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New Law Paves Way for Expanding Organic Market

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The demand for organic foods, though small, has grown tremendously in recent years. Total retail organic food sales rose from \$178 million in 1980 to \$1 billion in 1990 and reached \$3.5 billion by 1996. A greater number and variety of retail outlets are offering organic foods, and interest in producing organic products is also on the rise. Continued industry growth may be hampered, however, without agreement among organic producers, processors, and certifiers on how to define and implement organic standards.

The Organic Foods Production Act (OFPA), passed by Congress in 1990, and the regulations to implement the Act are intended to establish national standards for organic foods and a system of mandatory certification and Federal oversight to ensure truth in labeling of organic products (see box on a national definition of organic as outlined in the OFPA). Regulations will be proposed in the near future. A final rule will be published after a period of public review and comment, and

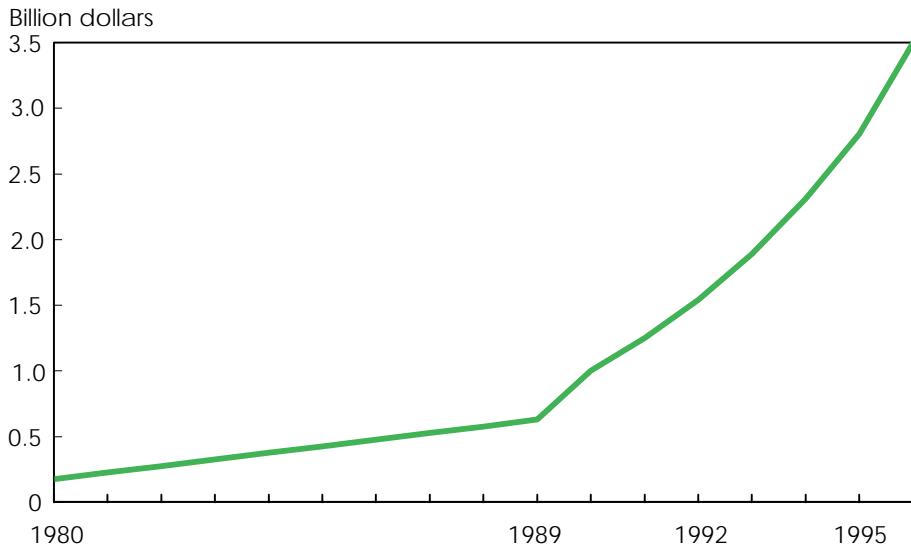
implementation of the rule will follow.

Implementation of OFPA will create the conditions for a well-functioning market in organic food. Consumers will benefit from greater confidence in the organic label, a wider selection of organic products, and the potential for lower prices as markets expand and become more efficient. Producers will benefit from increased assurance in the quality of certification, protection from fraudulently labeled products, access to international markets, the ability to market organic meat and poultry as organic, and the economies of scale

and production efficiencies that may accompany market expansion.

Organic foods are distinguished from conventionally produced foods, not by features that are detectable in the product itself, but rather by production and processing principles developed originally in Europe in the late 19th and early 20th century, and later in the United States. These principles stress production and processing without the use of synthetic chemicals, and soil fertility management using techniques that enhance biological activity in the soil such as composting, green manuring, and rotating crops.

Figure 1
Organic Sales Take Off in the 1990's



Source: Monica Emerich. "Industry Growth: 22.6%," *Natural Foods Merchandiser*, June 1996, pp. 1-39.

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If a product has a characteristic that consumers value, then in general market forces will establish a price for it and producers will supply it. Organic can be thought of as such a product characteristic. But organic and conventionally produced products look the same. Market forces cannot signal producers to supply organic products without some other means, such as labeling, for consumers to distinguish these products. Without a common definition for organic and without

enforcement of truth in labeling, the integrity of an organic label cannot be ensured and the market for organic products cannot operate efficiently. When conventionally produced products are mislabeled organic, both the producers and the consumers of organic products pay a cost. Consumers lose by not getting what they pay for, and organic producers lose when sales of their genuine products have to compete with mislabeled products in the market.

A National Definition for Organic Food

The OFPA provides some clear guidance on the necessary components of organic standards. The law:

- Requires producers and handlers to develop an organic plan of management, approved by the certifier, that contains provisions for soil fertility management through proper tillage, crop rotation, and manuring.
- Prohibits, with some exceptions, use of synthetic chemicals in production and handling.
- Prohibits use of naturally occurring toxic materials such as arsenic or lead salts that have long-term effects and persist in the environment, plastic mulches (unless removed at the end of each growing or harvest season), and transplants treated with synthetic or prohibited substances.
- Requires a period of 3 years during which prohibited synthetic materials cannot be used before a crop can be certified as organic. A 1-year transition period is required for dairy animals. Certified organic poultry

must be raised organic from 1 day after hatching.

- Provides for requiring defined boundaries and buffer zones separating land in organic production from other cultivated land, and physical separation of organic and nonorganic products in processing and handling facilities.
- Requires livestock to be fed organically produced feed.
- Prohibits use of plastic pellets for roughage, manure refeeding, feed formulas containing urea, growth promoters, hormones, subtherapeutic doses of antibiotics, synthetic internal paraciticides on a routine basis, or medication other than vaccinations in the absence of illness.
- Limits nonorganic ingredients to no more than 5 percent of the weight of the total finished processed product bearing an organic label.
- Prohibits use of packing or storage materials containing synthetic fungicides, preservatives, or fumigants.

Lack of Consistent Standards Limits Growth

The organic industry organized itself to provide protection for producers and consumers against mislabeled organic products through organic certification. Organic certification is currently voluntary in most States. According to the most complete data available to USDA's Agricultural Marketing Service (AMS), 33 private and 11 State agencies certify approximately 3,900 farms and 480 handlers in the United States. The 11 States that run their own certifying agencies are Colorado, Idaho, Kentucky, Louisiana, Maryland, New Hampshire, New Mexico, Oklahoma, Rhode Island, Texas, and Washington. In California, organic producers are required to register their farms as organic with the State, but private agencies conduct certifications. Still, not all producers and handlers choose to have their operations certified and many organically labeled fresh and processed products do not carry a certifier's seal.

Over half of the 44 agencies certify both farms and handlers, while the others certify only farms. Most certifying agencies are small, measured in terms of both the number of farms and handlers they certify and the total amount of certification fees they collect (table 1). Over three-fourths of the agencies certify fewer than 150 farms and 20 handlers each, and over half collect less than \$25,000 in certification fees annually.

Each certifying agency determines its own definition of organic and certifies organic products according to its own rules. This system may be impeding growth in the production and sale of organic foods. While there is general agreement within the industry on the principles of organic production, without a uniform standard and consistent over-

Table 1
Most Certifying Agencies Certify Fewer Than 50 Farms as Organic

Size of certifying agencies	Percent of certifying agencies	
	State agencies	Private agencies
Number of handlers certified:		
No handlers	45	50
Fewer than 20	36	34
20 or more	18	16
Number of producers certified:		
Fewer than 50	45	66
50-150	37	19
More than 150	18	16
Certification fees collected:		
Fewer than \$25,000	NA	55
\$25,000-\$200,000	NA	0
More than \$200,000	NA	45

Note: NA = Not available. Source: Tabulated from USDA's Agricultural Marketing Service data.

sight organic means different things in different parts of the country. There is no one source that consumers can go to for complete information about what constitutes organic. The high cost of obtaining this information, in terms of time and effort, may be keeping some consumers, retailers, and processors out of the market. In addition, recognition and acceptance of certification standards have been a matter of dispute in some cases among certifiers in the United States. These disputes can restrict interstate and international trade in organic products, and disrupt production of organic foods. Convincing certifiers to accept each other's standards can be a costly and time-consuming process. In the case of processed organic foods, production schedules can be interrupted and product losses can result when an end-product certifier refuses to accept another certifier's seal on product ingredients.

Further growth in markets for organic food products is also limited by current labeling restrictions. USDA prohibits the sale of meat and

poultry labeled organic because the term is undefined. This meat and poultry product exclusion prevents the development of markets for these products and restricts the development of new organic processed foods such as nonvegetarian soups and entrees.

International Trade Hindered Without Consistent Standards

Among the areas for potential expansion in the U.S. organic industry, international trade is perhaps the most significant. The European Union (EU), for example, where the principles of organic production originated, is the largest market for organic food outside the United States—valued at approximately \$1.7 billion in 1990. Organic food sales grew by 25 percent per year in the early 1990's in France and Germany—the two largest EU member states in terms of organic sales. In 1994, these two countries alone had organic retail food sales of

approximately \$2 billion, equal in size to the entire U.S. organic food market.

In 1991, the EU adopted standards defining organic produce and a system to enforce standards for the EU member states. Many EU countries also operate under their own nationally mandated standards of production and inspection for both crops and livestock. The EU is expected to adopt livestock standards in the future. Under the EU rules, imports from non-EU countries are allowed to enter the EU only when the non-EU country's national standards have been determined to be equivalent to the EU standards.

The EU has opted to withhold blanket approval for importation of certified organic products from the United States until national U.S. organic standards are in place. Thus, currently U.S. organic producers and handlers can access European markets only by obtaining specific product permissions granted to individual importers by organic regulatory authorities in an EU member state, or by using a certifier accredited by EU-recognized authorities. Obtaining EU permissions is a time-consuming and expensive process, requiring the importer to satisfy the authorities through documentation and possible site inspection that the product in question has been certified under standards equivalent to EU standards. As of early 1995, 110 import authorizations (24 percent of all the authorizations issued by EU member states) had been granted for U.S. products.

OFPA Implementation Removes Barriers to Market Expansion

Regulations implementing the OFPA will create market conditions under which the problems discussed above can be overcome. Once the final rule is published, it will establish a uniform, national definition of organic products, including live-

stock products. National standards will facilitate the opening of export markets in Europe and elsewhere, and facilitate trade between individual certifiers, thereby lowering their costs of operation. Further, the new regulations are expected to impose little additional cost on the producers of certified organic products. Certified organic producers and handlers are currently following the standards imposed by their certifiers and paying fees for certification.

Consumers of Organic Food Will Benefit

Common requirements for and accreditation of U.S. certifying agencies will create a basis for consumer confidence in the organic label. The national organic standards enforced by accredited certifiers will correct an information gap and provide buyers and sellers with consistent terminology so that the market for organic products can operate more efficiently. The uniform national standard proposed in OFPA will reduce confusion over the meaning of organic and raise confidence in the organic label by providing additional assurance of the authenticity of organic claims. The standard will allow the U.S. Food and Drug Administration, which regulates most food labeling, and the USDA, which has responsibility for meat and poultry labeling, to recognize the definition of organic as a common and usual term with a specific meaning. The OFPA regulations will allow enforcement of the standard by various government agencies for all products labeled organic, including the requirement that imported organic foods meet equivalent standards.

Consumers will also benefit from OFPA implementation through the availability of greater amounts and varieties of organic foods and through the potential for lower retail

prices. Implementation of OFPA may help overcome the reluctance of many conventional foodstores, evident from industry sales data and wholesaler surveys, to carry organic products. For example, following the Alar scare in 1989, many conventional stores hurried to stock organic produce. They just as quickly turned away from these products the following year, frustrated over the shortage of reliable supplies of high-quality organic produce. Improved marketing and handling resulting in more consistent supplies already appear to be encouraging conventional foodstores to re-enter the organic market, according to industry reports.

The appearance of organic foods in conventional foodstores will likely improve sales, as the unavailability of organic food products in these stores has been shown to be a major reason that more consumers do not buy organic food—at times more important than price. In other words, consumers are less likely to buy organic products when they have to make a special trip to another store, such as a natural foodstore or health foodstore, to find the products. Thus, consumers stand to benefit from the greater supplies of organic products in a wider selection of stores. Consumers will also benefit as more competition between conventional supermarkets and natural foodstores creates the potential for lower prices for organic foods.

Organic Producers Will Benefit From Expanding Markets

We have argued that the lack of a nationally recognized definition of organic poses a barrier to marketing organic food products in the United States and abroad. At the same time, producers who have successfully made the transition from conventional to organic production practices in the United States and elsewhere have demonstrated that

production problems, such as tackling pest and nutrient management problems without the use of synthetic chemicals, can be overcome. Thus, in the absence of barriers to increasing production, removing barriers to marketing organic products by adopting a national standard could sharply increase growth in the organic industry instead of simply enabling the current growth trend to continue. This may be true particularly for increasing exports and for sales of organic meat and poultry where no national market currently exists.

Industry data reported in the *Natural Foods Merchandiser* on meat sales in natural foodstores provide one indicator of the potential size of the organic meat market. At \$32 million in 1995, these sales represent less than 1 percent of current meat consumption. Another measure is 1994 AMS data showing that two States—New Mexico and Washington—and about a dozen private agencies certified the organic production of 3,300 beef cattle and 110,500 chickens and turkeys. Other States, Maryland and Texas for example, have moved in the direction of establishing organic livestock certification programs, also indicating a growing level of interest in this market segment.

Implementation of OFPA will help open up international markets to U.S. organic producers. The demand for U.S. organic products abroad may be substantial and may offer price premiums for organic producers. Austria, for example, expects its organic market to equal one-third of all food sales by the year 2000. Japan and EU countries report price premiums of 10 to 30 percent for organic milk and fresh produce.

According to industry sources, U.S. exports of organic products totaled \$203 million in 1994 (9 percent of total U.S. organic output), the last year for which data are

available. This figure represents a near doubling over 1993 levels, possibly as a result of import authorizations granted by EU member states for some U.S. products. Despite restricted access to the European market, the United States is still the most important non-EU supplier of organic products to EU countries. Larger growth is anticipated upon recognition of U.S. equivalency by the EU and the removal of trade restrictions on organic products.

If national standards contribute to increased domestic demand and help to open international markets to U.S. organic products, they would provide opportunities for current producers to expand the scale of their operations as well as incentives for more producers to enter the market. Greater organic production would also provide an incentive for input industries to develop new technologies which would lower costs for organic producers. Input industries producing for the organic market could achieve economies of scale which could also reduce input costs.

Along with industry growth we can expect the demand for better information about the production and marketing of organic products to also increase. Currently, the retail food industry does not keep separate data on organic and conventional processed food product sales, making it very difficult to track

organic food sales, especially in conventional foodstores. Instead, organic products are lumped together with conventional products of the same type, such as frozen vegetables or baked goods. For example, grocery scanner data often do not include information on whether a product is organic in the item descriptions. With nationally recognized, uniform organic labeling, processed organic products will acquire commercial, standardized item descriptions similar to those used by the food industry to identify conventional products. These descriptions will make sales information more accurate and accessible and improve the efficiency of marketing organic products.

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