

Distribution of the added value of the organic food chain

The organic market is increasing across Europe, but organic land area is not keeping up with this growth, especially in the UK. ORC was a core partner in a European Commission (DG AGRI) funded study to understand whether farmers are rewarded with a sufficient share of the added value in the organic supply chain, and are therefore motivated to convert and scale-up organic production. ORC researcher **Stefano Orsini** discusses the findings.

The organic market in the European Union (EU) is continuing to increase. In the past decade, the value of European and EU markets has more than doubled, with an increase in organic food consumption by 110% from €22.4 to €47.4.¹ Despite such a dynamic market, the land managed organically is not growing at the same pace, leaving the market potential at the production level untapped. This is also true for the UK, where the organic market was estimated to be worth £2.09 billion² in 2016, with an increase in sales by 7.1% compared to the previous year, whereas the amount of land farmed organically has continued to decline with a drop of 3.6%.

Organic products are usually more expensive in the shops and farm gate prices are higher in many cases, but there is a lack of published data on prices at the various levels of the value chain, and especially on how added value is distributed among the market players. The project 'Distribution of the Added Value of the Organic Food Chain' investigated 18 case studies of product supply chains (SCs) for apples, milk and pasta, with two case studies in each of the nine European countries involved in the study. Market players (e.g. processors, distributors and retailers) and other experts (e.g. from certification bodies) were interviewed to estimate the distribution of added value along the SCs, and to identify the key factors affecting added value creation and distribution. The case studies illustrated that the organisation of supply chains can vary considerably. Some examples of the SC case studies are illustrated in Figure 1 below.

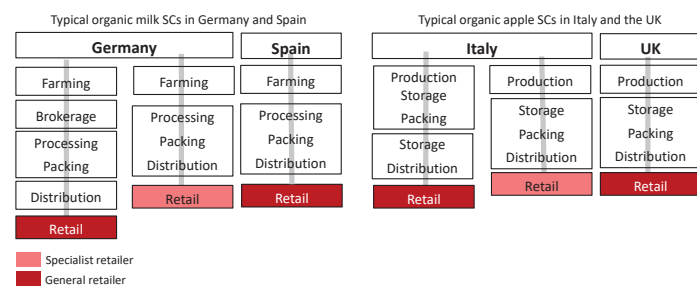


Figure 1: Examples of typical SCs studied. The boxes include operations undertaken by the same actor (integration of SC operations)

Capturing added value

Our results from the case studies reveal that organic producers get higher prices than conventional producers for the three products apples, milk and pasta (Figure 2).

Some organic producers capture more than 40% of the total added value, for example for organic milk in France and Germany, or even more than 60% as with organic apples in Estonia. Some others get less than 10%, such as milk producers in Spain and the Czech Republic. Producers of raw material for more processed food like pasta generally only capture a low share.

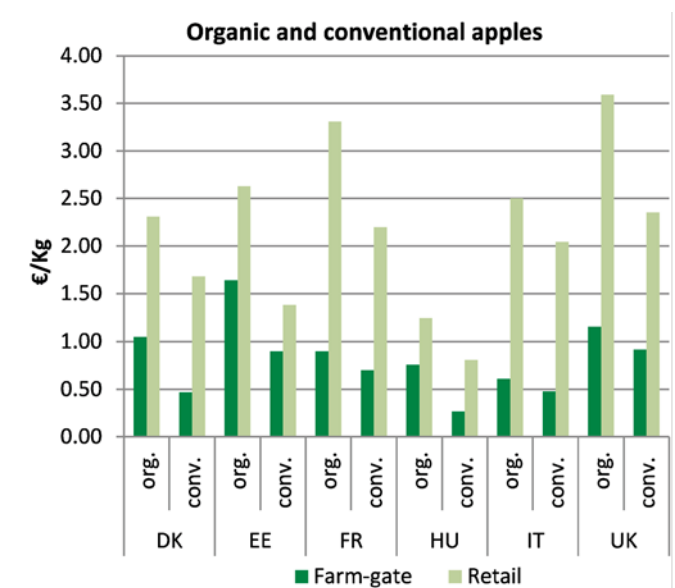
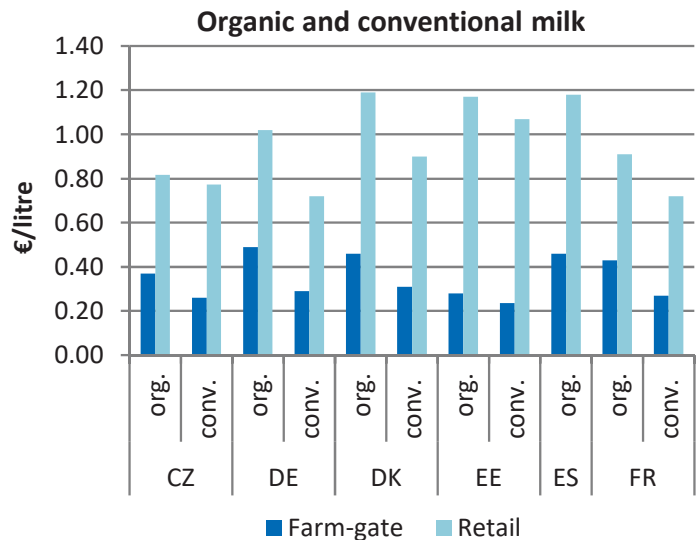


Figure 2: Farm-gate and retail prices for organic and conventional milk and apples at general retail, in €/kg (VAT excluded). Reference year = 2016

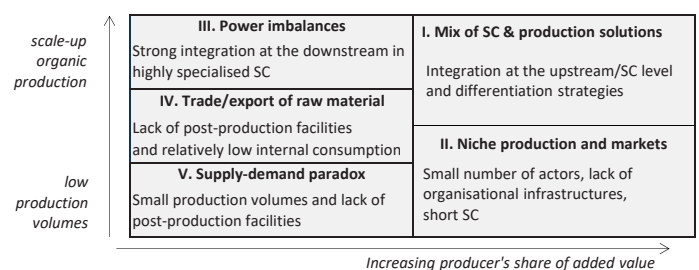


Figure 3: Five different models of organic SCs found in the case studies



Our study confirmed that multiples dominate the distribution side of the organic food chain in various markets. Cases of higher share of added value at production level were found both in specialist and general retailer SCs. This challenges some expectations that would essentially relate fair market models to specialist shop retailers.

In summary, the highest proportions of added value captured by producers are connected with the following cases (see Figure 3 facing page, below):

- **Niche production and markets**, as illustrated by the organic apples case study in Estonia, where the producer undertakes different SC operations including cold storage and packing, and at present can get more than 60% of the total added value. However, this emerging organic sector in Estonia involves only a small number of actors and lacks organisational structure, which prevents producers from scaling up production and penetrating the mainstream food market to meet a growing demand and to move out of the niche product category.
- **'Mix of SC and production solutions'** includes a number of business and marketing approaches that are more typical of more developed organic markets. Integration throughout the SC is key to let producers achieve a fair share of added value and economies of scale. For example, **cooperation among producers** of a supply chain often results in strengthened bargaining power, and reduced costs for collection, transportation and storage. Likewise, special **agreements between producers and retailers**, whether multiple or specialist, can result in win-win situations, where retailers commit to buy at a fair price products that meet specific high quality standards. Cooperation seems to be more likely to occur in countries and sectors with a strong tradition of cooperation like organic milk in Germany and organic pasta in Italy, where SC operators have developed together an interest in long-term economic sustainability and mutuality. Our case studies suggest that SC management based on cooperation is a precursor for successful **product differentiation** strategies in addition to organic, including the development of supplier brands such as the cases of organic milk in Germany (e.g. Bioland) or traditional-high quality organic pasta produced in Italy and sold in a supermarket chain.

On the other hand, the cases of low share of added value to producers can be related to the following circumstances:

- A lack of investment in special processing and storage facilities, and a lack of chain integration, were reported as structural weaknesses of the organic sector, preventing the development of efficient networks for collection, storage and processing. A **supply-demand paradox** seems to occur in some fragmented organic food chains, where producers find demand insufficient to justify scaling up organic production, and upstream operators find the supply insufficient to invest in special facilities for organic products. This is illustrated by the case of organic durum wheat production in Spain, which is usually exported to other countries, because of the limited domestic processing capacity to produce organic pasta.
- Typical examples of **power imbalances** were found in the markets for organic apples in France and Italy, which are the largest producers of organic apples in the EU,

and where the downstream actors have developed their positioning strategy by providing integrated solutions and becoming strategic partners for their customers. The share of added value at wholesale level for apples was found to be remarkably high in Italy and France, while producers capture a relatively small share. The Italian and French case studies were conducted in two regions, Bolzano and Languedoc Roussillon, which are highly specialised in organic fruit production. The wholesalers play a central role, providing services for transport, storage, calibrated packaging and distribution. Another example where a downstream firm has strongly developed its positioning strategy is represented by the case study of pasta SC in Italy, where a big firm specialised in organic food distribution and retailing has appropriated value from other supply actors, and operates in a 'near-monopoly' situation according to some expert interviewees. This case study suggests that power imbalance between producers and retailers are not necessarily connected only with supermarkets.

Conclusions

Despite the positive market context which is currently characterising the EU organic sector, it seems that organic production alone may not necessarily be able to overturn the added value squeeze at the farm level, even though organic farm-gate prices have been always found to be higher than conventional. However, the variability of findings shows that successful examples for a fair distribution of added value in organic SCs exist in various outlet types and in various stages of development of the organic market.

If the potential of the growing market for organic food is to be realised at the production level in the EU, special effort is needed in some key areas that can help organic operators achieve economies of scale and reduce the SC fragmentation, which is still greater than in conventional chains. Producers can implement better SC and production solutions through cooperation and through product differentiation. There also seems to be a strong case to support investments in post-production operations, such as processing and storage infrastructures dedicated to organic food chain products. Finally, a priority area for the future development of the organic sector is the improvement of the availability of public data on the organic market, such as demand/supply and benchmark prices for specific products throughout the organic food chain. Market transparency is indeed vital to assist market players and policy makers in their investment and decision choices.

The 'Value added' research project was led by the German Thünen-Institute. Other partners were Università Politecnica delle Marche (Italy), FiBL (Switzerland), and partners in other six EU countries (the Czech Republic, Denmark, Estonia, France, Hungary and Spain).

References

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