptive than the average of results.



APPENDIX B: QUESTIONNAIRE FOR FOOD HUB PARTICIPANTS

- 1) What year was the food hub established?
- 2) How many days per year is your food hub open for business?
- 3) How big is your facility (square footage)?
- 4) How many loading docks do you have?
- 5) Is your food hub a “Not-for-Profit” organization?
- 6) What do you consider “local”?
- 7) From how far away do you source your products?
- 8) Do you sell ONLY organic products?
- 9) Do you have a food safety certification requirement of your vendors?
- 10) Do you grow any of your own produce?
- 11) Do you buy from your own incubator farmers?
- 12) How many miles were driven by the delivery fleet?
- 13) Do you take ownership of the products you sell?
- 14) Can your customers order online?
- 15) How many vendors do you buy from (a vendor is an outfit that you, the food hub, buy something from)?
- 16) How many of these vendors are farmers?
- 17) How much do you spend (\$) with your largest vendor?
- 18) How much do you spend (\$) with your largest 10 vendors?
- 19) Do you charge a membership fee to your vendors?
- 20) How many customers do you sell to (a customer is an outfit that buys something from you, the food hub)?
- 21) What are the sales (\$) to your biggest customer?
- 22) What are the sales (\$) to your 10 largest customers?
- 23) Do you charge a membership fee to your customers?
- 24) What were your sales (\$) to:
 - a. Restaurants and caterers
 - b. Grocery/food stores
 - c. Institutions (school, hospital, government)
 - d. Your own direct retail
 - e. Processors
 - f. Other distributors
- 25) What are the sales (\$) of items you process in-house?
- 26) What are the sales (\$) of value added product you buy to resell?
- 27) What is the value (\$) of purchased product that was thrown away (spoiled, damaged, non-salable, stolen, etc.)?
- 28) How many W-2s were issued?
- 29) How much did you pay for workman’s compensation insurance and where is that expense recorded?
- 30) How many payroll hours were paid for each of these departments:
 - a. Sales
 - b. Delivery/Distribution
 - c. Office/IT
 - d. Management
 - e. Production/Growing
 - f. Marketing