

5. SURVEY RESULTS

The following section provides an overview of results from the organic food processor survey. The questionnaire is available in Appendix 3.

Demographic information

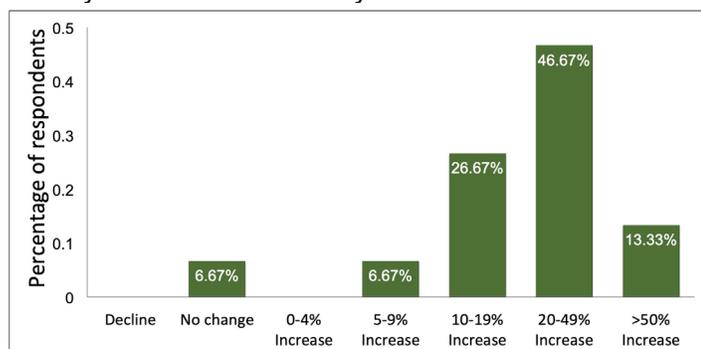
Forty-three manufacturers that process at least some organic food in Canada completed on-line or telephone surveys. Companies processed a range of organic product types, although the largest share of respondents were grain processors (33%). All but two of the companies were Canadian-owned and most were structured as private corporations. Twenty-three (53%) processed both organic and conventional products and 20 (47%) processed organic only. The average length of time businesses reported processing organic food products was 16.6 years.

Sales and Growth

The largest number of surveyed companies (34%) reported 1-5 million in annual sales. Four of the companies reported sales under \$100,000 and four had annual sales over \$50 million.

When asked about year-over-year growth in gross sales in the survey year versus the year before, most respondents reported strong growth. Figure 5.1 shows that 47% of respondents reported growth between 20 and 49% while 29% reported growth between 10 and 19%. Thirteen percent reported growth greater than 50%. None reported decreased growth.

Figure 5.1 Percentage of survey respondents reporting decreases or increases in gross sales from previous fiscal year to current fiscal year



Respondents were also optimistic about the future growth trajectories of their companies. Ninety percent expected to increase the number of different organic food products offered in the following year, while 92% expected to increase the volume of organic ingredients purchased. None of the respondents expected to see a decline in sales in the following year. In fact, the vast majority expected sales to increase over 10% year over year. This high level of optimism amongst organic food processors was also found in a survey by the Organic Council of Ontario (OCO, 2018) in 2017 of organic and non-organic farmers and processors in Ontario. In that survey, the largest number of Ontario organic processors expected more than 20% year-over-year growth, while organic farmers expected 5-10% growth. The OCO survey also revealed that processors were actively planning to expand organic offerings.

Marketing

Most of the processors we interviewed relied on retail as their primary distribution channel, but the majority used more than one channel, including wholesale, internet, farmers' markets, food boxes and food services. Most served only the Canadian market, but the larger companies also exported food products, with the U.S. being the key, but not the only export destination.

Almost all of the respondents employed multiple marketing claims on product packaging. Companies did not believe that multiple claims contribute to consumer confusion.

Organic was not always perceived by organic food processors to be the most important claim, although for products such as baby food, mushrooms and wild rice, organic certification was thought to be a necessity for doing business. For other products, the organic label is not always considered to be a marketing asset. This was most apparent in the alcoholic beverage category. Organic wine-makers were more likely to focus on the Biodynamic claim (which is an organic claim) on their packaging, while beer makers were more interested in the "Craft" designation. Organic meat manufacturers were most likely to employ a basket of claims including "humane" and "hormone-free" in addition to organic as these claims are more likely to motivate sales.

Processors were asked to rank marketing claims based on the degree to which they were used to distinguish the

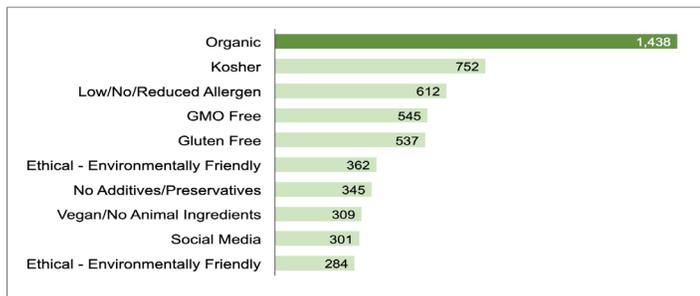
company’s organic food products from the competition. Options included organic, allergen-free, local, gourmet, quick/easy to prepare, healthy/nutritious, kosher, halal, fair trade, vegan, vegetarian and gluten-free. Overall, the organic claim was ranked as the most important to organic food companies. Second was healthy-nutritious, followed by local. Rankings are shown in Table 5.1.

Table 5.1 Perceived importance of particular marketing claims to surveyed organic food processors

Label Claim	Rank
Organic	1
Healthy/nutritious	2
Local	3
Gluten-free	4
Quick/easy to prepare	5
Vegetarian	6
Fair trade	7
Gourmet	8
Vegan	9
Kosher	10
Halal	11
Allergen-free	12

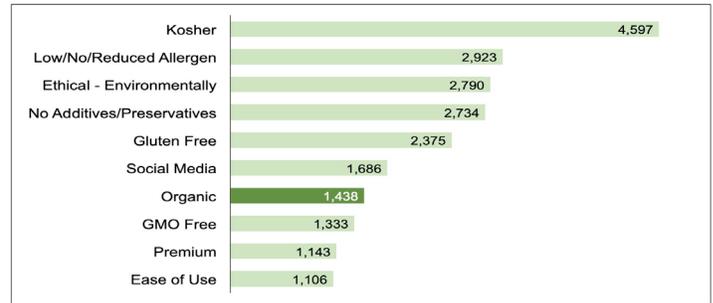
According to Mintel (2019), not surprisingly organic ranked as the top market claim on new products introduced between January 2017 and September 2018 by organic food processors (Figure 5.2). Organic was only the seventh most frequent claim used by all food processors (organic and nonorganic) during the same period (Figure 5.3). For all food processors, kosher was the most frequently used claim on new product introductions. For organic processors, kosher was second after organic (Figure 5.2).

Figure 5.2 Top 10 marketing claims on new organic product launches, 2018



Source: Mintel, 2019

Figure 5.3 Top 10 marketing claims on all new product launches, 2018



Source: Mintel, 2019

Key challenges related to organic

The survey asked respondents to rank a list of challenges in terms of the magnitude the challenge represents for the organic food processing part of the business. Ranks were averaged across all respondents and are shown in Table 5.2 with the most significant challenge ranked as 1.

Table 5.2 Perceived magnitude of the challenge for organic food processing

Label Claim	Rank
Access to capital	1
Sourcing ingredients	2
Cost of ingredients	3
Sourcing technical expertise	4
Sourcing ingredients close to the manufacturing facility	5
Quality control	6
Cost of distribution	7
Markets	8
Sourcing scale-appropriate equipment	9
Consumers willing to pay a premium	10
Complying with organic standards	11

Access to capital (1)

Accessing capital was ranked as the key challenge faced by organic food processors. A 2017 survey of all food processors in Manitoba revealed that less than 18% saw access to capital as a growth-limiting challenge. Rapidly growing business require more frequent expansions for processing space and equipment. Rapid growth also means increased outlays in marketing costs to access new markets and ingredients costs for new and expanding product lines. One organic business we interviewed detailed a

recent multi-million dollar investment in a new facility. With annual growth at around 50 percent, the company expects to outgrow the facility within five years.

Ingredient sourcing and cost (2,3,5)

After access to capital, processors ranked organic ingredient sourcing as their greatest challenge. The magnitude of the challenge was dependent on food type. Manufacturers using vegetable or maple syrup ingredients have significantly fewer difficulties sourcing ingredients than those using fruit (other than blueberries or cranberries) or grains. Almost all of the manufacturers relying on organic grain ingredients that we spoke with had implemented measures to increase the supply of ingredients. The two most common tactics were to increase the sourcing area - in some cases, food manufacturers are forced to search the world for the ingredients they want. Many of the larger processors work directly with producers to increase supply. Most focus on scaling up existing organic grain growers. Tactics include raising prices paid to producers, attending events such as organic trade shows in order to attract new suppliers, and hiring staff to develop relationships with growers. A few companies have gone so far as to hire organic agronomists who work with growers to provide free advice in exchange for a guaranteed grain supply. In the Canadian Prairie, many of the larger organic grain buyers joined together to fund a program called the Prairie Organic Grain Initiative which ends in 2019. Program goals included attracting new entrants to organic grain farming, scaling up existing organic farms and increasing production efficiency, while at the same time improving the overall quality of the organic grain. Other organic grain buyers work directly with conventional producers to help them transition them to organic, even offering transitional prices to provide a carrot to get through the transition period. These programs are showing results. For instance, acreage of organic field crops increased by 26% percent between 2015 and 2017 in the Prairie region.

High cost of ingredients was ranked as the third most significant challenge that organic food processors face. Processors understand that cost is a function of supply and demand and that by increasing supply, cost will come down.

Organic food and beverage processors also value being able to source ingredients close to their

manufacturing facilities. This was ranked as the 5th most significant challenge in the survey. Processors cited high transportation costs as the main reason to source nearby ingredients. The larger and heavier the ingredient, the greater the transportation cost and thus the urgency to build local supply.

Sourcing appropriate expertise and equipment (4,9)

Finding expert consultants who understood organic food processing was considered by most survey respondents to be a more significant issue at the start of their foray into organic food processing. With respect to knowledge acquisition, processors pointed out that there is very little published information available to help the new organic food processor. Processors tended to rely on certification bodies to help them through the certification process. Finding experts to advise them on the right processing technology and processes was more challenging. Those in a position to have the information were likely to be competitors. Most companies reported that learning usually progressed through trial and error. Some showed genuine innovation in developing appropriate processing technologies while others sought out experts in far flung jurisdictions who were not direct competitors.

Sourcing appropriate food processing equipment at the right scale did not rank as a particularly large challenge. It came in third from last in the list of challenges. This was also the arena where organic entrepreneurs demonstrated their greatest creativity.

In many cases, appropriate equipment is simply not available or if it is, it is not affordable. Alan Stewart of Horton Ridge Malt House in Nova Scotia was able to get the technical support he needed from the North American Craft Maltsters Guild, but he discovered that affordable small batch malting equipment was not commercially available. He decided to design and build his own steep tank and kiln. When the owners of Beau's All Natural Brewing Company in Ontario started out, they hand filled beer growlers due to the price tag associated with designing a custom automated bottle filling system. An owner of an organic microdairy turned to a mobile supplier of small scale dairy processing equipment found on the internet. The supplier was kind enough to make a road trip to Canada from his home base in Vermont. Almost all of the small scale grain millers we spoke with looked to Europe for small

scale grain processing equipment from stone mills to blanchers and debranners. Even with significant shipping costs, this approach made sense as North American equipment is typically built for processing at a larger scale.

Quality control (6)

Food processors told us that because their products are considered as premium by their end users who pay a high price for organic, expectations for quality are high, whether the product is an ingredient for further processing or a final product. This was particularly true for organic baby food ingredients and products. In this sub-sector, manufacturers routinely go well beyond legal requirements that specify maximum residue levels for contaminants such as pesticides, GEs, or heavy metals. The larger companies we spoke with had implemented the highest level food safety systems and tested their raw inputs for contaminants and heavy metals. Companies such as Crofter's Foods in Ontario protect their brand and reputation with state of the art in-house labs to test almost every ingredient that comes through the door. Smaller businesses were not able to afford this but were striving to improve quality control.

Cost of distribution (7)

This challenge ranked as number 7 on the list. Smaller processors were more likely to list cost of distribution as a key challenge, while the larger businesses were more likely to see this simply as the cost of doing business. Some of the processors we talked to found innovative ways to avoid the 15-35% distribution costs by piggybacking their products on trucks owned by other nearby organic processors.

Complying with Organic Standards (11)

Organic consumers want organic food to be minimally processed with no synthetic ingredients. However, they also want convenient, ready-to-eat, processed shelf stable foods. Overcoming this inherent contradiction is the fundamental challenge for organic food processors. Those who are successful at choosing the right ingredients and minimize the use of artificial ingredients, while creating a product that looks and tastes good can usually capture the heart and wallet of the organic consumer.

Based on comments from survey respondents, Canada's restrictive organic Permitted Substances

List (PSL) does represent a challenge, particularly for new organic businesses, but we found only a few cases where manufacturers decided not to produce a particular product because they could not find a food processing solution allowed in organic. One manufacturer actually told us that "The PSL acts as a filter that helps to keep competition out. If it was easy to manufacture food for the organic market, there would be a lot more competition for us."

6. CONCLUSIONS

Below we share some observations gleaned from our research and survey with organic food processors.

Growth in organic food and beverage processing outpacing mainstream processing

A report prepared for Food & Consumer Products of Canada (FCPC, Analysis Group, 2018) found that the food and consumer products sector is underperforming relative to expectations. Based on a survey of FCPC members, gross sales increases between 2013 and 2017 averaged 1.45%, which was below GDP growth of 2.12%. In our survey, with its much smaller sample size, 93% of respondents reported year-over-year sales growth over 5% and a surprising 13% reported growth over 50% (Figure 5.1). Organic food processors were also optimistic about future growth with 90% of respondents expecting to diversify their organic product offerings in the following year and 92% expecting to increase the volume of purchased organic ingredients.

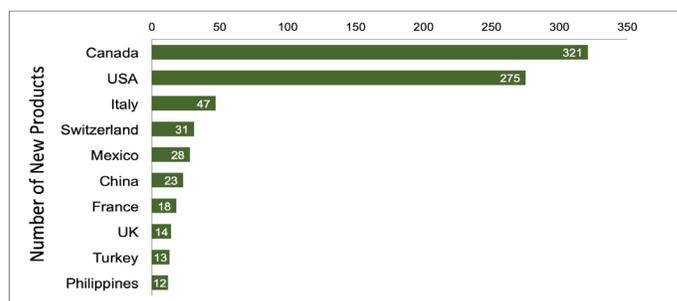
Several companies active in the Canadian organic food and beverage sector made Canadian Business's *Growth 500* list which profiles Canada's fastest growing manufacturing companies. In 2018, GreenSpace Brands, headquartered in Toronto topped the list with five year growth of 4,071%. Saskatchewan's TA Foods made the list with 245% growth over five years, as did Everland Natural Foods, Everspring Farms and Ecoideas with 170%, 245%, and 154% five-year growth, respectively.

Country of manufacture

The FCPC report also noted that most new product innovation in the mainstream food and consumer products sector does not take place in Canada and that few new food manufacturing facilities are being built in Canada. In fact, eighty-three percent of branded products sold in Canadian retail were neither developed or manufactured domestically. Two percent of products were manufactured, but not developed in Canada.

We tried to find comparable data for the organic food and beverage manufacturing industry in Canada. Mintel (2019) examined country of origin for 1428 manufactured packaged food and beverage products

Figure 6.1 Country of origin of organic packaged food and beverage products sold in Canadian retail



Mintel, 2019

with an organic food claim that introduced a new product, packaging or a product reformulation between January 2017 and September 2018. Results are shown in Figure 6.1. Twenty-two percent of the products were manufactured in Canada, 19% were manufactured in the U.S. and 3% were processed in Italy.

The processed products we found to be most and least likely to be imported versus domestically processed are shown in Table 6.1. Some are not grown in Canada or they cannot be sourced year round from Canada so it makes sense for them to be processed elsewhere. Each food represents a unique situation. In some cases, a single company can dominate the market, possibly because they were first to market with a disruptive innovation, to the extent that they discourage competition. This seems to be the case for Mott's. The company's single-serve applesauce is the only organic product in this space. Local environmental factors can also make certain products such as honey difficult to produce in Canada. For other products such as those in the ready meal category, the reasons why Canadian companies do not produce frozen pizzas or prepared frozen meals are unclear.

Organic price premium

Premiums on organic foods are declining, a factor that may be contributing to increased consumption. According to an article published in the U.S. Financial Post in January 2019 (Durbin, 2019), organic premiums were in decline, but there was wide variability in premiums for different products. Overall, the cost of organic food and beverages in 2019 was 7.5% higher than conventional. This was down from a 9% organic premium in 2014. Basics, such as milk, eggs and bread commanded some of the highest premiums. We

Table 6.1 Organic foods that are the least and most likely to be processed in Canada

Organic foods <i>least</i> likely to be processed in Canada	Organic foods <i>most</i> likely to be processed in Canada
Cane sugar	Hemp products
Baby carrots	Dairy products
Ready meals, including boxed lettuce/spinach	Maple syrup
Soy, olive, coconut oil	Flax, hemp, sunflower oil
Baking ingredients such as yeast and starch	Mushrooms
Natural and organic flavours	Roasted coffee
Fruit purées	Flours from crops grown in Canada
Apple sauce	Bone broth
Regular rice	Wild rice
Tomato-based products	Meat products
Honey	Dried fruit
Nuts	Butter
Nut butter	Chocolate
Colas	Tortilla chips
Baby food	Popcorn
Fruit snacks	

decided to undertake our own quick comparison by shopping on-line on a large chain box store's website. Organic premiums were calculated by comparing organic and conventional versions of similar products offered by the same brand. For the most part package sizes were the same, but in some cases, conventional pack sizes were slightly larger. Results are shown in Table 6.2.

There was considerable variability in the premium as measured by percentage increase in the cost of the organic product over the conventional product. One of the most surprising findings was that there was no premium for some organic products versus similar conventional products produced by the same company. We did not repeat the experiment to see if this was just a temporary marketing promotion.

Table 6.2 Premium of assorted organic fresh and processed foods sold on-line at Walmart.ca on March 25, 2019

Product (organic vs. conventional)	Premium (percentage)
Great Value granola bars	98.0
Private label pasta sauce	74.9
Heinz ketchup	72.0
Nestle Gerber baby oatmeal	66.8
Private label all-purpose flour	64.8
Cherry tomatoes	60.7
Avocados	50.4
Private Label baby carrots	35.5
Private Label single serve apple sauce	35.5
Fresh Gourmet croutons	33.7
Vita Eggs - large	30.9
White mushrooms in trays	25.0
Dairyland half and half cream	25.0
Bananas	10.9
Parents' Choice squeezable fruit baby food	0.0
Labonte organic honey	0.0
Tazo black, herbal or green tea	0.0
Happy Planet soup	0.0

Mergers and acquisitions

There has been considerable talk over the past two decades about consolidation within the organic industry. It is generally believed that small organic startups that develop innovative processes that begin to dominate sales in their category will be quickly gobbled up by large agri-businesses.

Aquisitions offer a way for large companies to gain a foothold in niche markets like organic in which growth dramatically outpaces that for mainstream brands. It is fair to ask why these companies don't simply build their own organic brands from scratch. The answer is complex, but trust and innovation are at least part of the equation. Consumers who purchase organic simply do not trust large multinationals - they see smaller companies as being more environmentally and socially responsible - factors that may play into purchasing decisions. It turns out that creating a successful,

transparent and sustainable organic brand is not all that easy, nor is acquiring the skills needed to bring new products to market using processes and products that are allowed in organic. It may actually be easier to acquire brands that already have these attributes than to try to create them from scratch.

There is plenty of evidence in the U.S. market that multinationals are acquiring local organic startups as a way to gain a foothold in the organic food processing industry. According to the Food Institute, there were 152 mergers and acquisitions in the U.S. food processing industry in 2018 and many of these involved acquisition of organic companies.

Some of the largest food multinationals have been busy acquiring organic brands. For instance, Unilever acquired Pukka Herbs, Brazilian company Mae Terra acquired Tazo and Sun Basket. General Mills is now the third largest organic business in the U.S. with a number of organic brand acquisitions. Annie's Homegrown was the company's first organic purchase in 2014 at \$820 M U.S. Other organic brands including Cascadian Farm, Muir Glen, LaraBar, Liberté and Rhythm Superfoods have been acquired since. White-Wave Foods Co., which subsequently merged with French company Danone, acquired organic brands So Delicious and Horizon. Other acquisitive multinationals include: Hain Celestial (Spectrum Organics, Earth's Best Organics, Ella's Kitchen, Imagine, Rice and Soy Dream, Celestial Seasonings, Rudi's Organic Bakery), Danone (Silk), Campbell's (Goldfish, Pacific Foods, Wolfgang Puck), The Coca-Cola Company (Honest Tea, Green Mountain Coffee, Odwalla, Suja), J.M. Smucker (Knudsen, Santa Cruz Organic), The Kellogg Company (Kashi), Kraft Heinz Co. (Classico, Capri Sun), Hershey Foods (Dagoba) and Nestlé (Chameleon Cold-Brew, Terrafertil).

Most of the organic businesses acquired by mainstream food companies have been in business for ten years or more, but many agribusinesses are actively seeking the next great company amongst food start-ups. Several have developed their own venture-capital wings in order to nurture promising start-ups. Examples include General Mills' 301 Inc. and Kraft-Heinz's Evolv Ventures.

Information about brand ownership is usually available on parent company websites but information about the parent company is rarely, if ever, available on the websites of the acquired brands, leaving most

consumers blissfully unaware that their favourite brands are controlled by multinational agribusinesses. Suja, the California cold-pressed juice company, comes clean on its website, but in a totally defensive manner it explains how it could not afford to be in business without help from The Coca-Cola Company.

Of course Canada is not immune to acquisitions and mergers in its much smaller organic sector and even has a few homegrown companies with acquisitive tendencies. For instance, Richmond, BC company Nature's Path acquired nearby Que Pasa Foods in 2012 and in 2015 it acquired U.S.-based organic cereal company, Country Choice Organic. The difference here is that Nature's Path has always been an organic company so it is not acquiring organic businesses as a way into the industry. In 2018, Ocean Spray Cranberries Inc., which dominates the mainstream cranberry industry, acquired QC-based Atoka Cranberries Inc. from the Bieler Group. Atoka processes fresh, dried and chocolate coated cranberries, including organic versions. In 2019, BC-based cannabis company, Tilray Inc. acquired organic hemp business, Manitoba Harvest from the U.S.-based Compass Group for \$419 M. Also in 2019, organic grain company Pipeline Foods, with offices in Minneapolis and Winnipeg, purchased part of Vancouver-based SunOpta Inc.'s organic grain infrastructure in the U.S. for \$66.5 M.

Despite these recent acquisitions, most of the consolidation in the organic sector in Canada has a slightly different pattern than in the U.S. Rather than being driven by multinational food companies, many of the organic food company acquisitions take place through holding companies. Unlike large food companies, holding companies do not manufacture food. Instead, they buy controlling shares in food companies, a model that confers certain tax advantages.

Some of the larger holding companies that buy Canadian organic brands include U.S.-based Treehouse Foods which counts several Canadian companies that manufacture organic food products amongst its suite of brands, including E.D. Smith (beverages, condiments, soup, spreads and other products), BFG Canada (baked goods), and Protenergy Natural Foods Corp. (soups). Treehouse's goal is to acquire food brands in diverse categories to build its capacity to compete in the private label sector. GreenSpace Brands is a holding company highlighted in the previous section as one of Canada's fastest growing manufacturing companies.

GreenSpace achieved this growth by acquiring successful smaller organic businesses such as Lovechild Organics, Kiju and Central Roast. Recently, it has expanded into the U.S. through the purchase of an organic plant-based protein company. Premium Brand Holdings is another Canadian company that controls a large number of specialty food companies. Key Canadian organic brand acquisitions include Duso's, Belmont Meats, Yorkshire Valley Farms and Canadian Organic Popcorn Co. Inc. The company also owns a number of U.S. based specialty food companies.

Innovation in the organic processing sector

Innovation in food processing can take many forms, including technological, social and environmental aspects. Innovation reveals itself in new product development, improvements to process, supply chains, packaging or in marketing and sales approaches. There is general consensus amongst business analysts that innovation is linked to success in the marketplace by giving the innovator an advantage over competitors.

Organic is often seen as being reactive against large scale disruptors in the food industry. Many consumers perceive disruptive technologies such as genetic engineering, food irradiation and cloning as socially unpalatable. Innovation in the organic sector must be compatible with the consumer values and ethics that have been described throughout this report.

We identified cases where organic food businesses are innovative in highly socially acceptable ways. The argument can be made that successful organic companies are by necessity innovative. Bringing new food products to market while overcoming the inherent technical limitations associated with a small list of permitted substances forces many companies into uncharted territory. Without access to many of the modern processing aids that mainstream food companies are permitted to use to extend shelf life, enhance food appearance, flavour and taste, processors must develop new uses for existing ingredients while developing new processes to minimally process food.

The processors interviewed for our survey did find the limited organic Permitted Substances List (PSL) to be challenging, but the limitations rarely prevented processors from manufacturing the specific products they envisioned. In fact, several processors told us that they liked the challenge and the fact that a small

PSL acts as a filter that keeps the pool of competitors relatively small.

Organic new product launches have consistently been between three and four percent of total food product launches between 2013 and 2017 (Mintel, 2018). Organic companies lead the development of new food products such as hemp hearts, unsweetened ketchup, drinkable bone broth, fermented beverages and dozens of other food innovations.

Organic processors are also ahead of the pack when it comes to innovations in packaging that reduce waste and decrease dependency on plastic. Organic beer companies are dramatically reducing the amount of water used to process beer. Companies such as Nature's Path and Riverside Natural Foods have committed to zero waste programs. Others are using green energy to power their operations, recycling spent grains for animal feed and opting for leading edge low energy processing equipment. Some organic businesses are also greening their transportation. For instance, BC-based organic distributor SPUD offers bicycle delivery on some of its routes, others such as Nature's Path provide subsidies for employees to purchase electric cars.

Organic processors are also leading the way towards more eco-friendly food packaging options. Every company we interviewed said that finding alternatives to plastic was high on their priority list. Some have already achieved this. For instance, Club Coffee has developed more sustainable coffee and tea pod systems made using compostable paper, bioresins and coffee chaff instead of plastic. Organic tea companies have found alternatives to the bleaching and plastics used in bag production. Beer companies such as Mill Street are experimenting with silk-screened applied ceramic labelling rather than paper labels. Bottles are re-fired after the inks are applied so that the ceramic actually becomes part of the glass. This reduces waste and the water and energy required to wash old labels off. Mill Street washes and reuses all its bottles and the painted labels last as long as the bottles. A European organic business is using a CO₂ laser etching technology to label fruits and vegetables without stickers.