Values-based food supply chains: Home Grown Wisconsin Co-op

G.W. Stevenson, UW-Madison Center for Integrated Agricultural Systems

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This series of case studies examines values-based food supply chains—strategic business alliances formed between primarily midsized farms/ranches and their supply chain partners—to distribute significant volumes of high-quality, differentiated food products and share the rewards equitably. Farmers and ranchers function as strategic partners rather than easily replaced input suppliers. All participants in these business alliances recognize that creating maximum value for the product depends on significant interdependence, collaboration and mutual support. These supply chains attach importance to both the values embedded in the production of the food products AND the values that characterize the business relationships.[1]

Historical development

Introduction. Home Grown Wisconsin was a cooperative, multi-farm wholesale and Community Supported Agriculture (CSA) food business founded in 1996 in south central Wisconsin. Home Grown Wisconsin successfully sold fresh produce to upscale restaurants and CSA customers in the Chicago area for more than 10 years. In 2009, after being significantly impacted by floods, a downturn in the economy and mounting overhead costs, the cooperative tried to shift to a 100 percent CSA business model. Unable to subscribe sufficient CSA members in the Chicago area that year, they could not cash flow the enterprise. In the spring of 2009, Home Grown Wisconsin closed its business operations and transferred its assets to a newly formed business that folded after several years of operation. The core farmers of Home Grown Wisconsin continue to farm and market their products, and several of them have been quite successful.

Home Grown Wisconsin was a cooperative, multifarm wholesale and Community Supported Agriculture food business

While this case does not provide detailed information about the logistics and economics of Home Grown Wisconsin, it does illustrate some of the opportunities and challenges, internal and external, confronted by a small-scale, farmer-owned marketing cooperative.

Strategic and philosophical goals. Home Grown Wisconsin's primary goal was to expand the market for fresh, local, organic produce. They accomplished this by distributing high-quality vegetables and fruit that conveyed the variety and value of Wisconsin's

[1] *Values-Based Food Supply Chains: Strategies for Agri-Food Enterprises-of-the-Middle* explains the terminology and general characteristics of values-based food supply chains: <www.agofthemiddle.org>.

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harvest. Home Grown Wisconsin was created as a result of research carried out by the University of Wisconsin Center for Cooperatives (UWCC) and Center for Integrated Agricultural Systems (CIAS). During interviews and meetings, food buyers indicated that purchasing from regional farms would be easier if it could be accomplished with one phone call, one availability list, one invoice, standard delivery days and professional service. In response to these signals, the Home Grown Wisconsin cooperative was created to link growers and restaurant chefs with consolidated ordering and delivery.

Another important goal of the cooperative was to attain a good price for growers. Home Grown Wisconsin set up an allocation and pricing system in which experienced growers set the prices for products based on their production costs and desired profit margins. (See page 3 for details.) To help protect markets and prices, Home Grown Wisconsin members were required to sell products to existing Home Grown Wisconsin customers through the co-op. Members were only allowed to sell directly to existing customers if they were marketing an item that the co-op did not normally sell.

Customer base and products. Home Grown Wisconsin began by selling to restaurants in Madison, Wisconsin, its logistical base of operations. This market soon proved too small. In addition, although chefs in Madison had said they would prefer a single contact for sourcing produce, in practice the chefs preferred communicating directly with growers and were resistant to price increases necessitated by having an intermediary in the supply chain. By 2003, the co-op's primary customers were upscale Chicago restaurants, with additional sales to Madison and Milwaukee restaurants. Home Grown Wisconsin also sold to colleges and retail stores. For a short time, the co-op sold produce through a grower's stand at a Chicago farmers' market. In 2005, Home Grown Wisconsin started a CSA enterprise in the Chicago area.

During its peak years between 2003 and 2006, Home Grown Wisconsin sold an array of vegetables, herbs and edible flowers, offering more than 150 items during the high season. The co-op also sold berries, apples, cider, cheese, mushrooms and eggs. Specialty vegetables, greens, root crops and tomatoes dominated sales. In the early years of the co-op, all growers were supposed to follow organic practices but did not need to be certified. Shortly after the USDA National Organic Program was implemented in 2002, all growers were required to obtain organic certification.

Organization, logistics and sales. Home Grown Wisconsin was a closed cooperative. New members needed an invitation to join and were accepted after a vote by a board of directors representing the co-op's membership. During the peak years, more than 25 growers sold produce through Home Grown Wisconsin, though most sales were associated with eight to 10 farms. Farms ranged in size from small market gardens under an acre to farms with more than 50 acres in vegetables.

The Home Grown Wisconsin board of directors was composed of seven people: five co-op members (farmers) and two non-members who served in an advisory capacity and could not vote. Until 2003, the co-op employed only a general manager, who handled all management, marketing and accounting. From 2003 to 2006, they hired additional staff to help with accounting/logistics coordination, truck driving, warehouse work, CSA coordination and sales. By 2003, the co-op rented a dock, warehouse space and a truck, further increasing overhead costs.

Tomatoes, specialty vegetables, greens and root crops dominated Home Grown Wisconsin sales.

Home Grown Wisconsin delivered fresh produce to Chicago restaurants twice a week during the growing season and once a week during the winter. Growers sent product availability lists to the co-op's general manager. These were compiled and faxed or e-mailed to customers, who then placed orders. Growers had one and a half days to pick, pack, cool and deliver their orders to the Madison warehouse. Growers maintained ownership of their products until sold; if a batch of carrots was rejected by a chef, for example, the grower took the loss.

The co-op distributed sales through an allocation system in which co-op members were prioritized as "A" or "B" growers for specific products. When the co-op launched, farmers received priority status based on their history and capacity for growing high quality products. "A" growers were given the first opportunity to fill the order, followed by "B" growers. Farmers who were not members of the co-op could sell items through the co-op if no "A" or "B" growers had that item or if sales exceeded what priority growers could provide. Growers maintained their priority status based on their history and success of supplying quality product. The co-op's board of directors and managers annually reviewed the priority allocations as well as the quantity of food products projected for the coming year.

Priority growers set prices based on their experience, production costs and required profit margins. The co-op manager could suggest a price change if the proposed price seemed extraordinarily high or low. If two or more priority growers offered the same product at different prices, the lower price prevailed. Deliberate "dumping" of low-priced items was limited. Most Home Grown Wisconsin prices paid to co-op farmers fell at the high end of organic wholesale prices.

Home Grown Wisconsin sales grew from about $12,000 in 1996 to about $300,000 in 2002 to $757,000 in 2008.[2] Sales for the first several years were mainly during the growing season. In 2003, the

[2]Sales figures from John Hendrickson, former Home Grown Wisconsin secretary, and Jenny Bonde, former treasurer.

co-op introduced year-round sales with storage crops, hoop-house greens and frozen tomatoes offered through the winter. Home Grown Wisconsin marked up produce 50 percent to cover overhead expenses such as trucking, labor, marketing and rent. If a grower offered a case of tomatoes for $20, the restaurant paid $30. A 50 percent mark-up generated a 33 percent gross profit margin, an acceptable rate for Home Grown Wisconsin in its formative years.[3]

Home Grown Wisconsin held farm tours for chefs each summer, and member farmers attended kitchen tours in restaurants each winter.

Historical dynamics

Enterprise dynamics (1996-2006). These were strong years for Home Grown Wisconsin. Founded on an understanding that the enterprise could meet the needs of both farmers and restaurants, the co-op succeeded for 10 years without outside grants. During this time, it also benefitted from very low expenses.

Home Grown Wisconsin provided good prices for farmers and high quality local produce for restaurants. A stable base of eight to 10 farms consistently sold product through the co-op. In 2005, the Chicago-based CSA created a new income stream and stretched cash flow. This resulted in a period of predictable prices and stable, personal business relationships. Home Grown Wisconsin held farm tours for chefs each summer, and member farmers attended kitchen tours in restaurants each winter.

For the most part, Home Grown Wisconsin board members and managers provided high-quality leadership. The Home Grown Wisconsin Board of Directors was made up of farmers selected from the co-op's membership, plus advisory members from the UW-Madison and other organizations. The board reviewed policy and set the manager's salary. While the board initially had a strong hands-on role, over time the board members reduced their direct involvement, placing more responsibility on staff.

The following enterprise dynamics that developed in Home Grown Wisconsin's early years presented major challenges and barriers when the co-op faced new realities in 2007-2009:

> ***Overall enterprise economics.*** While Home Grown Wisconsin succeeded in getting high prices for its farmer members, the co-op did not perform as well in terms of the overall economics of the enterprise. Its two main problems were overall profitability and uneven cash flow. First, Home Grown Wisconsin set insufficient business margins. Its 50 percent mark-up for the restaurant trade translated into a 33 percent margin (Jenny Bonde, interview, 3/17/11), which was sufficient in the co-op's early years when costs were low. But these margins became increasingly insufficient when overhead costs rose beginning in 2003-2004 (Jenny Bonde, interview, 3/17/11). By comparison,

[3]All remaining statistics for the case study were provided by Jenny Bonde.

successful commercial food distribution enterprises run on margins of 26 to 28 percent, based on volumes and efficiencies far greater than Home Grown Wisconsin's.

In addition, maintaining the 33 percent gross margin on restaurant sales was difficult from year to year. In reality, the co-op averaged about a 31 percent gross margin on restaurant sales. The CSA margin was better—generally 33 to 35 percent. However, Home Grown Wisconsin's gross margin in its final year of operation (2008) was just 30.44 percent, including CSA sales. This margin resulted from two issues: 1) the Home Grown Wisconsin manager gave discounts to certain restaurant customers to increase sales and 2) the cost of produce purchased from co-op members for the CSA was higher than anticipated.

Uneven cash flow throughout the year presented another impediment to overall economic success at Home Grown Wisconsin. The bulk of the restaurant sales occurred from June to November, leaving major time periods with little or no active income streams. Cash flow was a particular problem in the early spring, prior to the onset of restaurant sales. Home Grown Wisconsin tried to address this in 2005 by adding the CSA, as CSA members pre-pay for their shares in the late winter or early spring. While the CSA income helped, the co-op was unable to recruit enough members to substantially address the cash flow dilemma. At its peak in 2008 with 440 full-share equivalents, the CSA accounted for $328,000 of the co-op's $757,000 total sales.

Farmer members priced produce themselves, and were prioritized as suppliers for specific products.

Increases in overhead costs. When it began in 1996, Home Grown Wisconsin's overhead costs were extremely low. A part-time manager was responsible for taking orders, making deliveries and recordkeeping. Produce was consolidated at a centrally located co-op member's farm, rent-free, and delivered in contracted trucks or growers' vehicles. A fax machine was the co-op's only capital equipment.

But growing costs hurt Home Grown Wisconsin's bottom line. By the time the last manager was hired in 2005, the enterprise's staff included a full-time manager, a salesperson, a CSA coordinator, a dock assistant and a truck driver. Personnel expenses grew from $97,000 in 2006 to $138,000 in 2008, although these salaries were not high by industry standards. Staff turnover became an issue. (The co-op had some outstanding managers and some poor managers at the helm during these years.)

Additional overhead costs included rental of warehouse and dock space, purchase of walk-in coolers and the purchase, then lease, of a truck. Transporting product to Chicago was an ongoing challenge for the co-op. In the early and middle years, Home Grown Wisconsin purchased a used truck, but it repeat-

Many board members found that their growing farms left them little extra time to deal with co-op issues.

edly broke down. The co-op later paid a high price to lease a truck that was only on the road for two days a week during the growing season and one day during the winter. Due in part to record-high fuel costs in 2007-2008, trucking expenses grew from $38,000 in 2006 to $66,000 in 2008.

Pricing system. Home Grown Wisconsin's pricing system certainly benefited the co-op's farmer members. However, one board member noted that prices were high and reflective of a pricing system that was resistant to discipline from the market (Steve Pincus, interview, 3/4/11). Two aspects of the pricing system were at odds with the market: First, the larger growers with priority status typically set the prices. There was little incentive for others to offer lower prices because of the allocation system. Second, the co-op's managers and sales staff were not empowered to negotiate prices with customers, nor did the co-op's board and farmer members request realistic price and market information. This was due to the fact that, in its early years, Home Grown Wisconsin was able to receive above-market prices set by farmers. This institutionalized resistance to the market's signals impacted Home Grown Wisconsin's resilience during 2007-2009. During this time, the cooperative faced increasing price pressures from competing farmers while the recession cut into restaurants' purchasing abilities (see "The recession of 2008," page 7).

Board functionality. Given turnover in the co-op's staff, the Home Grown Wisconsin board needed to be highly functional. For the most part, this was the case. The burden of board responsibility fell on a few stalwarts who held board positions year after year. Many board members were at a stage of life in which growing farm businesses and young families precluded them from committing extra hours, so board member burnout became an issue. As one board member put it, "We just wanted to turn the co-op's business over to a good manager." (Steve Pincus, interview, 3/4/11). A lack of commitment and communication within the enterprise and between Home Grown Wisconsin's board and staff had consequences in 2008. The board did not receive a clear picture of the co-op's degraded economic situation.

Enterprise dynamics (2007-2009). During this period, multiple factors forced Home Grown Wisconsin to close and transfer ownership of the enterprise. Many of the issues internal to the co-op had been building for several years and are reviewed above. However, two external forces also contributed to the troubles:

100-year floods. In both 2007 and 2008, record flooding in southern Wisconsin destroyed significant amounts of the co-op farmers' produce. Because of Home Grown Wisconsin's internally oriented sourcing system, the co-op was not well-positioned to source produce on an emergency basis from growers outside the cooperative. For two years, Home Grown Wisconsin had a significant shortage of product for its customers. This was particularly disheartening because the co-op finally had adequate infrastructure to move considerably more product. Supply shortages hurt the co-op's already precarious cash flow and overall profitability. Its shorted restaurant customers found other regional organic producers who had recently entered the Chicago market and were selling at lower prices than Home Grown Wisconsin. Reducing or losing these accounts further impacted the co-op's economic picture. For instance, the second year of floods coupled with the 2008 recession resulted in an 11 percent decrease of restaurant sales compared to 2007 (Jenny Bonde, email, 3/3/12).

Although CSA sales goals were met for the 2008 season, CSA expenses were grossly over budget. Cost of goods exceeded the budget by $20,000. Packaging and other expenses were significantly higher than expected.

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With both restaurant and CSA operations, the co-op could not trim personnel expenses to reflect actual sales. There were also fixed costs and a number of unexpected and unavoidable expenses in 2008, such as a high fuel costs and product loss. By year's end, 2008 sales were $170,000 lower than anticipated, yet total expenses exceeded the budget.

The recession of 2008. The restaurant sector is very sensitive to economic downturns, and Chicago-area restaurants were not immune in 2008. First, the co-op lost restaurant business to competitors who sold at lower prices. As noted above, Home Grown Wisconsin managers and sales persons did not have the authority to negotiate prices with restaurants, which put them at a competitive disadvantage in the 2008 market. Second, facing cash flow problems of their own, restaurants did not pay Home Grown Wisconsin invoices on time. It should be noted that some restaurants were notoriously late in paying invoices even during better years with farmers accepting very late payments during the winter months from 1999 to 2006.

In the context of flooding and the recession, Home Grown Wisconsin was feeling the financial hurt in 2008. By the end of that year, the overall margin on restaurant sales was only 28.5 percent. Growers were not paid for months. Eventual payments to growers and other operating expenses were increasingly paid from the co-op's capital fund, a practice that had begun several years earlier.

The co-op also faced management challenges during this time. The business manager for restaurants was terminated during the summer of 2008. The general manager assumed that role while continuing to manage the co-op as well as the finances/accounting, which suffered from lack of attention. During much of 2008, the Home Grown Wisconsin board of directors did not have a clear picture of the co-op's troubled finances. For instance, the co-op's net profit for 2007 was -$14,000, but it was reported to the board as -$2,000. Even more divergent, Home Grown Wisconsin's net profit for 2008 was -$44,000 but reported to the board as -$27,000.

During much of 2008, the Home Grown Wisconsin board of directors did not have a clear picture of the co-op's troubled finances.

Winter 2008 and spring 2009. Through collaborative work by the co-op's manager and treasurer, the true picture of Home Grown Wisconsin's degraded economics became clear during the winter of 2008. After reviewing an analysis that pointed to the increasingly competitive restaurant market in Chicago, Home Grown Wisconsin's board proposed shifting the co-op's business model to 100 percent CSA, keeping the geographical focus on Chicago. The board wanted to develop the growing CSA business begun in 2005 based on the perceived CSA market opportunities in the Chicago area. CSA business margins are easier to determine and predict than restaurant sales margins (Jenny Bonde, interview, 3/17/11).

Using the co-op's newly understood financials, the board determined that a workable budget for the proposed CSA enterprise would require selling 700 member shares. After a CSA recruiting effort during the winter of 2008/2009 produced only 450 customer shares, the board decided in the spring of 2009 to terminate the Home Grown Wisconsin business enterprise and transfer the company's assets, debts, customer and farmer bases to a private food distribution company.

In retrospect: Thoughts on administration and organization from Home Grown Wisconsin members.[4] By about 2004, staff were spending an inordinate amount of time on bookkeeping and accounting tasks that could have been handled by an automated software system. Staff spent an enormous amount of labor on these tasks. They used QuickBooks for invoicing, but sorted crop orders to farmers by hand—a tediously slow process. They often oversold items and didn't realize it until orders were sorted, resulting in miscommunication between the farmer, manager and restaurant. An inventory system would have cost about $18,000 at the time but would have freed countless hours for staff and prevented burnout.

Some members also thought they should have separated the sales/management duties from bookkeeping. Given the clumsy order-taking/allocation/billing system, it was easier for the salesperson to be the bookkeeper. However, it wasn't reasonable to expect staff to

[4]Comments in this section from Home Grown Wisconsin members were culled from email sent to Steve Stevenson by former treasurer Jenny Bonde and former secretary John Hendrickson, April 2011.

successfully juggle two or three positions. Members said the board should have insisted on a separate bookkeeper (even though the employee doing multiple tasks did not think it necessary). Members would also have liked to have hired an outside firm to perform a quarterly review of the books.

Some members suggested the co-op should have allowed the sales manager more flexibility in setting prices. The manager could have contracted with growers during the winter for certain prices and allowed a 10 percent variation.

Finally, members would have liked to have consulted with retired business professionals, small business development agencies or other organizations every six months or so. Having a board member from the University of Wisconsin Center for Co-ops was invaluable, but in retrospect, members said the board should have worked harder to gain more outside perspective. They said it often felt as though farmers were attempting to run a second, separate and complex business that was outside their areas of expertise.

Summary observations

- Home Grown Wisconsin's original business model based on selling high quality, organic food products to urban restaurants and CSA customers was sound, as long as the business kept overhead modest and maintained margins, as it did during its successful first years.
- As margins decreased and overhead costs rose significantly, the business tapped the growers' equity fund to cash-flow the enterprise. This short-term strategy enabled the co-op to extend the period during which it could operate at a loss.
- Home Grown Wisconsin's pricing system, which was based on securing high and stable prices for growers, worked well in the early years, but it greatly reduced the staff's negotiating capacity. This was particularly damaging during the recession and times of increased price competition from other farmer suppliers.
- Home Grown Wisconsin's leadership did not know the extent of the co-op's troubled finances due to inadequate accounting and lack of communication on the part of staff during the co-op's final years.
- The benefits of the cooperative structure, including farmer ownership and direct decision-making, also involve challenges and costs, including stiff demands on growers' time and energy when they are already attempting to manage their own unique businesses.

Policy note

John Hendrickson, former Home Grown Wisconsin secretary and grower, and UW-Madison Center for Integrated Agricultural Systems staff member who helped launch the co-op, reports that he and other members of Home Grown Wisconsin made some use of federal programs, including the Conservation Reserve Program, farmers' markets programs and a USDA Sustainable Agriculture Research and Education grant used to develop a report on the economics of vegetable production at different scales (John Hendrickson, interview, 4/3/12).

John procured cost-share dollars for organic certification for his farm and assumes other growers did as well.

At the state level, the Wisconsin Agricultural Development and Diversification Program funded a project to conduct food safety education and cost-share on Good Agriculture Practices (GAP) certification for a group of farmers including Home Grown Wisconsin growers. The Home Grown Wisconsin Advisory Board included staff from the UW-Madison including personnel from the Center for Cooperatives and John Hendrickson, and several UW Extension agents did some of the GAP training.

Home Grown Wisconsin did not use local county or city programs. They did have a line of credit with Badgerland Financial, which is part of the nationwide Farm Credit System.

The federal organic standards rule posed a problem for Home Grown Wisconsin. When the business started, the National Organic Program did not exist. There was much discussion and debate about certification, and Home Grown Wisconsin leadership ultimately decided to require that all members be moving towards certification. Eventually many members were certified. Most members commented on the proposed organic rule in 2000. More recently, after the co-op dissolved, a number of members responded to the proposed legislation that became the Food Safety and Modernization Act.

Food safety was a great challenge for the growers, and John would like to see a Food Safety Incentive Program established to provide cost-share funds for small vegetable producers to improve food safety practices in washing and packing operations.

Finally, John strongly believes that the development of new enterprises like Home Grown Wisconsin is central to building local food systems, but there are many challenges. Farmers and other food supply chain participants need technical assistance and advice, which have been sorely lacking. He believes more energy and funding should be funneled in to this area.

Credits

Jenny Bonde, John Hendrickson and Steve Pincus provided the primary interviews upon which this case study and the policy note are based. The policy note was authored by Kate Clancy, University of Minnesota Institute for Sustainable Agriculture.

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Organizations involved with this report:

The National Initiative on Agriculture of the Middle is concerned with a disappearing sector of midscale farms/ranches and related agrifood enterprises that are unable to successfully market bulk commodities or sell food directly to consumers. See www.agofthemiddle.org. The initiative has three areas of emphasis: new business and marketing strategies; public policy changes ; and research and education support.

The Center for Integrated Agricultural Systems (CIAS) is a research center for sustainable agriculture in the College of Agricultural and Life Sciences, University of Wisconsin-Madison. CIAS fosters multidisciplinary inquiry and supports a range of research, curriculum and program development projects. It brings together university faculty, farmers, policy makers and others to study relationships between farming practices, farm profitability, the environment and rural vitality. For more information, visit www.cias.wisc.edu or call 608-262-5200.

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