

NESAWG 2015 *It Takes A Region* Conference

Distribution & Food Hubs Discussion & Work Group

Presenters: Jeff Farbman, Jim Barham, Ann Karlen, Michael Rozyne, and Laura Edwards-Orr

Session One

Big ideas

- Distribution and logistics working group developed into the food hub-working group.
- Food hubs arose due to a failure to satisfy markets.

Main Questions

- How do food hubs compete with market place giants?
- Where are we?
- Where are we going, and how do we live through it?
- Who are the food hub innovators?

Jeff Farbman: Overview of Wallace Center and National Good Food Network collaboration studies

- 2014 Benchmarking Study
 - Done with Farm Credit East
 - 48 participants
- 2015 National Food Hub Survey
 - In collaboration with Michigan State Center for Regional Food Systems
 - 149 self-report participants
- Keep in mind that food hubs are a very diverse group, which can impact averages
- How big are hubs?
 - Size of local foods market:
 - \$6 billion estimated by USDA (known to be an underestimate)
 - \$12 billion estimated by AT Kearney
 - ~9% annual growth through 2018
 - Size of food hubs
 - ~350 hubs nationwide
 - \$1/3 billion
 - 98% of food hubs expect demand for local food products to increase in the next two years
 - Half of hubs have revenue \leq \$500,000
 - Of 128 food hub respondents, they employed 2187 workers
 - 80% of employees were women
 - Includes full-time and part-time
 - Of the 40 hubs that responded in 2013 and 2015, they experienced growth in employment
- Are hubs viable?

- Income
 - Average hub had a 2% loss
 - The highest 25th percentile had a 4% profit
 - For-profit: +1%
 - Non-profit: -7% (not including grants/contributions)
 - Retail: +6%
 - Wholesale: 0% (breakeven)
 - Hybrid -1%
 - Age:
 - <3 years: -34%
 - 3-5 years: -49%
 - 5-10 years: 12%
- Operating Expense Ratio (OER) = (Total Operating Expenses)/(Total Gross Revenue)
 - On average, hubs are profitable
- Are hubs getting *more* viable?
 - OER ratio has gone down from 2013 to 2015
 - This is a positive sign
- Reliance on grant funding (111 respondents):
 - Not at all: 45%
 - Somewhat dependent: 40%
 - Highly dependent: 15%
- Are hubs “Making a Difference?”
 - Impact on consumer
 - Supply side impact
 - Average hub has 80 suppliers. Roughly 24,000 suppliers across the entire food hub system.
 - About 1/3 owned or operated by women
 - 92% of hubs report **most or all** farm/ranch suppliers are **small or mid-sized** (classified as <\$500,000 in gross sales)
 - 72% say they increased the number of small farm suppliers since their hub began
- What are top challenges?
 - FSMA and food safety
 - 83% concerned on their own ability to comply
 - 50% were very or extremely concerned
 - 98% concerned over the ability of suppliers to comply with FSMA
 - 2015:
 - Most hubs say they cannot meet these challenges in the next 12 months

Jim Barham: The 8 C's of Food Hub Innovations

- C for Classical Economics
 - Definition: Economics is the study of how to efficiently allocate scarce resources

- Externalities: How to minimize our external costs
- C for Cooperation/Collaboration
 - Example: Working with smallholder farmers in Tanzania. Offered training on crop diversification and marketing practices. However, farmers were unable to reach markets. The middlemen getting products to market suffered their own problems, such as lack of access to capital.
 - Created learning platforms where all members of the supply chain were brought together.
- C for Community Currency
 - Mission driven businesses look at all the ways they can benefit their communities. Examples: Environmental stewardship, economic development, jobs, and healthy individuals.
 - Oxygen Mask Rule of food hub viability: secure your own financial viability before helping others.
- C for de-Commoditization
 - Product differentiation is key: an apple is not an apple.
 - Values and attributes you give to a product.
 - Ex. Oklahoma Food Coop: “Y’all bon appétit, ya hear”
 - Ex. This Old Farm: “rejuvenating the land, one farm at a time”
 - Value can be added through emphasizing local food, tastiness, freshness, and health benefits.
- C for Clear
 - In marketing: “Clear is the new clever.”
 - Ex: “Know your farmer, know your food.”
- C for de-Centralization
 - Up until now, we’ve been told the centralizing will improve efficiency and profits
- C for Coordination
 - Decentralization makes sense when there is coordination.
 - Example: Central Appalachia Food Hub Network is identifying optimal trading routes.
 - Example: Michigan Food Hub Network is exploring shared IT platform with searchable database across the region.
- C for Cluster/Co-location
 - Food innovation clusters involve co-locating production, distribution, and aggregation.
 - Example: Local Food Chicago has a very robust distribution system. They move up to \$5 million dollars to product. They have a full market grocery space filled with multiple businesses.
- C for Conclusion
 - Food hubs are upending the classical model...

Laura Edwards-Orr: Red Tomato

- Reflection: This field of study and data are remarkable. Seeing hubs in context is brand new and incredible.
- Efficient allocation of scarce resources.
- We need to keep a clear vision of our purpose and of challenges.
 - How do we keep with our values and customers while following new opportunities?
- Make sure to understand the hub system and the larger food system to know what we're good at and where we need to create smart collaborations.

Discussion

- What's the food hubs role in identifying infrastructure gaps? Is anyone else filling that gap?
 - A gap to increasing access to local food is the protein side. There are few USDA slaughter facilities. There are none for poultry, other than private ones owned by corporations.
 - James Barham: We don't need a food hub in every county. Before creating a food hub, these questions need to be asked: What distributors are there? What facilitators are there? Value-chain coordinators look into these questions and help connect the dots. In January, USDA will hopefully expand support of these coordinators. Lauren Gwen from Oregon State looked at slaughter capacity. It turned out to be more of a coordination issue than capacity issue.
- How do you find the right size as a farmer or food hub business? And what do you think about when making that decision?
 - Laura Edwards-Orr: it's about the mix more than the number. Grossed \$4.6 million last year. That's a drop in the bucket in the food industry. We think strategically about the impact we want to have when determining growth.
 - Jeff Farbman: There are some hubs that are too small to be viable. It is a volume business. The size necessary varies on model. When starting a food hub, make sure you have a food hub to get to size quickly.
 - James Barham: Financially viable food hubs generally have a break even of \$1 million. There are tech companies that go 20 years before grossing a profit. Give yourselves a break.
 - Laura: When we ran data, we were most sustainable at 5.5 employees. We had to think critically about how to use that number, and recalculate that number over time.
 - Jeff: We're at a moment in time when consumers are really hot about this. The market is growing, and there are supply constraints.
- SNAP is \$80 billion per year. Can we think of SNAP recipients as the oxygen mask for food hubs?
 - James: We need to see where there are successes of that happening and get it out there so people can be inspired. Let's see what works and what doesn't work.

- What is the power of public and institutional procurement as a market for mid-size producers with food hubs in the middle making it happen? Public schools are low-priced buyers. Profitable food hubs are generally retail direct to consumers. Wholesale are generally less profitable. Based on the current reality, where can we go?
 - Jeff: Schools K-12 are actually one of the more common markets.
 - James: There are very few food hubs that could just be servicing institutions. When you've secured your oxygen to high-market buyers, then you can turn attention to high need areas. You may be breaking even or seeing some losses, but you can sustain that if you have a profitable high-value market.
 - Laura: Unity of demand allows food hubs to make long-term plans.
- Are there collaborations between regional distributors and food hubs?
 - James: 40% of food hubs were selling to broad line distributors, which is pretty high. Highest growth in food distributors. Some food hubs are selling to distributors who sell to schools.
 - Laura: Unlike a retail chain that might have the resources to promote distributors. You have to do all the work to form relationships with chefs so they can explain to customers the added value of the produce. So both collaborating with broad line distributors and selling directly to buyers have challenges.
- Is there any idea where the impetus for the food hubs to be working with the distributors is coming from? Are consumers asking for the local food transparency?
 - James: No. I know case-by-case but not generalizing. It's probably a little bit of everything with no one thing more than another.
 - Audience member: Institutions are making demands that are being required of food service providers. The food service provider asks this of their broad line distributor who then approaches food hubs.
 - Michael Rozyne: We always think about the buyer as the bottleneck because you need a good relationship. But in this case we discovered that the distributors sales force are not absorbing our education on local food benefits. The QR code became a very important differentiator in the eyes of the sales force. Even if the broad liner had the same commodity from the same region on the same price list, QR code made local distinguishable. Gives the sales force confidence because there's something tangible.
 - Laura: The QR code is a case label. It all fully transparent supply chain for our customers. The broad liner doesn't have to do anything. Has so much value to the buyer. One customer, it was very important that the buyer could offer local foods as a choice.
- An observation of what he's seen over time is what's been the bottleneck. In 2010, it was all about "we don't know how to do this. We haven't figured out the logistics yet." And then it was "we don't have enough farmers." More and more it has become "the low-hanging fruit of demand has been picked." Especially in Vermont and the Northeast. The rate of growth seems to be flattening out in this region. If that's true, what's the next innovation? Does commoditization need to be more than local now if the demand is not there?

- Blue Apron: Is there any data on how food hubs have caused increases in agricultural production? One area that is in need of innovation is in the volume. I agree that the low-hanging fruit has been met, but there are new frontiers that need to be explored.
- Jeff: Is there reduced demand for local at Blue Apron?
- Blue Apron: Local is a very unique principle at Blue Apron. We're shipping our food halfway across the country, so we don't use local in our marketing very frequently. For our customer base, the demand is for organic more than anything else. That comes back to the consumer education piece. The number two from production standards disintegrates from there to non-GMOs, pesticides, and labor. I think local has a place in there, but I don't know how to articulate it.
- Laura: As we try to scale up the portion of the pie that food hubs have, a challenge we're going to have is that consumer demand is moving into alignment with the supply we have. For example, if consumer want cosmetically perfect fruit, we'll be out of sink. That's not possible.
- Audience Member: 20 years ago wholesale is what we were all railing against. Now, I'm working with new farmers teaching them that once they reach their time limit to directly marketing their food, they can pivot to the wholesale market.
- Jeff: The match made in heaven is food hubs and mid-size farms. Mid-size farms are declining. I assume these farms are run by the older generation and tend to be more conservative. They're probably less likely to join a three-year old model.
- What kind of value added are some people trying?
 - James: I was going to add Candy as another C for processing. We're seeing more and more diversification of products in food hubs for year round supply to buyers. More food hubs are saying, "we're thinking about getting into our own processing." But they're being smart and doing feasibility studies. Many of them see this isn't a viable model, but they are pursuing the profitable pieces.
- Freezing and vacuum packaging has been used by the meat industry since the 1960s. Why aren't more food hubs freezing?
 - James: It is definitely being explored. When it comes to food hubs, you need a large volume for freezing to be viable.
 - Audience Member: It's a big investment. Maybe it's a partnership and not something you do buy yourself.
 - Audience Member: My study found that the price increase from freezing was well above what institutions were willing to pay.
- I've been working on providing equal access to healthy food. We've hit a wall on farm suppliers.
 - Jeff: Corbin Hill Project in New York is a great example of a hub based on equity of access. They source from upstate and bring boxes of produce to the Bronx and Harlem. They have educational programs so the purchasers can go smoothly from purchaser to eater. It is subsidized.

- James: Another great example is Arcadia in DC. They have a mobile market that goes to 19 low-income locations. Aggregated products from 60-70 growers any given week. They have people that provide recipes on the spot. It turns out that's a great model. They set a great example on how to take advantage of the EBT and SNAP resources that bring the costs down. They're not year round. They are beginning to offer protein. A recent study was done on what needs to be done to reach a viable level for different numbers of stands.
- Audience Member: We need to strategically use subsidies without relying on it and taking it for advantage.
- Jeff: There are several food banks that are starting to expand to food hubs. Food Link New York also has a mobile market. It's an excellent new-ish frontier that can be leveraged.
- James: Harvesting Here in Chattanooga is fully owned by a food bank. Over production that's not selling is being shifted to the food bank.

Next Steps

- What is the perfect pie that we build? What trends do we see emerging? Will we survive and how? Who is we?

Session Two

Laura: The Future of Grocery Retailing and How Food Hubs Can Help

- Data from *Retail Revolution: Will Your Brick and Mortar Store Survive*
- "For the first time ever, in 2006 1% of American consumers did not set foot in a traditional supermarket."
- Industry Satisfaction Scores
 - Highest: Amazon
 - Lowest: Newspapers
- In grocery stores, the cash register sales are not providing the profit. Vendor allowances (promotional fees, stocking fees, etc.) make the profit. Because of this stores need to keep vendors happy. How can they keep customer service in focus in this environment?
 - *Retail Revolution* says grocery stores have 5 years to figure it out
- Factors:
 - ecommerce
 - Peapod: .9% of New England
 - Fresh Direct: 1.9% of NYC
 - Rising income inequality
 - Shrinking middle class

- In 1971, middle income made up 61% of supermarket sales. In 2011, they made up only 51%.
 - Shopping segmentation
 - Supermarkets are fighting over every segment
 - Average number of trips have decreased over the last few years
 - Supermarkets are gaining market share
 - Chasing the supercenter
 - Profit per square foot is going down.
- How does this look in Europe? What are future solutions for profitable retail?
 - Click and collect: order online and go to the store to pick it up.
 - Looking into small footprint locations.
 - 600 locations in 2010. 2,278 in 2013.
 - 20% of the population using it
 - 1.8% of France's retail market
 - ¾ of growth is from same-store sales
 - Automated future store
 - Fresh and ready-to-eat at the front of house. All dry goods in the back of house where they show up at the checkout.
 - Helps address the footprint problem, especially as urban growth continues.
- What does this mean for food hubs, and how can we help?
 - A place for improvement and increased sales is the perishable produce section. They need help. It's incredibly competitive.
 - A well-situated food hub can partner with retail. Bring in a good product, and work with staff to be knowledgeable.
 - The competitive market requires retailers to think more strategically than in the past.
- Question: If the retailer is not getting money from the customer, what's the motivation to get more local produce? What's the value proposition?
 - Laura: They can't keep doing what they're doing. ecommerce isn't going to solve the problem of profitability. Can we work together to find this solution.
 - Michael: Grocers have spent 30 years increasing efficiencies and reducing costs. Now they've realized that consumers can't tell stores apart. They aren't differentiated.
 - John: If they're going to beat the onliners, they have to increase customer satisfaction.
 - Brian: Aldi has made a concerted effort to focus on this, and they're up 3%

John: Recap of Yesterday

- From yesterday's data, what stuck out to you?
 - More food hubs now than two years ago
 - A little bit better profitability, but still a ways to go
 - Half the farms are relatively, or very, new
 - Opportunity for new and beginning farms

- Questions surrounding processing
- Question of low hanging fruit. Have we reached a ceiling? Is that national or just in Vermont?
- Institutional purchasing and selling to distributors. Will it continue? What's the role of food hubs in a scaled up system?

Discussion

In the entire supply chain, to what extent do the food hubs play next to the traditional system (broad line and secondary distributors)? Is it a take over one-way or another? Is it like the co-op movement where it's absorbed into the broad line system? Do both sides agree to co-exist?

And what does that look like? Is there a third option to totally take over the system?

- Abby: Overheard two national fish distributors talking about a smaller fish distributor using a more regional product and selling as a brand. As each other, what are we going to do about it? Acquisition.
- John: It's not food hubs for food hubs sake. It's a vehicle to an end. Keep the end in mind to position and operate. If it's not food hubs, what else is it? If integrating loses values, then there's the challenge of competing against the system. Challenge is to find profit without losing our values. What do we need to do around capital access to the extent that we can grow and keep our values? What policies need to change?
- Abby: Is it a win if Cisco adopts a mission driven profile? Maybe it's exactly the same as Red Tomato.
- Ann: What about smaller distributors such as Farm Mart? Is that a win? I personally think it is.
- Audience member: It's important to have this conversation, but is it premature since profitability isn't proven?
- Jeff: Is it too early to pull our hair out about this? Looking at a microcosm, any start up that doesn't have a vision for exit, is unlikely to exit properly. You're setting yourself up for a failure exit. Have a vision of where your going even if it's way down the line, helps you make the day-to-day and five-year decisions.
- Audience: I've never met any entrepreneur with an exit strategy.
- Michael: That's not true in high tech.
- Audience: Does success have to be the American capitalist definition?
- James: Cisco through their fresh point our acquiring regional distributors. They still have their autonomy. One of the issues at corporate, they can't force down such a decision. The danger that food hubs get co-opted is real. However, there is a possible future where food hubs are part of fresh point and still keep their values.
- Audience: I'm stunned we're talking about exit strategies. I'm still trying to understand what the value proposition of food hubs is. In regards to growth, what's the plan?
- Michael: We're not talking about exit strategy. It's a financial concept. All food hubs are value driven. We're talking about not getting eaten or killed. The Cisco metaphor is worth keeping alive in this conversation because it raises long-term questions. Given the structural existence of a Cisco in a US system, is it actually possible to retain value

autonomy. Cisco requires 4 things of distributors: gross sales, gross margins earned, brand commitment, and food safety.

- Kate: Given the six-year expanding regional food in the Northeast. Given the question of certain areas being saturated, is there any effort to find optimal locations. Is there any work to use optimization in terms of feasibility?
- James: I'm not a big fan of a lot of these optimization programs. These just aren't how businesses run. There are so many intangibles.
- Audience: Baldor did a huge re-imagining toward local. All these companies understand that there's something they need to do there. Helping customers understand what's real and what's not is the real challenging. We need to be really clear about the values we expect to see.
- John: In the spirit of alternate futures is food hub linkages. What's to say it's not going to be a web based linkage that creates an alternative future for regional food systems to decrease costs and hopefully redistribute wealth.
- Audience: I saw one study of optimization in that way, and it was really badly done. I think where that fails is, and what I've learned over the years, is the importance of first mile/last mile. The relationship they forge with the farmers and buyers. Those optimization models deal with the middle stuff, the least important things.
- Audience: I'm waiting to hear what we pick out what we learned from breakfast's nourishment. If we're talking about food hubs as an alternative model, how do we make sure that food hubs are not co-opted like co-ops? How are we going to bring fresh produce to, what are currently, urban food deserts?
- Michael: You build competitive products, or value chains. If you don't do that, then co-opting or going out of business are the only options. The consumer co-ops that were gobbled up were wholesalers.
- Audience: I agree I don't really like exit strategy. We're a young co-op and we need to figure out how to get to profitability. Do we set ourselves up for a position to be acquired? Is that what we want? We are a farmer-owned co-op. A group of producers don't necessarily know how to run the business end of this co-op. Cisco can be an opportunity. There's already this system out there that has proven to be efficient. We might not like everything about it but we can utilize what's already out there.
- Charlene: If you talk to Garry of Stony Field, one of the reasons he sold out was the slotting fees at brick and mortar stores. Maybe brick and mortar aren't the way we go. There needs to be an exploration of ecommerce opportunities.
- James: The fastest growing segment of food hubs is the ecommerce direct consumer delivery. One interesting avenue to explore is more of the ecommerce on the wholesale side. What does that look like? Typically that wholesale ends up at a brick and mortar store.
- Kathy: In terms of it being as simple as food hubs having to be competitive, can you
- Audience: I live in NYC. I work with low-income communities. We're looking at food hubs as a potential way to get food into these communities. I'm trying to figure out, at what point in your development does that food get into these low-income communities?

- James: There are generally speaking two types of food hubs. One is more geared toward generating revenue for producers. Higher margin market, so more revenue gets pushed backed down to the farmer. Focus on high-end restaurants. Within the wholesale producer benefits, they can tackle some institutional sales such as schools, but they're generally not making money on. The other model is an increased consumer access. Looking to bring, sometimes more expensive, local food into low-income communities through subsidized models. Is regional really the most important thing here? Don't we care more about getting fresh food to these communities? You can have the local-regional food producers, but it's a tough one. You have to be really innovative and really smart.
- Audience: Our group is trying to bring local food into NYC. Part of our model is that it has to be publically subsidized. In areas where is highly valued, there's no way to bring in regional food without it being highly subsidized. At the same time, we hope to bring it to restaurants and institutions.
- Kathy: Food hubs do have to be competitive whether they're producer or consumer oriented. What does it look like when a food hub is competitive? What can an uncompetitive food hub do to become competitive?
- Michael: There's about three or four answers. Basic requirements: right package, right quality standards (mostly as defined by USDA standards), cold-chain maintained, on-time delivery, volume, food safety certification, and traceability (with particular product code specifications such as PLU code). If you can't do those things, you're pretty much not at the table. So now go to the food hub talking about social and environmental goals. This is where it gets tricky, but also where there's opportunity. Need to make a clear value proposition to customers to be able to have a higher price. Red Tomato is accountable in both directions (the farmer and consumers). The farmer is part of the pricing equation. Price needs to be mutually satisfactory. We together need to be able to say our value proposition. Some of the largest players out there care about this. This is why companies are showing up at the sustainable food lab. They need the supply as sustainable product demand increases.
- Sara: What is the food hubs role in customer/consumers education?
- Audience: I'm surprised how capitalistically conservative this conversation is. The starting point of the conversation should be feeding people in a sustainable way, not profit and sales.
- Peter: Related to binary aspects: the consumer focused versus producer focused food hubs. They need to be competitive, but there needs to be subsidies. The subsidies are justified when you know you're being pulled in two different directions. One is to be under the bar of a safe, profitable company. The other is to meet the social values. Do subsidies need to be part of the on-going equation when the ultimate goal is to feed people? What about when the goal is to support producers? Is the goal to get away from ongoing subsidies? In a way a goal is to have adequate subsidies to meet the market place. I'm curious whether we need to be more explicit about the role of subsidies in *all* food hubs.

- Audience: One piece of the equation that hasn't been discussed is the labor piece. Especially when we talk about what food hubs look like at scale. The best food access strategy is a job. Food hub models in this current stage are fighting against these systemic problems. The market conditions are distorted. How can food hubs facilitate work force development through their labor activities?
- Abby: Trying to please both sides of the spectrum, farmers and producers, equally well is incredibly complex. It's not just buoying up the farmer, it's buoying up the concept of how to change our relationship with food. It isn't just about selling the product. It's about conversations. There are food hubs that are focused on moving product with a conscience. The starting point of aggregating farmer products is still the same.
- Jeff: The USDA subsidy of the commodity market is the cheapest way to do a subsidy. You're starting at the very beginning of the value chain, and the market is stable for decades. The food access subsidies are the most expensive way to do subsidies. You're at the very end of the value chain. And you're often talking about fresh product. I'd like to propose that maybe there's a way to solve that expensive subsidy problem and the problem of farm facing versus consumer-facing food hub. Is there a way to design a fresh food production subsidy that is somehow connected to delivering that food to low-income consumers? Are food hubs somehow a way of delivering that?
- Audience: There are some private not-for-profit models. One group delivers some of the CSA's to low-income recipients. They're subsidizing it. These models are really patchwork.
- Ann: This is an example of the expensive subsidy.
- David: 70% of USDA's budget is the expensive subsidy through nutrition programs.
- Audience: It's great to subsidize farmers at their farm. It will take many years of farmers making a profit to cover the basic costs. We need to look to local and state subsidy to help build these food hubs geared to low-income communities.
- Audience: Can scale be a solution in that it cheapens food access and supports farmers simultaneously? Does scale allow you to get to a price point where you can do both? In general, how do the models we're building move us into a system where we don't need subsidies in the future? If we don't have a model that's doing that and we need annual subsidies, are we doing something sustainable and worthwhile?
- John: Before the name food hub even existed, the goal was business survival. When we talk about low-income communities, we're talking about market failure. Therefore market programs aren't going to solve the program. Subsidies are part of the game in these communities. The scale is an important factor. There are pros and cons. Good Nature Family Farms out of Kansas City, they do \$4-6 million per year across 60-80 farms. They did this across high-income markets. They can use this successful model to branch out to food access. Their food access work is subsidized by their other success and some grants.
- Lindsey: Biodiversity is important for our survival, business survival is important for ourselves... Eventually we came to realize that we also had to interact with existing businesses to survive. You need to have diversity in markets to survive. You can have

both high-income markets and food access markets at the same time. The biodiversity is important.

- Michael: Maybe more important is the scale of the growers that are supplying the food hub. So much of this work was begun by working with retail growers and new growers and still bearing enormous burden of their capital expenditure. Wholesale mid-size growers are the key to delivering competitive product at all let alone urban markets.
- Jim: Do we lose democracy and self-management when we join this possible Cisco market? I see a future of food hubs that are in a network that are mutually managed.

Main Ideas

- Viability of food hubs
- Producer-focused food hubs compared to food access-focused food hubs
- Saturation of “low hanging fruit” market
- The role of subsidies: commodity vs. consumer. Institutional vs. governmental.