Revised August 2016 Agdex 845-24

Pricing: Moving from Farmers' Market to Retail Sales

You have been selling your product at a farmers' market and have earned a loyal following. Your customers are enthusiastic, and you think your product could do well in a larger market. Moving beyond the farmers' market to a retail setting can be a natural next step in the evolution of your product.

Moving to retail

This factsheet explores three issues to consider in evaluating a move from a farmers' market to retail:

1. Do you really want to grow bigger?
2. What are your retail options and how do these affect your costs and pricing?
3. How do you calculate costs and ensure profitability for your product?

1. Do you really want to grow bigger?

If you have been successfully selling at a farmers' market, congratulations! While farmers' markets may be viewed as a stepping stone to bigger opportunities, many producers never leave the farmers' market environment because it offers so many advantages for farm-direct foods or value-added products.

Consider the following advantages:

- you have direct contact with your customer and can build strong, lasting relationships
- you represent your own product, rather than relying on someone else in a retail setting who may not know it as well
- you can often ask a higher price than the same product could command in a retail setting
- you get paid on the spot, without waiting weeks (or months) to get paid
- your supply chain is simpler, without distributors and brokers
- your marketing costs are lower because simple packaging fits the farmers' market sensibility and meets regulatory requirements
- your profit may be higher than you could achieve in a retail setting
- you can inexpensively test new products and get direct feedback from customers

> *Carefully evaluate if you want to move from a farmers' market to retail sales.*

If you have considered these advantages, but still see the potential for a wider market for your product, here is some help. The next steps explore different options for selling your product outside a farmers' market.

2. What are your retail options and how do these affect your costs and pricing?

Every year, over 12,000 new food products are introduced to consumers, and over 98 per cent fail to sell enough within the first year to become a sustainable product. Ensuring your costs and profits are built into your pricing structure will help your product succeed.

Your product could be sold in a wide variety of retail operations from small, local stores to large, national retail chains. Despite the differences in these operations, these businesses have one thing in common: like any other business, they exist to make a profit.

When you sell your product at a farmers' market, the price the customer pays is your revenue. When you sell to a retailer, or through a broker, they will keep a percentage of the retail price. Thus, your profitability will be determined not by the price a customer pays the retailer, but by the wholesale price the retailer pays you.

Selling into larger markets involves more players and more logistics – labelling, distribution, warehousing – all of which can add to your upfront costs.

You will need sufficient financial resources to pay for items required for the retail market, a few of which are listed here:

- cost to design and print professional bilingual labels with a UPC product barcode, nutritional information and ingredient listing
- product analysis for nutritional breakdown
- product registration fees (UPC, etc.)
- food safety certification, equipment and/or software
- inventory management software
- transportation to store or wholesaler
- warehousing or storage, if applicable
- listing fees for shelf space in larger retailers
- broker or distributor fees, if applicable
- proper "hold harmless" and recall insurance levels retailers require

Starting small: leveraging local contacts

A great way to move into the retail market is to start close to home. You may know smaller, local retailers or can ask your farmers' market customers where else they shop.

Think outside the grocery market and consider bakeries, coffee shops, butcher shops and gift stores. For example, an established Edmonton bakery has a retail section inside their store that stocks many specialty jams, jellies, cheeses and condiments that can be eaten with their baked goods.

If a local retailer likes your product and believes they can sell it at a profit, your product could be on the shelf quickly. Small, local stores are an excellent introduction to the retail industry, but the long-term challenge is volume: can the retailer sell enough of your product to give you a decent profit?

Other considerations for producers as they move into this market include the following:

- each retailer may have a different payment structure; ask them what their payments terms are
- in a local market, you will likely be responsible for delivering the product to the store, and you will need to ensure safe food handling regulations are met when delivering products (including transporting in a covered vehicle, proper temperature control during transportation, etc.)
- retailers will not have on-site storage and do not carry excess inventory, so you may need to arrange storage for your inventory
- to track your inventory in multiple stores, you may need to invest in software for this purpose
- inquire about re-stocking turnaround times at the store – the time period may be only a few days
- now that you are not selling directly to the end consumer, your brand position may need re-working ("cooked with love" may not be enough if the customer does not get to meet you in person)

Smaller chains: pros and cons of multiple-location retailers

In Alberta, there are a number of smaller, independent grocery retailers who could be the perfect fit for a producer or processor entering the retail market. These retailers include Sunterra, Planet Organic, Community Natural Foods, Nutters, Calgary Co-op, etc.

Several benefits can result from selling through these smaller chains. You get access to more consumers, the distribution system can be well established and some retailers may market your product for you. Managers in these smaller chains may have more control over what is in their store than store managers at the big-chain retailers and may support local producers enthusiastically. They may ask you to demonstrate your product in-store. Tasting events can give you direct customer feedback and build interest, but will create costs for time and travel.

The challenge in selling to retailers is that you may need to rely on other companies to get your product into the stores – such as brokers, distributors and transportation companies. Their fees add cost to your product. If you only sell through wholesalers, you also lose direct contact with your customers. And, of course, you may need to invest in equipment that helps you produce a higher volume of product.

Larger retail chain stores: dreaming big

Do you dream of seeing your product on the shelves of a major retail grocery chain like Loblaw's Superstore, Sobeys or Overwaitea Food Group's Save-On-Foods? These retailers are built to sell in large volumes – and that fact can be challenging for agricultural producers or small processors.

Some larger grocery chains offer opportunities to local producers and processors, but this situation is usually the exception rather than the rule. More often, you will be dealing with a corporate head office to get in the door.

Assuming you make it, they may ask you to supply their entire chain, their provincial district or their specified distribution service area. That result means ensuring a consistent supply, providing transportation options, warehousing, having a strong professional image (product packaging and branding) and a comprehensive marketing plan on how you are going to promote your products within the retail chain.

Sometimes, chains charge you a listing fee to secure a spot on the shelf, which covers their costs if your product does not sell. This fee can be in the thousands of dollars for a single product. Even with this fee, there is no guarantee. If your product is not selling, it will be sent back to you (without a refund of the listing fee).

Be sure to ask about the payment structure. Some retailers pay quickly (for example, within 15 days of the invoice date), but they take 2 per cent off the invoice amount for these payment terms.

Other possibilities: thinking outside the box

While this factsheet deals primarily with brick-and-mortar stores, many producers and small processors have successfully found other markets for their products.

One idea is to market your product as a fundraising venture to local organizations such as hockey teams, school music programs, gymnastics clubs, figure skating teams and so on. This approach can be an effective way to get your product into more consumers' hands. An added benefit is that your customer orders and pays up front, so you know your exact inventory before production begins.

Another idea is to sell your products to a home delivery grocery business. These businesses offer a variety of products to their customers and deliver their orders directly to customer homes.

3. How do you calculate costs and ensure profitability for your product?

Setting a price for your product can be difficult. In fact, pricing a product too low is one of the most common mistakes food processors make. Your price must cover all your costs – even your time and business costs not directly related to the product – and generate a profit that sustains your business.

Cost of production: all costs associated with producing the product:

Cost of production = variable costs + fixed costs

Variable costs:

These costs include (but are not limited to) the following:

- raw ingredients
- processing expenses or fees for co-packers
- packaging costs such as boxes, bags, labels
- shipping and/or transportation
- labour (include you and family members)
- broker fees
- listing fees
- marketing costs (advertising, price lists, recipe cards, onsite demonstrations)

Fixed Costs:

These costs include (but are not limited to) the following:

- land and equipment expenses
- operating interest
- utilities
- management salaries
- office supplies
- professional fees (accounting)
- depreciation (building, machinery)
- warehouse (storage) costs

Understanding your break-even point

A break-even point is a standard calculation in business used to discover the point where costs are covered by a certain price and volume. The break-even point is the price at which there is neither a loss nor a profit from the sale of your product.

For this break-even example, you will need to know the cost to produce 1 unit of product (variable costs) plus what your monthly business costs are (fixed costs). Keep in mind, this example is intended to show the process, and your numbers will vary depending on the type of product you offer and your own costs.

Break-even Scenario

Marv's Salsa Company produces 400-gram jars of salsa and has found a wholesaler who wants this product. Marv has added up all his costs related to one jar of salsa (variable costs) and found it to be $2.50 per unit.

He wants to set his wholesale price for one 400-gram jar of salsa at $4.00 and wonders how many units he will need to sell to cover his costs and break even.

He will subtract his costs per unit from his selling price to see how much 1 unit will contribute towards covering his fixed costs.

Unit contribution = $4.00 - $2.50 = $1.50 per jar

So, each jar of salsa contributes $1.50 towards covering Marv's fixed costs.

Marv's Salsa Company's total monthly fixed cost is $2,025 for the salsa operation.

To break even (have no profit), but cover all his monthly costs (variable + fixed costs) by selling the jars at $4.00 each, Marv's Salsa Company must sell 1,350 jars of salsa each month.

Break-even analysis can also help you analyze how a different wholesale price affects your business. Using the same example, Marv's Salsa Company decides to sell the salsa to the wholesaler for a higher price of $4.75 each. Here is what happens to the number of jars of salsa he must sell to cover the same costs and break even:

> Unit contribution = $4.75 – $2.50 = $2.25 per jar goes towards covering Marv's Salsa Company's monthly fixed costs.
>
> Marv's Salsa Company's total monthly cost is $2,025 for the salsa operation.
>
> Break-even in units = $2,025 / $2.25
= 900 jars of salsa

A wholesale price of $0.75 more per jar means Marv can sell 450 fewer jars (1,350 – 900) per month and still break even, compared to selling at a lower price of $4.00 per jar.

You can use break-even analysis before you plan for a new food product or decide on a new price to be sure you can generate enough income to cover the costs of your business.

How do I calculate my profit goals?

Covering your costs is a critical starting point. Making sure you earn enough profit to ensure your business thrives is the next important step.

You can set your profit goals as a percentage above the cost of the product, or you can set a total profit amount for the entire business. Make sure you are familiar with the product price range in your industry, so your profit goal is suitable for your product. You will need to balance your profit goals with a price that consumers see value in.

A note about retail margins

You may hear retailers talk about their "margin." Profit margins are usually expressed as a percentage and will vary from category to category (typically, bulk items have a 40 per cent margin while bakery products have a 60 per cent margin because of their high shrink rate and short shelf life/perishability).

Margins can also vary from store to store. Retailers often experiment with margins using a complex system of shelf placement, pricing, promotions and discounting to achieve an overall gross margin goal.

For these reasons, calculating your profit goals using retail margins can be like trying to hit a moving target. Rather than calculating your price based on the margin the retailer hopes to get after they sell the product, it is better to take control and offer a firm price to the wholesaler or retailer – a price that is also profitable for you.

You cannot control what the retailer charges the consumer for your goods; retailers are constantly dealing with what the market will bear and is willing to pay. If you continue to sell the same products at the farmers' market, you want the retail price to the consumer to be the same or as close as possible to the price you set at the farmers' market. A large price discrepancy between the two may mean you are missing something in your product pricing or you may not be charging enough for your products at the farmers' market.

Making the leap

Many businesses in Alberta have made a successful transition from farmers' markets to retail sales. There is no one formula for success, and each business will have to address its unique challenges and opportunities before going in this direction.

It is best to move slowly, and make sure you are well informed. As long as your decision is based on a knowledgeable calculation of all your costs, a thorough understanding of the logistics involved and a healthy target profit, you will be well-positioned for growth and success.

This factsheet is an introduction to pricing your product for the retail market. More information on pricing strategies by agricultural segment is available on the Alberta Agriculture and Forestry (AF) website or through AF publications such as the free factsheets *Essentials of Pricing* (Agdex 845-1), *Methods to Price Your Products* (Agdex 845-2), *Pricing Processed Food Products* (Agdex 845-3), *Pricing Horticulture Products* (Agdex 845-4) and *Pricing Meat Products* (Agdex 845-25) available in on the web or in hard copy. Visit the AF website at www.agriculture.alberta.ca.

Prepared by Alberta Agriculture and Forestry

More information, contact:
Alberta Ag-Info Centre
Call toll free: 310-FARM (3276)
Website: www.agriculture.alberta.ca

08/16

The development of this factsheet was supported in part by *Growing Forward 2*, a federal-provincial-territorial initiative.