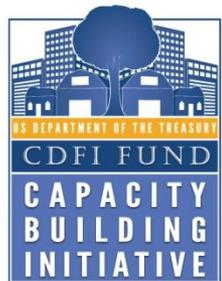




# Underwriting Natural Food Cooperatives

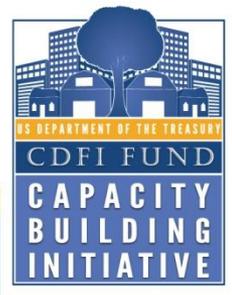
Margaret Lund

April 11, 2012



# Introduction

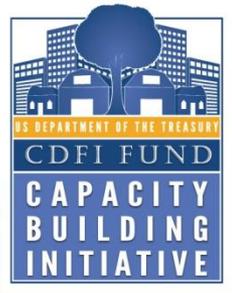
- CDFI Fund's Capacity Building Initiative
  - Financing Healthy Food Options
    - Workshops
    - Technical Assistance – individual and group
    - Resource Bank



# Today's Webinar Topic

## Underwriting Natural Food Cooperatives

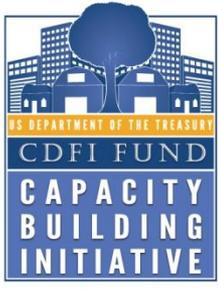
- Why?
  - Understand the structure and unique nature of cooperatives
  - Learn about the “nuts and bolts” of underwriting cooperative food retail outlets



# Presenter



Margaret Lund  
[MLund95@gmail.com](mailto:MLund95@gmail.com)  
612-750-1431





# Underwriting Natural Food Cooperatives

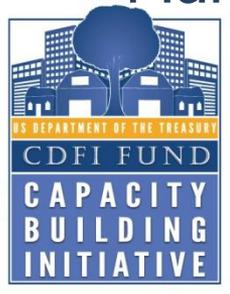
Margaret Lund

April 11, 2012

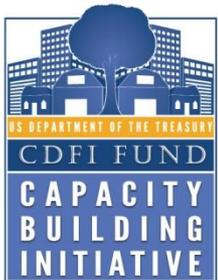


# Basic Elements of a Natural Foods Cooperative:

- Owned and controlled by its (usually consumer) members
- Adheres to an international set of common cooperative principles and values (see [www.ica.coop](http://www.ica.coop))
- Governed by an elected board, managed by hired staff
- There are 300+ consumer food co-ops in the U.S.; the largest 125 are members of the NCGA
- NCGA members have annual sales of \$1.4 billion, membership of 1.3 million;
- Many formed in the 1970's-1980's; lots of recent start-ups

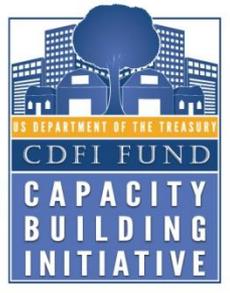


# Not the '70's anymore . . .



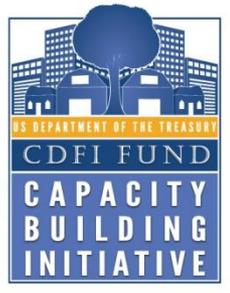
# Market Trends and Developments in the Natural Foods Sector

- Sales of organic products have grown from \$1 billion in 1990 to \$26.7 billion in 2010;
- Double-digit sales growth every year for the last 20 years until 2009 (7.7%)
- Largest seller of organic foods in U.S. is Walmart; top 5 are conventional chains, Whole Foods is # 6
- It is a significant, growing, and increasingly mainstream segment of the market
- Food co-ops have more than held their own during the recent recession; growing part of the market



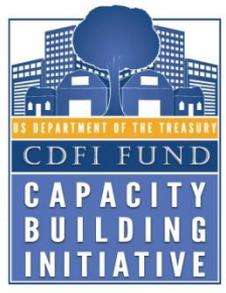
# National Context

- *Cooperative Grocer* industry publication since 1985
- NCGA was formed in 1999; provides business services and group purchasing for member co-ops
- Savings from group purchasing has allowed the organization to fund a variety of specialized TA services, including its own development arm and financial benchmarking system (CoCoFiSt)
- Specialized TA also available from private consulting firms, primarily Cooperative Development Services – CDS
- Food Co-op Initiative founded to assist start-ups



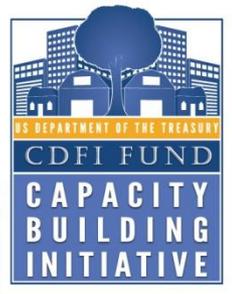
# Key underwriting differences from conventional grocery stores

- Gross margin is higher -- 36 – 39%
  - Mix of products
  - Margin on products
  - More artisan products, organics, bulk
  - Commonly offer deli and prepared foods
- Labor expense is higher – 23 – 25%
  - High expectation of service and knowledge
  - Fund member services and education functions
  - High road employers, good benefits etc.
  - Offer much greater number of SKUs etc.,



# Other differences between Co-ops and conventional food stores

- Market draw is often much wider than regular grocery stores
- Education rather than income is the key variable in natural foods purchasing; race is not
- Personal guarantees are generally not feasible collateral; need to underwrite, have confidence in the operation itself
- Food co-ops are often key players in, and builders of, existing healthy foods infrastructure



# The "Locovore" advantage

> YOU SAVED \$0.40 <  
0.WW Elbow Noodles 16oz Bion 1.99 F  
> YOU SAVED \$0.40 <

-- PRODUCE --  
Lettuce Green Leaf Organic 2.49 F  
\*APPLES 3# Bag Breazy Hill Org 4.99 F  
\*APPLES 3# Bag Breazy Hill Org Mbr special -0.51 F  
Lettuce Red Leaf Organic 2.49 F  
Lettuce Red Leaf Organic -2.49 UD

-- REF GROCERY --  
\*Hummus Tahini 7oz Holyland 3.19 F  
\*Greek Pita Bread 4ct Holyland 2 @ 2.59 5.18 F

MEMBER DISCOUNT 3 @ -2.50 -7.50 F

SUBTOTAL 80.43  
TAX 0.89  
TOTAL 81.32  
CREDIT CARD 81.32  
CHANGE 0.00

----- YOUR SAVINGS -----

DISCOUNTS: \$7.50

SPECIALS: \$8.51

You Saved \$16.01

\* Local Products/Companies: \$31.98 \*

35.96% of purchase

Member 284172

Thank You!!!

Returns accepted with receipt  
within 90 days of purchase

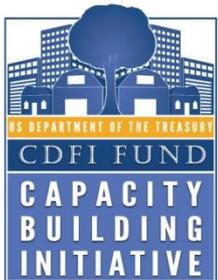
Visit us at  
[www.wedge.coop](http://www.wedge.coop)



Explore our online store  
gifts, housewares, clothing!  
[www.WedgeWorldwide.coop](http://www.WedgeWorldwide.coop)

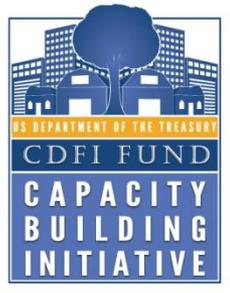


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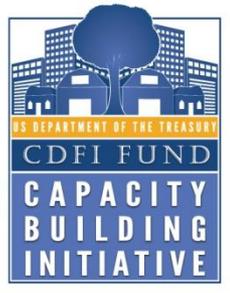
# What is *not* different . . .

- Average profit margin is around 1 to 2 percent . . .



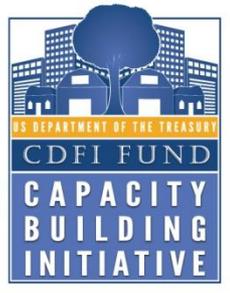
# Understanding Membership

- Members provide the base capital in terms of a set share price each
  - Be sure to understand how the co-op's membership system works
  - Most co-ops moving away from a discount structure to an annual patronage dividend
- Members typically (depending on state law) also offer subordinate "quasi-equity" members loans for start-up or expansion
  - Co-op structure is governed by state law; state securities laws vary regarding how member investments are treated



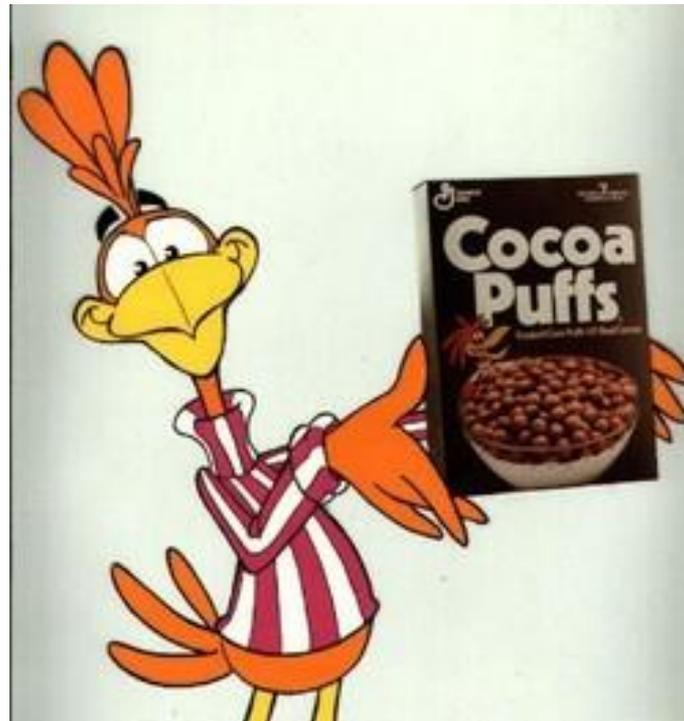
# Understanding Membership continued . .

- Members should provide a solid percentage of sales
  - This amount will vary by market – over 50% and less than 100% is best
- Membership should be growing
- Members elect the board of directors from amongst themselves
  - Food co-ops typically do not have outside directors
  - Look for mix of skills, mix of tenure
  - Ask about board turnover



# What is this CoCoFiSt?

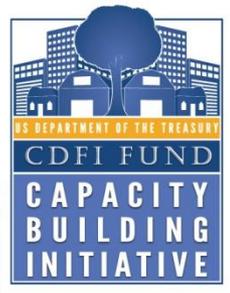
Not this . . .



# But this!

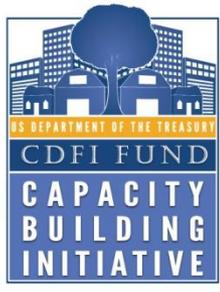
**Common Cooperative Financial Statements** – a unique peer comparison and support system

- All NCGA members share a common chart of accounts
- Finance managers send monthly data to CoopMetrics, who return reports comparing each store's performance to a selected peer group
- Can also get comparison reports by department, region, size etc.
- Has spawned several subsidiary groups (CoCoBuds, CoCoHabana, CoCoMamas) whereby department managers at different co-ops can both compete with and support each other



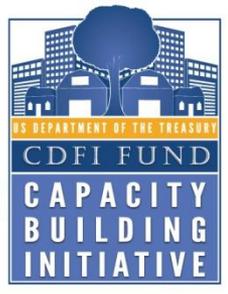
# Some national CoCoFiSt data . .

	<u>Small</u>	<u>Med-Small</u>	<u>Med-Large</u>	<u>Large</u>
Sales	2,025,732	6,156,301	8,895,379	12,285,258
Gross Margin	35.80%	39.29%	37.74%	37.16%
Personnel	23.45%	25.08%	22.75%	24.33%
Occupancy	3.97%	3.54%	4.07%	2.95%
Net Income	1.44%	0.98%	2.21%	0.81%
4th Quarter 2007				



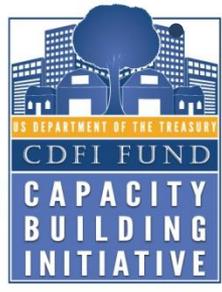
# Underwriting Issues

- There is COGS, labor and everything else
- Real estate costs do not drive the deal; location does
- Quite a bit of variability by store size
- Sales growth trajectory slower in rural markets
- Deli can add a lot of margin, also potential for loss (TA)
- Market studies based on conventional grocery comps are often not accurate; G2G has database specific to food co-ops
- These are not hard collateral loans
  - Your key security is their ability is turning tomatoes into cash – ability to **turn inventory** and know where they are making their \$



# Food Co-op Expansions

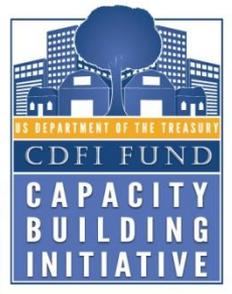
- Look to current comparable CoCoFiSt data for projections
  - Make sure market study is for natural foods co-ops, with comps to similar-size, similar market food co-ops
  - Ask what kind of TA, support they are getting from NCGA, peers, consultants
  - Make sure members are sufficiently vested
  - Don't tie up their cash
  - Very typical to lose \$ first year, 18 months before it cash flows
  - Discounts, terms from vendors can be substantial
  - Expect it will take 6 months or so to stabilize margins etc.
- Strong sales can cover a lot of mistakes



# Additional thoughts about Food Co-op Start-ups

All the same thoughts as expansions plus . .

- National support organization the Food Cooperative Initiative has lots of data, technical assistance
- 50 new food co-ops have started in the last five years, 50 more in some kind of development;
- Only five of these have failed so far
- Strong and growing interest in local foods; is this the new organic? Too soon to tell . . . .

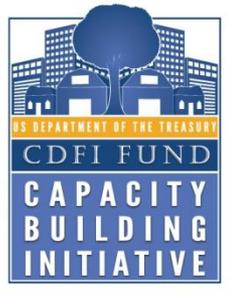


# Case Study – Lexington Food Co-op, Buffalo, NY



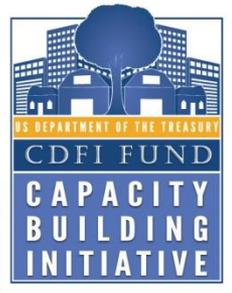
# At time of expansion . . . 2005

- Co-op founded in 1971
- 1,200 SF retail; self-described “worn-out hole-in-the-wall”
- In 1997 co-op sustained a loss of \$50,000 on sales of \$800,000; on top of eight years of flat sales, equity near zero; finance staff recommended closing
- Instead, key board and staff members worked on turnaround – staff began wearing nametags, had customer service training - sales grew, almost at \$2 million by 2004
- In 2001, started planning expansion, hosting member forums, working with consultants, building vision



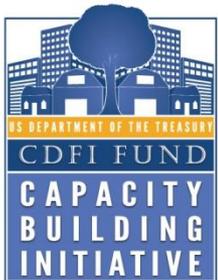
# New Store Projections

- 4,500 SF retail (3x as big)
- New construction building
- Addition of a deli
- Projected first year sales increase of 75%



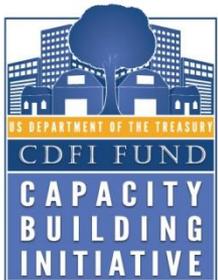
# Project Sources

SOURCES	Total	
Cash Reserve	121,000	3.5%
Cash from Operations	84,412	2.4%
New Member Equity	65,000	1.9%
Donations, Sale of Equipment	15,000	0.4%
Member Loans	574,347	16.6%
Owners Contribution	859,759	24.9%
Vendor Credit	27,198	0.8%
Free Fill	30,000	0.9%
LEAF	100,000	2.9%
BERC Forgiveable Loan	200,000	5.8%
NCDF	300,000	8.7%
ECIDA & BERC	360,000	10.4%
2nd Position Debt	1,017,198	29.4%
NCB - Equipment and Working Capital	480,000	13.9%
NCB FSB	1,100,000	31.8%
1st Position Debt	1,580,000	45.7%
<b>Total Sources</b>	<b>3,456,956</b>	<b>100.0%</b>



# Project Uses

USES			
Acquisition - Land		618,000	17.9%
Builder's Risk, Electrical Service Install		35,000	1.0%
Construction		1,219,989	35.3%
Equipment		550,000	15.9%
Additional Inventory		110,000	3.2%
Fees		461,025	13.3%
Start-up Promotion		14,322	0.4%
Start-up Staffing		14,322	0.4%
Business Disruption		12,788	0.4%
Holding/Site Costs		45,298	1.3%
Interest during project		111,212	3.2%
Working Capital 1st Year		125,000	3.6%
Subtotal Uses		3,316,956	96.0%
Overrun Allocation (10% of project costs-purchase price)		140,000	4.0%
Total Uses		3,456,956	100.0%



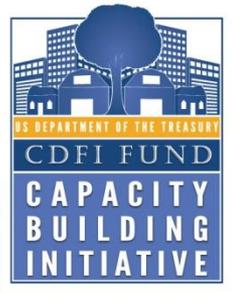
# Risk Issues

- Store size over 3 times as big
- Added element of deli operation
- New building construction
- Limited collateral
- Recovering, but still not really strong balance sheet
- Site has limited parking
- Overall economy of Buffalo stagnant to declining



# Elements of Success

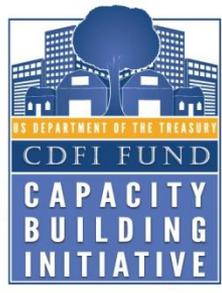
- Over \$250,000 in member loans raised before securing site, average size of \$3,000 indicating deep member commitment
- Strong general manager with years of experience building vision and relationships
- Very strong local neighborhood market (walkable, mixed-use, lots of independent businesses); very limited competition



# Results

## Lexington Food Co-op Results vs. Projections

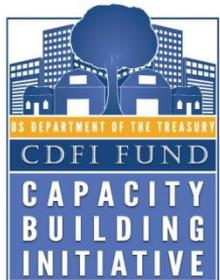
	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>Proj 2012</u>
Sales	1,948,029	2,116,333	4,483,561	5,272,556	6,319,454	9,400,000
Growth		9%	112%	18%	20%	
Net Income		(5,324)	(238,243)	38,410	87,108	
Projected Growth			3,500,000 75%	4,025,000 15%	4,427,500 10%	



# Lexington Food Co-op today



# Happy Shoppers – 6,500 members with 20 more joining every week



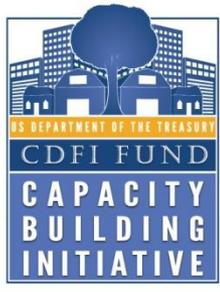
# Resources

Natural foods cooperatives:

- [Ncga.coop](http://Ncga.coop)
- [Cooperativegrocer.coop](http://Cooperativegrocer.coop)
- [Foodcoopinitiative.coop](http://Foodcoopinitiative.coop)

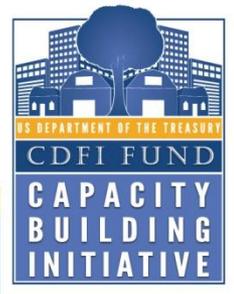
On cooperatives, generally:

- [Ica.coop](http://Ica.coop)
- [Ncba.coop](http://Ncba.coop)
- [Go.coop](http://Go.coop)





# Additional Resources



# Financing Healthy Food Options Resource Bank

[http://www.cdfifund.gov/what\\_we\\_do/FinancingHealthyFoodOptionsResourceBank.asp](http://www.cdfifund.gov/what_we_do/FinancingHealthyFoodOptionsResourceBank.asp)



The screenshot shows a web browser window with the URL [www.cdfifund.gov/what\\_we\\_do/FinancingHealthyFoodOptionsResourceBank.asp](http://www.cdfifund.gov/what_we_do/FinancingHealthyFoodOptionsResourceBank.asp). The page features a navigation menu on the left with links: WHO WE ARE, WHAT WE DO, IMPACT WE MAKE, NEWS & EVENTS, and HOW TO APPLY. The main content area is titled "COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND" and "UNITED STATES DEPARTMENT OF THE TREASURY". Below this, the page is titled "Financing Healthy Food Options Resource Bank" and lists three main sections: I. Training Curriculum, II. Financial Resources Catalogue, and III. Food Desert Mapping Tools. Each section contains a list of links to various resources. A disclaimer at the bottom states that the documents were funded by the CDFI Fund under Contract TPD-CDF-10-C-0006, Task Order 0001, and that the content is the responsibility of the authors. The page was last updated/reviewed on 12/07/11.

CDFI Fund - U.S. Treasury - x

www.cdfifund.gov/what\_we\_do/FinancingHealthyFoodOptionsResourceBank.asp

Opportunity Financ... CARS™ - Comprehe... Other bookmarks

- WHO WE ARE
- WHAT WE DO
- IMPACT WE MAKE
- NEWS & EVENTS
- HOW TO APPLY

## COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND

UNITED STATES DEPARTMENT OF THE TREASURY

### Financing Healthy Food Options Resource Bank

#### I. Training Curriculum

- [Food Systems Overview](#)
- [Healthy Food Retail Financing](#)
- [Financial Services for Mid-Tier Food Chain Enterprises](#)
- [NMTC & Urban Supermarkets](#)
- [Understanding the Grocery Industry](#)
- [Underwriting Supermarkets & Grocery Stores](#)
- [Mid-Tier Food Chain Enterprises Overview & Underwriting](#)
- [Capitalizing Healthy Food Retail Initiatives](#)
- [Identifying Optimal Areas for Supermarket Development](#)

#### II. Financial Resources Catalogue

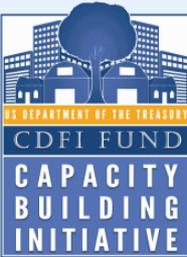
- [Financial Resources Catalogue](#)

#### III. Food Desert Mapping Tools

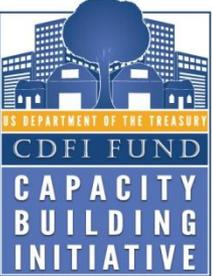
- [USDA Food Desert Locator](#)
- [Policy Map](#)

*These documents were funded by the CDFI Fund, under Contract TPD-CDF-10-C-0006, Task Order 0001. The curriculum and opinions expressed in these documents are those of the authors, who are solely responsible for the content, and do not reflect the opinions of the CDFI Fund or any other person, entity, or organization.*

Last updated/reviewed: 12/07/11



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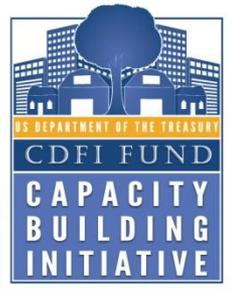
# Upcoming Workshops

## Farms & Food Production

Boston, MA

May 31<sup>st</sup> and June 1<sup>st</sup>

[Link](#) to Training Information & Registration



# Upcoming TA Webinars

## **Underwriting Supermarkets & Grocery Stores**

•Wednesday, April 18, 2pm ET

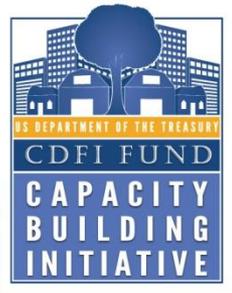
## **The Grocery Gap**

•Tuesday, April 24, 2pm ET

## **Connecting Farms to Institutions**

•Monday, April 30, 2pm ET

Visit [www.opportunityfinance.net/FHFOwebinars/](http://www.opportunityfinance.net/FHFOwebinars/) to register for one or all of the TA webinars



# Contact Information

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215.320.4303



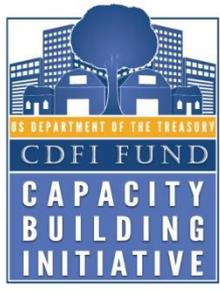
**Christy Bare**

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# Underwriting Natural Food Cooperatives

Margaret Lund

April 11, 2012

