

Organic Monitor: market consolidation raises supplier challenges

By Amarjit Sahota, Organic Monitor

10/26/2007- ***Manufacturers of organic products need to find innovative ways to keep their share of the supply chain as the squeeze of market consolidation begins, says Organic Monitor in the closing article of an exclusive FoodNavigator-USA.com series.***

Following the approval of its acquisition of rival Wild Oats, Whole Foods Market has become the single most important natural food retailer in North America. The growing power of this 'supernatural' retailer is expected to consolidate supply chains of natural and organic foods, and some suppliers risk being squeezed out of the picture.

Whole Foods Empire

Whole Foods Market was finally given the go ahead last month by the US Court of Appeals to complete its purchase of Wild Oats. The Boulder-based retailers accepted a \$565m offer from Whole Foods Market in February 2007, however the deal is only now being completed. Wild Oats operates 114 natural food stores in the USA and Canada, reporting \$1.2bn in sales in 2006.

Not all of Wild Oats stores will be integrated into Whole Foods. The retailer has announced that 35 stores - operating under the Henry's Market and Sun harvest banners - will be sold to the private equity firm Smart & Final. Another 8-10 Wild Oats stores will be closed down. The remaining 70 plus stores will slowly be re-branded into Whole Foods Market.

The Texas-based retailer was already operating 188 stores in the USA and Canada prior to the merger. Its retailer tally is expected to exceed 300 by 2010.

Supplier challenges

Whole Foods Market's expansion has not been entirely welcomed by natural and organic food companies.

With its closest rival acquired, there is cause for some alarm amongst suppliers as the retailer strengthens its bargaining power.

Natural and organic food companies have already been marginalized by mass market retailers.

Large retailers like Kroger and Safeway have come into the market and introduced organic ranges, many under their private labels. Most, like Wal-Mart, have encouraged their large conventional food suppliers to develop organic lines. Mass market retailers have thus used their existing supply chains for their organic product ranges.

With few openings in the mass market, most dedicated natural and organic food companies have continued to focus on natural food retailers. Although the USA has about 20,000 such retailers, most sales are from large supermarket-type formats. Whole Foods Market, Wild Oats and Trader Joe's are the leading chains of natural food supermarkets.

With Whole Foods Market now dominating this sector, many natural and organic food companies could be further marginalized.

Whole Foods Market, like all retailers, will seek to rationalize its supplier base. As this happens, the number of its current suppliers will decrease.

Private label producers will be adversely affected as some manufacturers of Wild Oats and related brand products will see their markets disappear. Whole Foods Market will slowly replace these lines with its own 365 brand and private label products.

Manufacturers of branded products will also be affected as Whole Foods Market streamlines its product portfolio.

It is likely to use the same suppliers of its Whole Foods Market stores for its newly acquired Wild Oats stores. Loyal and larger suppliers are likely to be favored over small suppliers.

The greater bargaining power of Whole Foods Market could also squeeze existing suppliers who will have fewer market options.

Size dominates

Big was always beautiful for the mass market retailers; it appears that large-scale production could also be favored by Whole Foods Market.

If this proves to be the case then the organic food industry will suffer another blow as smaller companies continue to suffer at the hands of large manufacturers.

The American organic food industry has already received much criticism for its large-scale producers. Just last month, the USDA imposed restrictions on Aurora Dairy because of its large dairy farms. The company operates five dairy farms in Texas and Colorado, ranging from 4-8,000 head per farm. In spite of its large farm sizes, Aurora Dairy remains a dedicated organic company.

Other sectors of the organic food industry are now almost entirely controlled by large conventional food companies.

White Wave Foods, a leading producer of soy foods and organic dairy products, is owned by Dean Foods. It was formed by the acquisition and merger of Horizon Organic and WhiteWave in 2003. Stonyfield Farm, the leading organic yogurts producer, is owned by French multinational Danone. Large food companies that have launched organic products include Unilever, Campbell Soup, ConAgra, Kellogg's, Tyson Food, and Pepsi Co.

It is hard to imagine that with consumer interest in organic foods so high, dedicated natural and organic food companies are feeling threatened.

The entry of mass market retailers has encouraged large food companies to come into the organic sector. And now, the growing bargaining power of Whole Foods Market is making some dedicated organic companies feel threatened in their tradition channels.

As supply chains continue to consolidate, how can the organic companies compete?

Survival strategies

Finding a niche is perhaps the obvious answer.

Some organic food companies will 're-find' their roots and focus on the independents. Before the days of large natural food shops and the supermarkets, most organic food sales were from small 'mom & pop' shops that focused on health foods.

Others will move forward by using the internet to set up home delivery schemes and deal direct with consumers. This is already so for organic fresh produce companies that are marketing their products as regionally produced and having 'no food miles'.

Other organic and natural food companies will re-align their business models to the changing market conditions.

Some will adopt high organic production methods to differentiate their products, whilst others will focus on new product development.

By developing novel organic and natural products, these companies are differentiating themselves from new entrants that have launched 'me-too' organic products.

The few independently-owned remaining organic and natural food companies are highly successful with this strategy. Companies like Golden Temple and Amy's Kitchen have showed that the organic spirit can and will live on!

Organic Monitor is a business research & consulting firm that specializes on the international organic & related product industries. For more information, please see www.organicmonitor.com.