

Returns In Alternative Marketing Channels for Organic Producers

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OVERVIEW

- Growth in Direct Marketing
- Objective
 - compare relative marketing costs and profitability of different marketing channels
- Approach—case studies
- Findings
- Conclusions

Growth In Direct Marketing

- Direct agricultural marketing, particularly farmers' markets, has grown in popularity
 - Farms engaged in direct marketing increased from 86,432 in 1992 to 110,639 in 1997 and 116,733 in 2002
 - Revenues rose from \$404.1 million in 1992 to \$812.2 million in 2002
- Promoted extensively by small farm programs
 - Farmers markets
 - CSAs
 - Roadside stands



But some recent articles.....

Farmers burn out on markets

San Francisco Chronicle, September 19, 2007

"Sales have gone down as the number of produce sellers has increased and the diversity of items on everyone's tables has increased. This is great for shoppers but makes life rough for us."

FARMERS MARKET; A victim of its own success?

LA Times, April 11, 2007

"Farmers markets saved me in the past when otherwise I would have been unable to make payroll. They really need to be there for farmers who are in that situation, but when it becomes inefficient, you ought to move on and make room for someone else. For me it was a question of how I could best spend my time."

Approach

- Compare the relative marketing costs and profitability of different marketing channels—farmers' markets, CSAs and wholesale markets
- Case studies of 3 organic fruit and vegetable producers
 - Well established
 - Small, medium & large
 - Northern California
 - Sell through farmers markets, CSA and wholesale

Case Study Farms, 2005

	Small Farm	Medium Farm	Large Farm
Acres	20	70	240
Full-time Employees (year-round)*	2	7	30
Total Revenues	\$229,013	\$627,046	\$2,276,818
Wholesale Revenues	\$45,086	\$131,611	\$1,607,769
Farmers' Market Revenues	\$50,363	\$196,960	\$435,126
CSA Revenues	\$133,564	\$298,475	\$233,923
*Excludes operators			

Approach

- Excluded all costs involved in crop production
- Developed detailed list of postharvest activities involved in the flow of product from the field to consumers for the different marketing channels
- Subsequently grouped these activities into 3 categories
 - packing and storage
 - transportation
 - marketing and administration

Measuring Costs

- Chronological sequence of events involved from harvest through sales
 - examined separately for each day of the week for the seasons (winter, summer) and for each market channel
 - elicited estimates of staffing and hours of labor involved for each marketing activity in each market channel type
 - determined what purchased goods and services and capital assets were utilized

Measuring Costs

- Used original purchase values and straight line method to calculate depreciation
- Included opportunity costs of capital (using short-term rate of 7.50% for operating capital and long-term rate of 6.01% for capital costs)
- Valued operator labor at same rates paid to hired labor for the same activity

Sorting & Packing Costs

- Sort & pack product – facilities & equipment
- Sort & pack product – labor & materials
- Load, unload truck – labor
- Maintain market supplies & equipment – labor
- Training & supervision - labor

Transportation Costs

- Delivery vehicle - capital & operating costs
- Delivery – labor
- Contracted Trucking
- Tolls
- Driver training & delivery management - labor

Selling & Administrative Costs

- Market communications – labor
- Wholesale sales – labor
- Retail sales – labor
- Marketing materials costs – labor and materials
- Unsold product
- Sales staff administration – labor
- Office facilities, equipment, supplies, services use
- Record keeping systems
- Account maintenance, banking, bookkeeping – labor
- Other office staff – labor
- Business planning – labor

Unsold Product—a major selling cost

- Included bad debts for uncollectible accounts of wholesale and CSA customers
- Produce provided at no charge to CSA site hosts
- For farmers' markets, there are three types of unsold product:
 - Product used for sampling, customer bonuses, and rounding-off weights
 - Product not sold because of lack of demand (such as bad weather) or because the farmer used the marketing strategy of keeping the tables full until the end of the market day. Much of this product is subsequently donated
 - Product that is too damaged/overripe to be sold and is disposed of

Unsold Product—a major selling cost

- Estimated unsold product based on daily farmers' market revenues and volumes shipped to and returned from a sample of farmers' markets
- Proportion of delivered product that was unsold varied from 17% for the small farm to 20% for the medium and large farms
- Valued unsold product at net profit (actual market revenues less all other marketing costs)
- Was 2% of all expenses for small farm, 14% for medium & large farms

Findings-Labor Costs

- Labor was the highest marketing expense item for all 3 farms
- For small farm, labor comprised 76.6% of all marketing costs, ranging from a low of 67.0% for the wholesale market to 82.3% for farmers' markets
- For medium farm, labor expenses comprised 50.4% of all marketing costs—was similar across market channels
- For large farm, labor comprised 46.8% of total marketing expenses for the large farm, varying from 41.6% for wholesale market to 57.1% for farmers' markets

Marketing Related Labor Costs

	All Channels	Wholesale	Farmers Market	CSA
SMALL FARM				
Cash Labor Expenses	\$37,677	\$6,623	\$17,175	\$13,878
Imputed (Operator) Labor Expenses	\$51,240	\$4,001	\$16,368	\$30,872
Total Labor Expenses	\$88,917	\$10,624	\$33,543	\$44,750
% of Total Expenses	76.6%	67.0%	82.3%	75.1%
% of Total Revenues	38.8%	23.6%	66.6%	33.5%
MEDIUM FARM				
Cash Labor Expenses	\$107,552	\$12,127	\$39,255	\$56,170
Imputed (Operator) Labor Expenses	\$21,714	\$2,459	\$14,825	\$4,430
Total Labor Expenses	\$129,266	\$14,586	\$54,080	\$60,600
% of Total Expenses	50.4%	53.9%	51.6%	48.0%
% of Total Revenues	20.6%	11.1%	27.5%	20.3%
LARGE FARM				
Cash Labor Expenses	\$304,305	\$166,974	\$95,020	\$42,311
Imputed (Operator) Labor Expenses	\$45,759	\$19,411	\$17,262	\$9,086
Total Labor Expenses	\$350,063	\$186,385	\$112,282	\$51,397
% of Total Expenses	46.8%	41.6%	57.1%	49.6%
% of Total Revenues	15.4%	11.6%	25.8%	22.0%

Marketing Costs For All Delivered Product By Channel, Medium Farm

	Total	Wholesale	Farmers' Market	CSA
Revenue	\$627,046	\$131,611	\$196,960	\$298,475
% of delivered product that is paid for (not unpaid, spoiled, or donated)		100.0%	80.0%	91.4%
<u>Packing & Storage Costs</u>				
Packing labor, packing shed utilities, supervision & administration, facility & equipment depreciation	\$48,383	\$11,338	\$11,338	\$25,707
Packing materials	\$10,019	\$6,022	\$0	\$3,997
Total packing & storage costs as percent of sales revenue	9.3%	13.2%	5.8%	10.0%
<u>Transportation Costs</u>				
Delivery vehicle fuel, insurance, maintenance, registration, depreciation	\$25,425	\$1,807	\$14,784	\$10,535
Delivery labor, driver supervision, transportation administration	\$23,331	\$1,323	\$15,065	\$6,943
Contracted trucking	\$1,307	\$1,307		
Tolls	\$1,070	\$388	\$341	\$341
Other transportation costs	\$6,268		\$412	\$5,856
Total transportation cost as percent of sales revenue	9.2%	3.7%	15.3%	6.0%
<u>Administration & Selling Costs</u>				
Office costs - rent or depreciation, utilities, phone, other general office services, and equipment depreciation	\$14,573	\$1,337	\$1,588	\$11,648
Postage, CSA newsletter costs, non-production payroll services, printing & copying, bookkeeping & administration labor	\$47,410	\$3,528	\$5,350	\$38,532
Selling Costs - Market supplies, conference & event fees, farmers' market fees, CSA database & website, selling labor	\$42,950	\$0	\$39,050	\$3,900
Opportunity cost of unpaid product	\$35,725		\$16,882	\$18,843
Total administration & selling costs as percent of sales revenue	22.4%	3.7%	31.9%	24.4%
Total Marketing Costs				
	\$256,461	\$27,050	\$104,811	\$126,301
Net Income (Revenue less total marketing costs)	\$370,585	\$104,560	\$92,150	\$172,174
Marketing Costs as % of Sales Revenue	40.9%	20.6%	53.2%	42.3%

Net Rate of Return to Marketing

FARM	MARKET CHANNEL			
	All Channels	Wholesale	Farmers' Markets	CSA
Small	49.3%	64.8%	19.1%	55.4%
Medium	59.1%	79.5%	46.8%	57.7%
Large	67.1%	72.2%	54.8%	55.7%

Conclusions

- Farmers' markets generated the lowest net rate of return to marketing for all 3 farms
- Wholesale channel produced the highest rate of return for each farm
 - may be atypical since these farms had high proportions of their wholesale transactions as direct sales to grocery stores and restaurants
- CSA channel generated 2nd highest return for all 3 farms, was similar across the farms

Conclusions

- Producers can earn “full retail” by direct marketing but the price premia are not pure profit
- Can producers actually increase their net returns through direct marketing by either:
 - providing the same services at a lower cost
 - eliminating or streamlining costs, such as transportation or packaging

Benefits of Direct Marketing to Producers

- Direct marketing can enhance producers' returns
 - Farmers' markets and CSA can create markets for produce that would be considered unmarketable through the wholesale channel
- Newer producers can sell at farmers' markets while developing the broader product lines needed for a successful CSA and higher production volumes needed to sell to wholesale customers
- Use their presence at a farmers' market to develop future CSA, restaurant and small wholesale customers
- Marketing costs in direct marketing channels can be substantial, but direct marketing--when used in conjunction with the wholesale channel--can increase producers' overall profitability



Exploring Options



- Direct marketing “puts a face” on consumers’ food and provides fresher, more flavorful produce
- Develop less labor-intensive options
 - Farm to institution
 - 2 major factors constraining CSA growth—product quantity and product choice (Perez, Allen & Brown, and Oberholtzer)
 - CSA hybrid structures
 - Offer different sizes of boxes and/or every other week deliveries
 - Exchange products with other local producers
 - Aggregated CSA, such as Pike Place Market Basket CSA that contracted with approximately 3 dozen farms
 - Reestablishing Public Markets