[Food SE] Channels Analysis

Agenda

Framework	• Channel analysis methodology
	  • [Food SE]'s current channel mix
	  • Channel evaluation framework

Research and findings	• Channel evaluation
	  • Unit margin
	  • Breakeven volume
	• SE interviews
	  • Costs by channel
	  • Customer acquisition
	  • Production capacity
	  • Mission

Recommendations	• Risks • Final recommendations and next steps

[Food SE] currently sells a total of 11K units through 6 primary channels

	Direct to consumer			Business to business					Total
	Online ✓	Brick and mortar ✓	Special events ✓	Distributors [Main Distributor] ✓	Distributors *(Other)* ✓	Wholesale (retail) ✓	Bulk sales ✗	Corporate ✗	
Definition	Digital sales through SE website	Physical sales in SE-owned outlet	Physical sales at SE-staffed events	Distributors and large chains	Distributors and large chains	Small and medium retailers	Private label	Corporate buyers	-
SE-specific description of channels	[website names]	[stores and other physical sales locations]	[example events]	[names of the largest distributor]	[names of other distributors and chains]	[Numerous small and medium businesses]	[Potential private label /co-branding partnerships]	N/A	-
Revenue	$3,024	$5,136	$5,880	$82,213	$14,237	$13,776	N/A	N/A	**$124,266**
Price per unit	$24.0	$24.0	$24.0	$9.5	$11.5	$14.0	N/A	N/A	-
Variable cost per unit	$8.5	$8.5	$8.5	$8.5	$8.5	$8.5	N/A	N/A	-
Contribution margin	$15.5	$15.5	$15.5	$1.0	$3.0	$5.5	N/A	N/A	-
Units sold	$126	$214	$245	8654	1238	984	N/A	N/A	**11,461**
Gross profit	$1,953	$3,317	$3,798	$8,654	$3,714	$5,412	N/A	N/A	**$26,848**

✓ Currently active
✗ Not currently active

Framework for comparing channels for investment potential

Channel Criteria	Criteria Specifics
Financial	
Unit margin	Profitability of an individual sale
Breakeven volume	Number of additional unit sales needed to break even
Sales and marketing costs	Expected costs associated with acquiring customers in channel
Number of potential customers	Number of customers that could potentially purchase through the channel
Production Capacity	
Staff	Additional FTEs needed to scale (feeds into investment cost)
Equipment / facilities	Ability to meet channel demand with existing equipment
Social	
Brand alignment	Opportunity to directly communicate mission with customers and build a customer base that shares SE values
Transitional people employed	Number of transitional workers needed to grow production
Upskilling opportunities	Opportunity for upskilling for transitional workers

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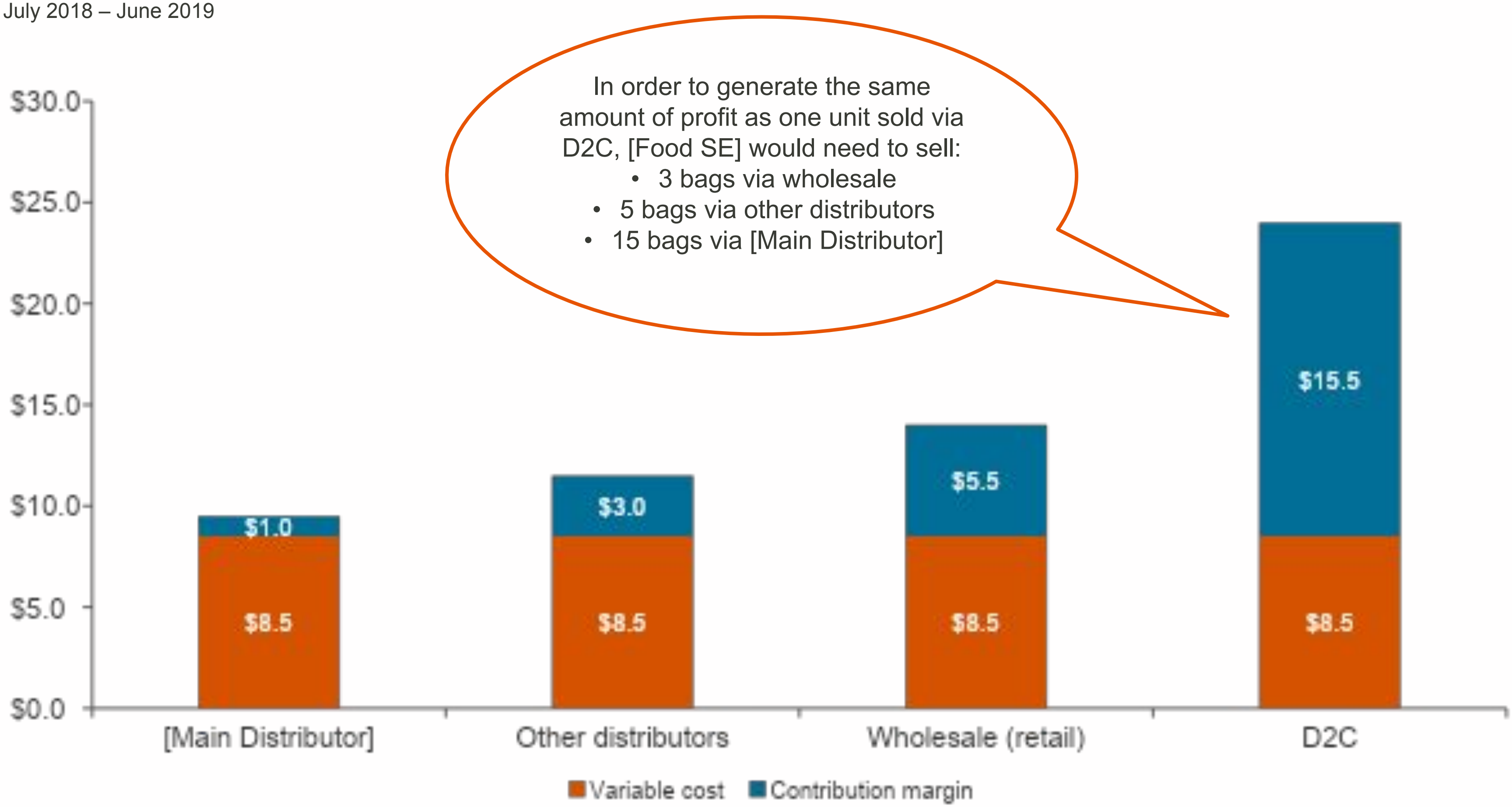
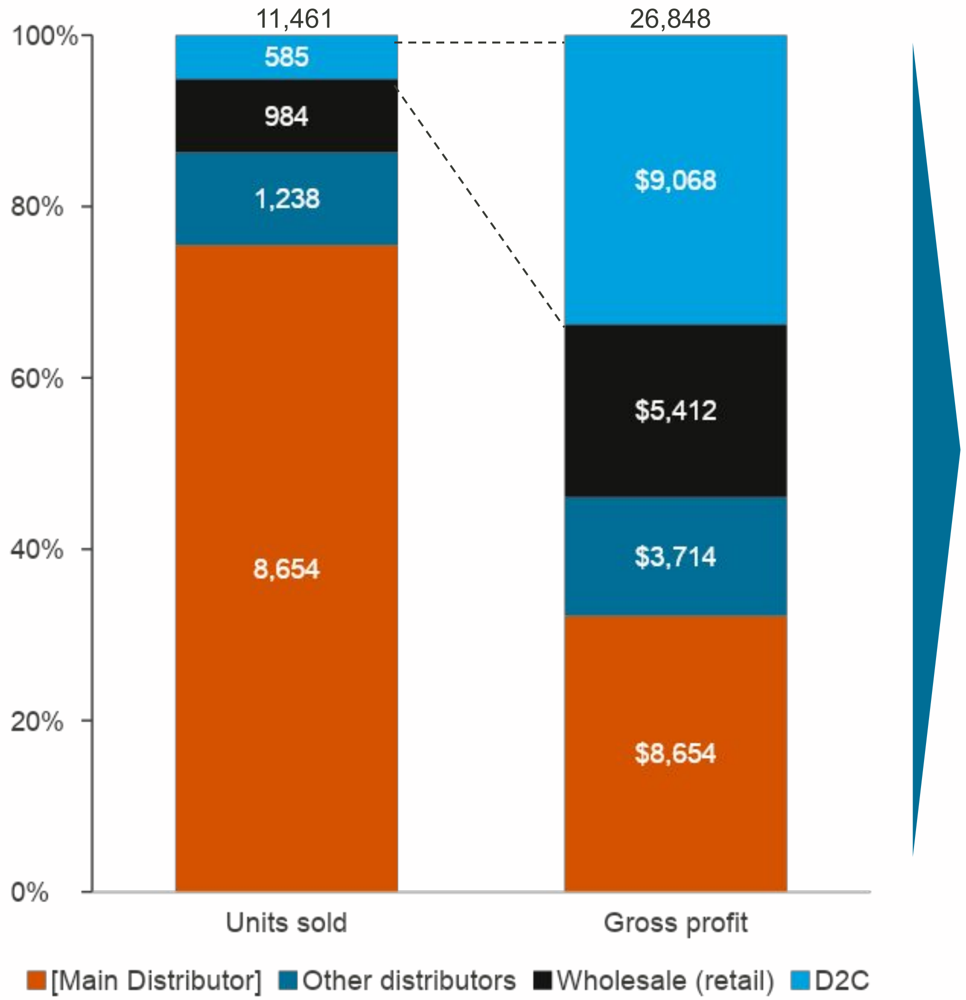
UNIT MARGIN: A D2C sale delivers 15X the contribution margin of a unit sold via [Main Distributor]

Variable cost and gross profit
generated per unit by channel
July 2018 – June 2019



UNIT MARGIN: D2C accounts for 5% of units sold, but delivers 34% of gross profit

Units sold and gross profit generated by channel
July 2018 – June 2019

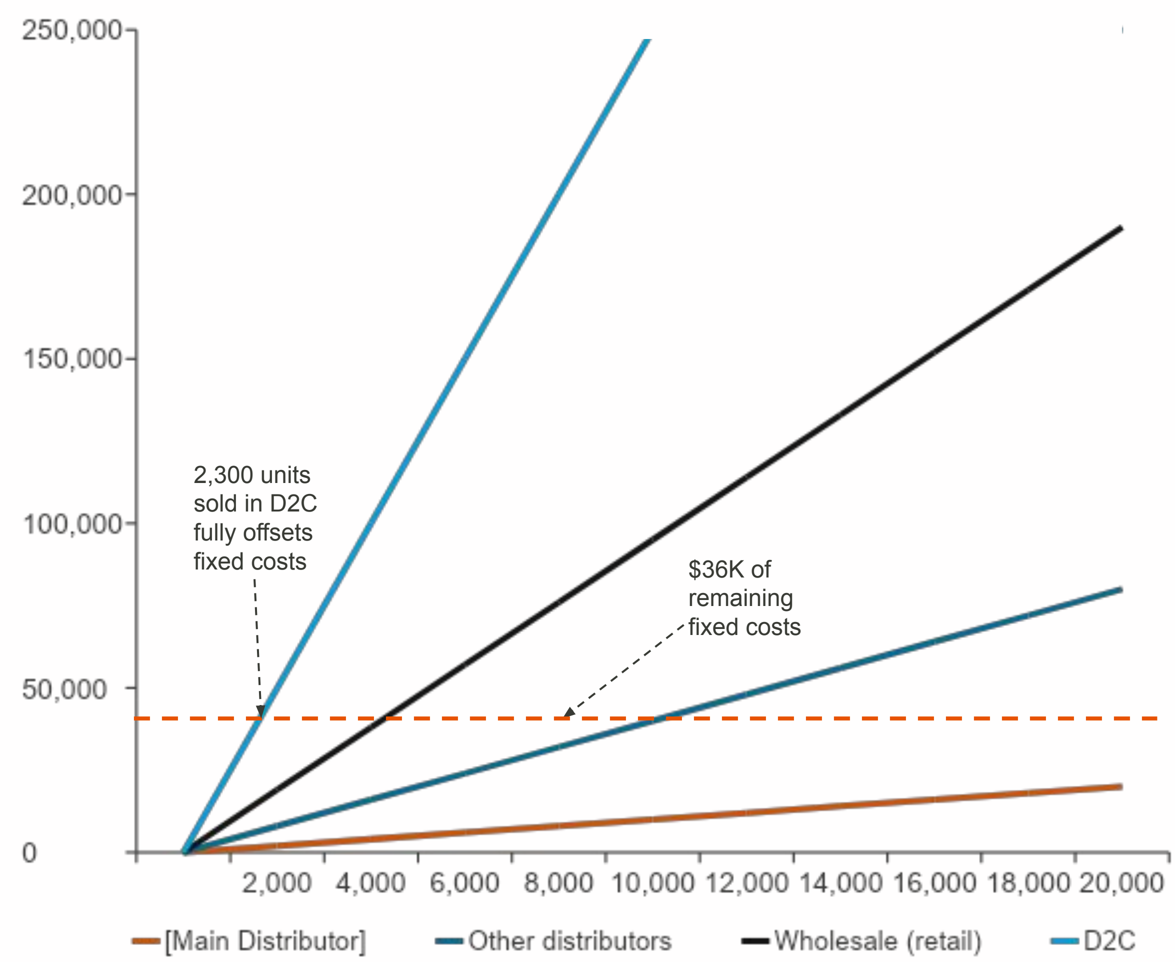


Key Takeaways

- Selling via D2C allows [Food SE] to capture at least 3X gross profit per unit compared to the next best alternative (wholesale)
- Margins at [Main Distributor] are so low that the 75% of sales volume generated there accounts for less than a third of the profit
- If [Food SE] could quadruple D2C sales, [Food SE]'s total gross profit would increase 2X

BREAKEVEN VOLUME: Only ~2,300 D2C sales are needed to cover [Food SE]'s outstanding $36K of fixed costs

Projected gross profit ($) by units sold by channel



Key Takeaways

- [Food SE]'s current fixed costs (SE Manager, Marketing & Advertising, and G&A) total $63K
- Current sales generate gross profit of $26.8K, leaving $36K of fixed costs to offset
- Increasing D2C sales would offset the rest of [Food SE]'s fixed costs with the least amount of needed marginal sales (2,300 units)

COSTS BY CHANNEL: Expanding D2C sales requires more investment in sales and marketing, while expanding B2B sales would require investing in scaling production

<table>
<tr><th></th><th></th><th colspan="3">D2C</th><th colspan="4">B2B</th></tr>
<tr><th></th><th></th><th>Online</th><th>Brick and mortar</th><th>Special events</th><th>Distributors</th><th>Wholesale</th><th>Bulk sales</th><th>Corporate</th></tr>
<tr><td rowspan="2">Sales and marketing</td><td>Staff</td><td>• FTE to manage online marketing</td><td>• FTEs to manage storefront</td><td>• FTEs to man events</td><td colspan="4">• FTE to acquire and manage accts.</td></tr>
<tr><td>Customer acquisition</td><td>• Consultant
• Online marketing
• Website re-design</td><td>• New storefront</td><td>• Travel
• Event fees</td><td>• Trade shows</td><td>• Trade shows</td><td>• Trade shows</td><td>• Special events</td></tr>
<tr><td rowspan="2">Production</td><td>Staff</td><td colspan="3">• No additional FTEs</td><td colspan="4">• Additional FTEs required to scale production</td></tr>
<tr><td>Equipment / facilities</td><td colspan="3">• No additional equipment
• No additional space</td><td colspan="4">• No additional production equipment
• Additional delivery vehicles needed as sales increase
• Additional space required for processing, packing, and storing additional product</td></tr>
</table>

Note:
[1] Staff costs are inclusive of fringe benefits.

CUSTOMER ACQUISITION: Although D2C sales offer the highest margin, they also have the highest customer acquisition costs

	Channel	Customer acquisition	Investment required	Customer exposure
D2C	***Online***	1. **Staff** (at least 1 dedicated FTE) = ~$50-100k per year 2. **Consultant** = ~$10k (one-time cost) 3. **Online marketing** (social media, email, and SEO) = ~$10k+ per year (scaling up with growth) 4. **Website re-design** (optional) = ~$10k (one-time cost) *~$60-110k+ per year + ~$10-20k one-time costs*		
	Brick and mortar	1. **Staff** (at least 1 FTE for daily store maintenance) = ~$50-100k per year 2. **New storefront** in neighborhood with heavier foot traffic = ~$50k+ per year *(rent varies based on location and square footage)* *$100-150k+ per year*		
	Special events	1. **Staff** (at least 1 FTE per event) = *varies based on number of events* 2. **Travel** = *varies based on number and location of events* 3. **Event fees** (generally waived for nonprofits) = ~$0–1k per year *Varies based on number and location of events*		

CUSTOMER ACQUISITION: B2B sales have lower customer acquisition costs than D2C, but there are still significant investments required

<table>
<tr><th></th><th>Channel</th><th>Customer acquisition</th><th>Investment required</th><th>Customer exposure</th></tr>
<tr><td rowspan="4">B2B</td><td>Distri-butors</td><td rowspan="3">1. Staff (at least 1 dedicated FTE) = ~$50-100k per year
2. Trade shows = ~$10k+ per year

<u>~$60-110k per year</u></td><td rowspan="3"></td><td rowspan="3"></td></tr>
<tr><td>Whole-sale</td></tr>
<tr><td>Bulk sales (private label)</td></tr>
<tr><td>Corporate</td><td>1. Special events (see previous slide)
= varies based on number and location of events

<u>Varies based on number and location of events</u></td><td></td><td></td></tr>
</table>

PRODUCTION CAPACITY: D2C requires less additional investment in production staff and facilities than B2B to drive equal gross profit

	D2C	B2B
Staff	Highly attractive • In order to cover its fixed costs, if [Food SE] were to focus its investment on D2C sales, they would only need to ***increase production by ~20%*** • ***No additional FTEs*** are required to support this increase in production	Somewhat attractive • However, in order to generate an equivalent gross profit by investing in B2B sales, [Food SE] would need to ***increase production by ~1.6X–3.2X*** • In this case, [Food SE] would likely need to ***hire additional production-focused staff*** to support this scaling • For example, a Bakery SE ***increased its production by 20X,*** which necessitated growing its team from ***five to eight staff***
Equipment / Facilities	Highly attractive • [Food SE] is not currently running at full capacity and can increase production significantly with its current equipment • ***No additional space*** would be required to process, pack, and store the additional ~20% of product	Somewhat attractive • [Food SE] is not currently running at full capacity and can increase production significantly with its current equipment • ***Additional space*** will likely be required to process, pack, and store the additional ~1.6–3.2X of product

MISSION: While B2B employees more transitional employees, D2C allows [Food SE] to directly connect with customers and provide upskilling opportunities to its transitional employees

	D2C	B2B
Brand alignment	**Highly attractive** • SE can ***directly connect with customers*** who care about the target population and their barriers, environmental sustainability, and other values that the SE promotes	**Somewhat attractive** • Some potential customers may be ***skeptical of SE product quality*** • Some retailers, e.g. Whole Foods and Ben & Jerry's, and ecommerce partnerships, e.g. Uncommon Goods, Packed with Purpose, etc. ***seek local, mission-based brands***
Transitio-nal people employed	**Somewhat attractive** • Because D2C is typically a high margin / low volume channel, there may be ***fewer positions for transitional employees*** than in B2B • However, the higher margins can be used to ***cover program costs,*** expand SE services, and provide capital for business investment	**Highly attractive** • Given the large quantities ordered by distributor, bulk order, and private label customers, SEs may be able to ***increase number of people employed***
Upskilling oppor-tunities	**Highly attractive** • Direct to consumer sales can provide valuable skills to transitional employees, including ***customer service*** • Expanding online sales can provide ***higher wage upskilling opportunities***, particularly around ecommerce (e.g. tracking online marketing sales conversions, optimizing SEO, offering direct customer service, managing social media, overseeing shipping logistics, and more)	**Somewhat attractive** • B2B sales can offer ***some upskilling opportunities*** to transitional employees, including account management, delivery logistics, inventory management, and more

Online D2C is the most promising channel…

Channel criteria	Supporting evidence	D2C			B2B				
		Online	*Brick and mortar*	*Special events*	*Pet Food Express*	*Other distri-butors*	*Whole-sale*	*Bulk sales*	*Corp.*
Financial									
Unit margin	D2C has a unit margin of 65%, whereas other channels range from 11% to 39%								
Breakeven volume	D2C requires 2,300 additional sales to offset remaining fixed costs, whereas other channels require at least ~6,500								
Sales and marketing costs	B2B sales and marketing is less costly than D2C, because D2C requires each customer to be acquired individually								
Number of potential customers	Online D2C, distributors, and wholesale have access to the largest portions of the addressable market								
Production Capacity									
Staff	D2C does not require major changes to production staff, due to limited volume increases relative to B2B								
Equipment / facilities	D2C does not require additional equipment or facilities, whereas B2B may necessitate additional space								
Social									
Brand alignment	D2C and corporate sales allow for direct interaction with customers whose values align with the brand/mission								
Transitional PE	The large production volume of B2B sales provides additional transitional employment opportunities								
Upskilling opportunities	D2C, particularly online, offers higher-wage upskilling opportunities via increase digital literacy and ecommerce exposure								

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RISKS: B2B is generally higher risk than D2C given the high concentration of sales in a few accounts and high level of account management required

Strong account management is necessary to retain B2B accounts	• "Lots of wholesale partners placed their first order 4-5 years ago and have never ordered again. A ***huge time investment is required to maintain those relationships***. We have to work with stores to fit our brand into their space. We ***train their staff*** on how to talk about our products and mission" – Accessories SE • "There is ***high turnover*** in the buyers that we have relationships with" – Personal Care SE • "With big retailers, such as Whole Foods, be honest about how much you can produce and when you can deliver. Work relationships slow and well, rather than over-promising. ***Account management*** is very important" – Woodworking SE
Having a single anchor customer exposes the SE to more risk	• "If something happened to our large private label partner, that would definitely impact us. It's the same with our other large retail partner. We would ***lose a national distributor***" – Brownies SE • "Our private label buyer is trying to streamline production processes across all of their suppliers, which requires us to redo our production, including investing in new equipment and doing additional quality testing. They're footing the bill for the consultant. However, their ***pricing doesn't include all the costs,*** such as sending out samples to lab for testing every week" – Bakery SE
Online sales involves less risk but requires more investment without guaranteed sales	• "If you hire a dedicated FTE for online sales and traffic is slow, that's a waste of the FTE time. You should ***hire someone part-time to test it*** out before creating a full-time position" – Woodworking SE • "Ecommerce is lower risk but ***requires more customer service*** and individual sales and time" – Brownies SE

Final recommendations and next steps

[Food SE] should invest in online D2C because…

- D2C unit margins are between 3X and 15X greater than those of B2B channels, meaning that [Food SE] would need to sell significantly fewer units to generate equivalent profits
- Because [Food SE] needs to sell fewer units in D2C, this channel does not require hiring additional production FTEs or expanding facilities
- Within D2C, online provides access to the greatest number of potential customers, due to the geographic limitations of brick and mortar and special events
- In online D2C, each customer has to be acquired individually via digital marketing, which requires increased spend and expertise
- Although the lower volume in D2C limits transitional employment opportunities, running an online business provides unique digital upskilling opportunities

Next steps to consider include…

- Hire or develop expertise in online marketing, including content creation and campaign management (particularly on Facebook and Instagram)
- Utilize a consultant to kick off digital marketing efforts, with key deliverables including both advertising strategy and implementation plans to enable hand-off to [Food SE] team
- Budget ~$500 per month for initial online marketing efforts, with [Food SE]'s online marketing manager developing, testing, and iterating on content and ad placement
- Increase monthly spend over time as the most effective content and placement strategies are identified
- Consider strategies to incentivize customers acquired through other channels to purchase online (e.g. free shipping with minimum order value)

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