

In: Deciphering Organic Foods

ISBN: 978-1-53610-517-9

Editors: I. Kareklas and D.D. Muehling © 2017 Nova Science Publishers, Inc.

*Chapter 5*

## **SELLING ORGANIC FOODS THROUGH CONVENTIONAL RETAIL STORES**

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### **ABSTRACT**

Organic foods, once produced and consumed in small amounts by specific groups of producers and consumers, have now become mainstream, and nearly all conventional retail stores have some organic food items in their shelves. Such conventionalization in the organic food industry, from production to retail, initiated confusion among producers and consumers alike. This chapter reviews existing literature on the impact of conventionalization of organic foods on the industry itself. It examines the reasons for large corporate businesses to become involved in the organic food industry and what potential consequences such conventionalization may result in. Potential market power, development of organic certification system and growth of international trade made organic food industry lucrative to large corporate businesses. The potential impacts, however, are mixed- from increasing consumer shopping convenience, knowledge and affordability to compromising organic integrity and endangering small organic farmers.

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**Keywords:** organic foods, retail marketing, conventional retail, mainstream retail of organic foods

## INTRODUCTION

Organic foods have traditionally been produced in small quantities primarily by family farms and sold to specific group of consumers either directly or through specialty grocery stores or small cooperatives. Specialized farms producing organic food commodities had a principal objective to address the demand for consumers with particular preference toward organic foods. In that, both producers and consumers had specific interests creating a separate niche market for organic foods. Situations have changed over time and organic foods have entered into the mainstream conventional food marketing systems. Today, nearly every conventional retail chain store (supercenters, supermarkets and nearly all grocery stores) carries at least some organic food items in its shelves. Many independent and large restaurant chains have started offering prepared organic foods to their customers (Pinard, et al. 2014; Hanks and Mattila 2016) and fast food chains have not stayed behind jumping onto the bandwagon (i.e., Amy's Drive Thru, Organic Coup, etc.) (Guthman 2003; Woodbury and George 2014; Grizzle 2015; Peterson 2015). Even organic candy, snacks and beverages, including alcohol, have become popular among younger generations (Candy and Snacks Today 2012; OTA 2015). Although organic foods remain in a separate food category, the marketing system became so integrated into the mainstream that the distinction between the markets of organic foods and non-organic foods has become fuzzy. The largest organic food retailers in the USA today are Wal-Mart, Costco, Whole Foods Market, Kroeger, Traders Joe's, Super Target and Safeway. Such involvement of large corporate retailers has made the organic food retailing corporatized (Clark 2007; Hermansen et al. 2012; EcoNexus 2013; Johnson, 2013; Gupta, 2014) and has involved modern technology for processing, distribution and retailing. On the retail side, promotion through conventional means, i.e., shopping flyers, mass media promotion (newspaper, radio, television and magazine advertisements), and digital promotions (on-line (Zebrowski 2014) and social media (Pechrova et al. 2015)) have become common.

The conventionalization of organic foods is not limited to retail outlets only; it has captured nearly every aspect of the organic industry - production,

processing, labeling, distribution and retailing. Perhaps the most consolidation and corporatization happened in the processing sector, creating specialized brands and further assisting the conventionalization of the retail sector. In this chapter, we focus on the retail sector only. Large national and transnational companies have taken over the retail sector of organic foods (Clark 2007; Johnson 2013; Gupta 2014; Courtemanche and Carden 2014). Safeway in the U.S. and Loblaws in Canada, for example, created their own organic brands, 'O Organics' and 'PC Organics', respectively. This involvement of large scale multinational companies or corporatizations in the organic food industry has raised concern, both in support and in opposition. On one side, conventionalization of organic food retail industry is being challenged for its impact on the central core of the existence and integrity of organic's distinct nature (Gupta 2014) – small production, specific consumers, local trading and separate from conventional foods. The argument behind this claim is that the quality of organic foods has been put into question despite regulatory developments. Even the survival of small organic producers and sellers has become challenging. In response to the large corporatization effect, the Whole Foods Market, the leading chain of specialized organic food sellers in the U.S., is considering introducing organic food in its low-cost discount stores (Sahota 2016). On the other side, conventionalization claims to make the organic food industry more popular, easily accessible to wider range of consumers, more profitable to producers and indeed further affordable to consumers who otherwise would not have been able to pay (Hausman and Leibtag 2007; Basker and Noel 2009; Blanc 2009; Johnson 2013). It brings the organic food market from a small niche to a mainstream market and allows potential for unlimited growth.

Organic foods are no longer products of specific groups of producers nor meant for particular groups of consumers. At present, these are available in most conventional retail stores at reasonable price premiums, and many consumers have become attracted to organic foods, which has resulted in a domino effect in the market (Henryks and Pearson 2011; Islam 2014). Although there are variations among consumers, in general, a vast majority of consumers buy a mix of organic and conventional foods (Islam 2013, 2014). Nearly 35% of the conventional store shoppers buy at least some portion of organic foods, with only 1.7% buying completely organic (Islam 2014). Adding specialized organic food shoppers, as nearly 100% of them buying organic, such proportion is expected to be much higher on an aggregate level – perhaps nearly two-thirds, as is reported in Monk et al. (2012). Again, this

share changes toward the organic side, at least in part, due to the domino effect and depending on consumers shopping characteristics – demographics, buying habits, shopping convenience, product range and shopping alone or with others (Henryks and Pearson 2011; Yadav and Pathak 2016). Aside from these, food quality and price play important roles in consumers' purchasing decision (Batte, et al. 2007; Lulfs-Baden et al. 2009; Richards et al., 2011; Ortega et al. 2015; Ankamah-Yeboah et al. 2016).

The nearly five-fold increase in world-wide organic food market over a 15 year period – from \$18 billion in 2000 to \$59 billion in 2010 (Willer and Kilcher 2012) to \$80.0 billion in 2014 (Willer and Lernoud 2016) – draws considerable attention to seek answers on what are possible driving forces behind this unprecedented growth. Many consumers switched from conventional to organic foods despite substantial premium prices for organic foods. Organic foods are often sold at much higher prices – from as low as 10% to nearly 150% price premiums – although a slightly lower price for some organic foods compared to conventional foods are also found on rare occasions (USDA 2016). Several possible reasons have been identified for switching to organic foods from conventional foods among which concerns about human, animal and environmental health is the foremost credited (Hutchins and Greenhalgh 1995; Davis et al. 1995; Williams and Hammitt 2001; Lea and Worsley 2005; Smith and Paladino 2010). Ozguven (2012) tested four motivation factors for buying organic foods – food quality motive, price motive, health motive and food safety motive – and found all of those are statistically significant contributors towards buying organic foods. Although consumers express different reasons for consuming organic foods, i.e., health, environment, animal welfare (Bourn and Prescott 2002; Fotopoulos and Krystallis 2002; Makatouni 2002; Zanolli and Naspetti 2002), extensive sales through conventional retail stores is considered an important reason for the rapid growth of organic foods (Hartman Group 2008; Bezawada and Pauwels 2013; Trauger and Murphy 2013). Conventionalization in all sectors of organic food industry not only increases efficiency in production, transportation and distribution, but also makes organic foods accessible to a broader range of consumers with (perhaps) lower prices by taking cost advantages in all fronts. It also makes information on organic foods easily available to the entire consumer pool. Access to information on organic foods is now as easy as that on any conventional foods, which makes the average consumers well aware of claimed benefits of organic foods. However, with the promotional influence of conventional retail stores comes increasing concerns

about maintaining integrity of the organic foods. Several areas of vulnerabilities have been identified – purity of organic content while producing, transporting and retailing on a large scale, maintaining integrity of organics when production happens over jurisdictions where regulatory regimes are less effective, and the like. It has also been claimed that this conventionalization is putting original small organic producers, as well as consumers at risk, as small producers cannot compete with large corporations due to the absence of cost advantages, and consumers cannot forfeit the convenience and price advantage of buying less pure organic foods from conventional retail stores.

The increased market share of organic foods is primarily thought to be demand driven and conventionalization is often given some credit for that. Irrespective of whether conventional supermarkets and grocery stores deserve credit or discredit for influencing the organic food industry, it is a fact that a vast majority of organic foods are now promoted and sold through conventional supermarkets and grocery stores, and the proportion is likely to continue to increase. However, the impact of conventionalization on the organic food industry – production, processing, distribution and retailing – has been examined focusing on specific aspects and from biased perspectives. For example, Johnson (2013) defended the involvement of large corporations in organic food industry, but Gupta (2014) advocated against that. Comprehensive reviews on the impact of conventionalization of specific sector of the organic food industry are scanty. This chapter is expected to contribute to such literature especially focusing on retail sector and from an unbiased perspective. However, before making any conclusive remark, we need to understand the evolutionary process of involvement of conventional retail stores in the organic food industry, what the impending motivating factors are and what their potential influences on the organic food industry would be. As mentioned earlier, although conventionalization happens in every sector of the organic food industry, our focus will only be on the retail marketing sector. Accordingly, the next section of this article will address the evolution of conventionalization of organic foods. The third and fourth sections of this chapter will address reasons for involvement of conventional retailers in organic food sales and the impacts of conventional retail stores might have on the organic food industry, respectively. These will be followed by a case study of Loblaw's involvement of organic food retailing in Canada followed by a section on concluding remarks.

## EVOLUTION OF CONVENTIONALIZATION

Originally agricultural and food production systems were entirely organic dating back to the ‘Neolithic Age’ and practiced by early civilizations (Behera et al. 2012). Production systems were not intensive, and no chemical fertilizer or pesticide was used. Productivity was certainly not as high as it is today. With the increase of population, pressure continued to increase production. At the turn of the 20<sup>th</sup> century, population growth and increased incomes led to increased demand for food. This resulted in two changes in agricultural production. More and more land was brought under cultivation and substantial efforts were made to increase productivity. Scientists sought for ways to boost production by improving soil productivity and by mitigating factors that reduce production. Adding chemical fertilizers to increase productivity and applying chemical pesticides to fight against insect-pests and weeds were the first to be implemented. Increasing demand for intensive production led to the development of technologies for accumulative agricultural productivity even further involving expanded use of high yielding varieties, intensive production systems, and extensive use of chemicals, fertilizers, pesticides and hormones (used in the cattle industry). This eventually led consumers to become concerned about foods they consume. Environmental and health conscious producers started to examine sustainability of their soil productivity. Europe was first to respond – biodynamic agriculture in Germany in 1920s, organic farming in Britain in 1940s and biological agriculture in Switzerland around the same time. These are commonly considered precursors of what is currently known as organic farming (Colom-Gorgues 2006). Similar developments also happened in the U.S. and Japan either at the same time or immediately after. Primary concerns for such a movement were loss of soil fertility, decline of crop variety, low quality food and livestock feed and emergence of rural poverty (Kuepper 2010). A soil management strategy of mitigating all soil productivity factors, called humus farming, also emerged at this time, but the term ‘organic agriculture’ was first used in a book published in 1940 entitled “Looking to the Land” by Sir Northbourne, an agricultural scientist at Oxford University.

Although organic farming is thought to have originated from soil management, it eventually acquired several different dimensions keeping principal focus on foods. Increased use of broad-spectrum chemical pesticides and fertilizers started threatening fish and wildlife species, and environmental activists became vocal against random use of such chemicals during the 1970s and 80s. As a result, instead of focusing purely on soil management, organic

farming started concentrating on a broader context, including environmental health benefits (Falguera et al. 2012) and food safety (Hutchins and Greenhalgh 1995; Davis et al. 1995; Thogersen et al. 2015).

Today, different consumers choose organic foods for different reasons. Producers, processors, distributors and retailers have responded to consumers' demand by providing organic and related foods using various names – organic, natural, eco-friendly, healthy, etc. etc. Organic food production became a movement within a small section of producers who were concerned with conventional intensive agricultural production and use of chemical fertilizers. Such a movement was small – a few farmers growing agricultural crops free from chemical fertilizers and distributing those to their selective consumers either directly, or through cooperatives or through specialty grocery stores. The movement gained momentum when further refined chemicals, i.e., antibiotics, growth hormones and GMO's came into the picture. This intensified health concerns among consumers that led to increased demand for organic products, and thus encouraged conventional retailers to take part in providing the product.

Developing differentiated foods based on production and processing procedures provides consumers a much wider choice, but organic remains the principal component and the market, for it has developed more than others. Producers produce and grocery stores sell food products marked as 'organic' and 'natural' to obtain premium price and sales advantage over their conventional industrial products. Some claim that local producers and small retail stores also obtain some share of the premium (Oberholtzer et al. 2014). Alongside, direct sales of food products by small family farms through farmers' markets became popular as well. The common notion was (and perhaps still is) that foods produced by small farmers are primarily for local consumption and are free from chemicals and other contaminants. So, organic foods are supposed to be healthier than conventional, as the former are produced organically with less intensive production techniques, maintain soil productivity and use no chemical inputs. Many other similar reasons, including environment, and human and animal health, have been added to justify organic agriculture and consumption of organic foods (Behera et al. 2012). Critics of such production system, however, did not stay behind bringing skepticism of such benefits (Reganold and Wachter 2016).

Despite the skepticism and reservation of some producers and consumers (Jahn et al. 2005; Reganold and Wachter 2016), organic agriculture continued to expand through the increase in production and consumption of organic foods (Behera, et al. 2012). The importance and attention to organic

agriculture resulted in national and international organizations being formed—the Research Institute of Organic Agriculture (FiBL) was established in 1973 and the International Federation for Organic Agriculture (IFOAM) was formed in 1972. Many national associations of organic producers and consumers were formed around the same time as well. With the expansion of production, consumption and the formation of national and international associations came many positive changes in terms of production practices, technology used, regulatory framework and the formulation and implementation of policies. At times production and consumption of organic foods were perceived as anti-conventional, anti-traditional and nearly a cult-behavior, and marketing channels were away from traditional market structure. Participants in this process – both producers and consumers – were isolated and contained within their own boundary, forming a strong belief that hardly matches with the general populace. Producers were small not only in size of production but also in numbers, and so were their consumers. Conventional marketing system with clear distinctions of market participants, i.e., producers, wholesalers, retailers and consumers were absent.

No one knows exactly when conventional retail outlets actually first became involved in retail marketing of organic foods, although some sporadic references are found. In Belgium, one conventional store first started offering organic bread and some products in 1985 (Aertsens et al. 2009). In the late 1990s, national standards of organic foods were initiated in the U.S., providing rules and guidelines for organic food production, processing, distribution and retailing. Large national and multinational companies saw opportunities for them and became interested in taking over independent operations (Pratt 2012). In fact, large corporations began integrating organic foods in their operation – production, distribution, processing and retail – one after one, and as such corporatization of organic foods did not happen only in retail industry, it happened in every subsector of organic food industry, from production to processing to distribution to retail. The most prominent alliances and acquisitions can be seen in North America in the processing sector where few multi-national companies grabbed many independent operations and offered their own brand of processed organic products (Howard 2009, 2009a; Snyder 2014). Similar acquisition by large companies happened in distribution sector. For example, SunOpta Food Group, a leading distribution company of certified organic foods in the U.S., acquired several Canadian organic brands, i.e., Pro Organics, Simply Organic, Supreme Foods, etc. (Pratt 2012). A few large companies, i.e., Cargill, ConAgra, Dean Foods, General Mills, Heinz, Kellogg and Kraft have acquired the leading organic retail brands (Pratt 2012).

In the U.K., Sainsbury's, a conventional food retail store, started stocking organic foods in its shelves in 1985 and by late 2000s, it was carrying over 900 organic products (Jones et al. 2001). Tesco, the largest food retailer in the U.K., incorporated organic food items in its shelves during late 1990s, and by 2000, it started carrying over 700 products. Around the same time, Marks and Spencer, ASDA and Waitrose also began stocking organic items in their shelves. Many of these conventional stores name their organic retail areas as "Organic Village", "Organic District" or "Organic Nations" to increase visibility of the products (Jones et al. 2001). Similar movement by conventional stores started in other parts of the world as well, especially other parts of Europe and North America. In the U.S., Whole Foods, a company established in 1980 to provide natural foods to their customers, added organic foods in its shelf in 2002, and in the following year, it became America's first certified organic food retailer. For several years, it remained the principal organic grocer, and was recently bypassed by several large conventional supermarkets. Distribution companies also played a key role in promoting organic foods to the conventional retailers. Albert's Organics, a leading organic food distribution company in the U.S. established in 1982, also provides organic foods to many retail stores in continental U.S. Costco first introduced Organic Baby Mixed Greens in its stores in the U.S. from Earthbound Farm in 1997 and has been growing since then. Currently, 5 to 15% of its grocery items are organic. It introduced organic foods in its stores in Canada much later, in 2008, through the introduction of organic Kirkland Signature tortilla chips. Such conventionalization has happened all over the world, though not exactly at the same time or at the same pace everywhere. Despite difficulty in finding a point of origin of conventionalization, it has now become the reality in the entire organic food marketing system – from field to plate – production, processing, distribution, retailing and consumption.

Conventional retailers came to organic food retailing in various parts of the world, primarily in Europe and North America, resulting in a typical trend of consolidation and integration of the entire agricultural industry – production, processing, distribution and marketing. In the production sector, the total number of farms is decreasing and the average size of individual farms is increasing. Similarly, entire processing and distribution systems are dominated by a few large national and multinational firms. In the retailing sector, the consolidation system is slightly different, as there exists retail chains, independent grocery stores, cooperatives and others.

It is an acceptable fact that consolidation has its advantages and disadvantages. A commonly observed advantage is increased accessibility

noticed in supermarkets or one-stop shopping centers. The demanders (shoppers) have increased convenience of saving multiple trips for various goods and buying all they need from one place at one trip. Consolidation also makes the business bigger – either integrating vertically or horizontally or even both vertically and horizontally – allows them to obtain cost advantage through economies of scale and in turn sell products at lower prices. Companies, being bigger, can afford to invest in research and new product development, offering consumers more choices. On the other hand, consolidation often results in less competition. And less competition means more market power to sellers increasing producer surplus or profit at the expense of consumer welfare. What is more interesting here is that consolidation results in concentrating producer surplus within a small number of producers and eliminating or reducing producer surplus of small producers. This puts the total social welfare into question.

### **REASONS FOR INVOLVEMENT OF CONVENTIONAL RETAILERS IN ORGANIC FOOD RETAILING**

From a neo-classical microeconomic perspective, the primary motive of conventional retailers to market organic food products is the profit margin. Organic foods are almost always sold at a substantially high premium prices, and any price premium is expected to contribute, at least to some extent, to profit even after accounting for relatively high wholesale prices to pay to suppliers. Since a vast majority of organic producers are small, their production costs are often higher compared to conventional food production, as the former cannot use high-productive inputs (synthetic fertilizers, pesticides and other chemical inputs for intensive production) and large-scale mechanization, do not have sufficient power in input market, and cannot experience economies of scale in production, storage and trade. Hence, the entire organic industry (at the production and consumption) is at a competitive disadvantage compared to the conventional food industry.

A higher price for organic foods relative to conventional foods is justifiably acceptable to both consumers and producers. Consumers of organic foods are ready to pay higher prices for their preferred food products as organic foods satisfy certain characteristics that conventional foods do not. Consumers also in general recognize that organic foods require relatively higher production costs. The production of organic foods costs approximately

30% more than that of conventional foods (McLendon 2010). The retail price premium, however, is often very wide and may range from as small as 0% on rare occasions to as high as nearly 200% (Islam 2013, 2014), which shows a clear possibility of earning high profits, at least in part, through retail price premium (Lukic 2011). Glaser and Thompson (2000) reported that price premium of organic milk can be as high as 103%, although a later study shows 64% (Schrock 2012). Islam (2014) observed that on average organic foods are priced at approximately 69% higher than conventional foods. Such increase is, however, not consistent across retailers nor across food products, and the range may vary from as low as close to 20% to as high as nearly 200% (Islam 2013, 2014). Differences in prices also vary from one period to another, although the variation across time is not as extensive as that across products and stores.

Conventional retailers make concerted effort to understand behaviors of both consumers and producers. Consumers are motivated to pay premium prices for the same two broad reasons – higher production costs deserve higher prices and better quality products warrant higher charges. The vast majority of consumers strongly agree that organic foods, relative to their conventional counterparts, are healthier, have better nutritional value, are chemical free, safe, natural and environmentally friendly, have more human touch and support local small farmers (Islam 2014). Since meat, dairy and cereal products are the types of foods people are inclined to buy organic, it makes sense for conventional retail stores to make an effort to obtain a slice of the pie. Consumers preferring organic foods are not very price sensitive (Monier et al. 2009) and pay higher premiums than what they actually want to, as reflected in their stated willingness to pay and what they actually pay (Islam 2013, 2014). It should also be noted that only a small proportion (approximately 2%) of consumers exclusively buy organic and the vast majority buy a mix of organic and conventional. Conventional retail stores, keeping organic and conventional foods side by side or aisle by aisle not only encourage organic buyers to have the option, but also inspire non-organic and price-sensitive buyers to experience relatively cheaper price for their preferred items, making it convenient for the customers. Since service convenience influences customer satisfaction (Berry et al. 2002; Colwell et al. 2008) and in turn increases customer loyalty resulting a higher repeat purchase, it can easily lead to higher sales in both conventional and organic foods, and of course, an increase in sales is expected to contribute to bigger profit, a motive consistent with any business.

Large conventional retailers can afford to supply organic foods at relatively lower prices than small specialty organic retailers due simply to the sheer volume and economies of scale of the former- in purchasing, transportation, storage, selling and promoting. Wal-Mart at times undertook an effort to sell organic food products with only 10% premium price (Green 2008) primarily based on the expectation that many of its large suppliers (Kraft, Heinz, General Mills, etc.) will come up with their version of organics and take advantage of economies of scale. Although this was an ambitious goal, and the realization of such a goal is hard to find, the process continues with more and more organic foods in conventional retail stores, which is often dubbed as ‘corporatization’ of organic foods. Nearly all supermarkets, discount stores and large box stores have organic foods. At times, Wal-Mart was expected to take over the largest organic food chain in the US., Whole Foods. Recently Costco, in some locations, is expected to do the same, surpassing the amount of organic food sales by Whole Foods (Fitzpatrick 2015). Costco has its own organic brand, ‘Kirkland Organic,’ and its hundreds of organic products include both human and pet food. Loblaw Companies Limited, Canada’s leading food and pharmacy leader, operates grocery stores across the country in the names of Superstores, Extra Foods, No Frills and others, and incorporated its own President Choice organic brand in 2001 with organic dark chocolates. Today, it has 282 President Choice labeled organic products in its shelf. It also carries organic foods from many other brands, devoting several isles for organic foods. Furthermore, it has launched a complementary brand named ‘Free From,’ to mean products free from hormones and chemicals.

Large conventional retailers have cost advantage from imported organic food products or their organic ingredients from geographic regions with low production cost, i.e., China, India, Africa or Central America. Many of Wal-Mart’s organic ingredients are imported from China, where organic certification systems are not as credible as in Europe or North America. Critics of conventionalization of organic retails cast doubt on the integrity and purity of the imported organic ingredients or products due to lack of enforcements. Although certification systems on paper and formal bodies to implement such systems may exist in most developing countries, their effectiveness is often dubious. To combat such a doubt, developed regions, especially the EU and North America, require all suppliers of organic foods and organic ingredients have to be certified. USDA has developed its own requirements for accepting imported foods as organic and has made many bi-lateral agreements, especially with developed countries such as, Canada, the EU and Japan.

The reasons for involvement of large conventional retailers in marketing organic foods are multifaceted. However, for a concise presentation, these can be provided in three major subheadings – sufficient market power, development of certification system, and bilateral equivalency arrangements to facilitate international trade. The following is a brief exposition of these three broad reasons.

### **Market Power**

An easily conceivable reason for the incorporation of organic foods in the conventional retail stores is the market power conventional retail stores enjoy over their suppliers (producers and wholesalers), and their competitors like specialty organic retailers. It may seem apparent, at least at the initial stage, that conventional retail stores put organic food products in their shelves to differentiate themselves from other stores in terms of honoring social responsibility and of providing consumers alternative opportunities for product variety. However, conventional retailers, especially ones with sufficient vertical integration, capture market power from both sides- suppliers and consumers- due primarily to their scale of operation or volume of sales. Organic food market is mainly demand driven and suppliers (producers) have limited opportunity to exercise bargaining power, as they produce products with limited shelf-life and have to sell to retailers or whole sellers within a relatively short period of time. Direct sale through farmers' markets is costly and still very small, despite a relatively huge growth of farmers' markets in major urban centers. Conventional retail stores can often exercise their monopsony power over small producers, as they have large consumer base, effective promotional machines and capacity to absorb constantly evolving new products. Most retailers charge slotting fees from their suppliers principally for new products (Marasteanu et al. 2014). Organic food has a growing market and over a thousand new organic food products are coming into the market every year (Dimitri and Oberholtzer 2009), which are subjected to slotting fees. For large grocery retailers, such fees can add substantial advantage over smaller local organic grocers, cooperatives or farmers' markets.

Conventional retailers may have to share some of their buying power with large processors, especially for processed organic foods. Several (nearly all) large multinational food processors entered in the organic food processing market and consolidated through buying smaller organic food processing

companies. Kraft, Heinz, Dean Foods, General Mills, Kellogg, etc. all have created their own brand and/or acquired smaller organic food production and processing companies (Green 2008), concentrating organic food processing sectors within a handful of companies. Such large processing companies are involved in organic food processing primarily in response to the demand from large retailers – Walmart, Trader Joe’s and Safeway in the U.S., and Walmart, Safeway, Sobeys and Superstores in Canada.

Many retailers include organic foods in their shelves for strategic promotional purposes specially to project an image of perceived values to their customers, such as high quality foods, environmental friendliness and social responsibility (Aertsens et al. 2009). The strategic inclusion of organic products may not directly increase sales, but improve the image of the retailers to potential customers who otherwise would not have come to these stores. This is more so for conventional discount stores, as they can attract consumers of upper middle class and eventually may have an increased sales volume. A declaration of willing to take low margin for organic foods, as the one advertised by Walmart, serves a double purpose- it attracts price-sensitive lower-income buyers and middle-income quality-sensitive and environmentally concerned customers.

Increasing concentration of organic food retails within a few large corporate chains creates an oligopoly that is often considered problematic, as it generates inefficiency, decreases social welfare and leads to unfair income distribution among retail agents (Chalil and Ahmadi-Esfahani 2005). Both sides of the organic food industry face market pressure. Aside from the oligopoly power of the large retailers, increased concentration in the food processing and distribution industry exerts monopsony power on producers which are relatively small (Roger and Sexton 1994). Principal reasons for such monopsony power are the smaller organic producers with their limited ability to independently market or transport to other processors and distributors. On one end, organic farmers face monopsony (or oligopsony to be more accurate) pressure from their buyers and on the other end, organic consumers face oligopoly pressure from their retailers. So, increased concentration of processors, distributors and retailers make both organic producers and consumers worse off. Conventional retail stores also have substantial market power on its own from the cost advantage of economies of scale, as they can lower their transportation, shelving and storage costs due simply due to their large volume of operation.

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## Certification System

An obvious reason for increasing involvement of conventional retailers in the organic food industry is the establishment of certification systems. Although certification systems differ from country to country or from jurisdiction to jurisdiction, and a global common certification system is unlikely to be implemented (Sawyer et al. 2009), nearly every western country has its own organic food certification systems, either government sponsored or through the self-regulation of the industry. In the U.S., Congress passed the Organic Foods Production Act in 1990, under which certification agencies were established to certify organic foods following specific methods and procedures spanning from production to retailing. Subsequent to the act, the United States Department of Agriculture (USDA) developed a national standard through the establishment of three categories – ‘100 percent organic’ (contains only organically produced ingredients), ‘organic’ (contains at least 95% organically produced ingredients) and ‘made with organic ingredients’ (contains at least 70% organically produced ingredients). This certification system is an indication of quality signal (Jahn et al. 2005) and provides assurance about the authenticity of foods to consumers (Trauger and Murphy 2013). In Canada, the organic certification system is monitored by the Canadian Food Inspection Agency (CFIA), which allows agencies to have the authority to certify foods as organic and use the seal. Nationwide, CFIA has approved about 20 organizations to independently certify food products as organic based on the guidelines provided. Similarly, in Europe, the EU ensures that the food carrying certified organic logo follows rules and procedure imposed by the EU for production and trade. ECOCERT, a private international certification body, delivers certificates based on the regulations, procedures and guidelines provided the EU. It is also accredited by the certification body of the U.S. and Japan, the USDA and MAFF, respectively.

Certification system allows organic food products to carry a label containing the organic logo of the country, which provides organic integrity of the food commodity. Such a label, irrespective of global, local or private, increases organic perceptions among consumers and companies can add value to their own brands by adding organic labels and as a result can complement profit. Bauer et al. (2013) reports that private organic brands are more effective in adding profits than global and local brands. The production of private brands of organic foods by many large retailers clearly attests that.

## **International Trade**

Expanded certification systems and bilateral equivalency arrangements (also termed as agreements) of organic certification encouraged international trade of organic foods which eventually aids large multinational firms to become involved in the production, processing, distribution and retailing of organic foods. These involvements of large retailers further accentuate international trade of organic foods, which adds another dimension of questions about the integrity of organic foods. Today, North America and the EU, the regions consuming the largest amount of organic foods, receive their products from nearly every corner of the world. This has been facilitated primarily by the existence of certification systems and the bi-lateral equivalency arrangements eliminating time and costs of double certification. The Canada-U.S. organic equivalency arrangement is the first of its kind, which respects the conventional trade agreements, increases efficiency, reduces the cost of transportation and eliminates double certification, although many organic foods imported from the U.S. to Canadian grocery stores carry both the Canadian and U.S. organic logo to project their credibility as organic. Canada currently has bi-lateral equivalency arrangements with Costa Rica, the EU, Japan, Switzerland and the U.S. (CFIA 2016). Similarly, the EU has an equivalency arrangement with Argentina, Australia, Canada, Costa Rica, India, Israel, Japan, New Zealand, Tunisia, Switzerland and the U.S. (EC 2014).

The implementation of organic equivalency arrangements has contributed substantially to the flow of organic foods from one country to the other. The U.S. organic export has increased by 58% within four years of implementing such an arrangement with the EU and Canada, from 2011 to 2014 (Jaenicke and Demko 2015). The demand for organic foods outstrips supply in most developed countries, particularly in North America, the EU and Japan, and importation of organic foods becomes necessary. Canada produces a small amount of organic foods and it imports a large quantity largely from the U.S. It also imports organic foods from Chile, Mexico, China, Italy, Germany and several other countries. The U.S., though imports organic foods from around the world as a net importer, exports organic foods to many countries including Mexico, Canada, Israel, Taiwan, UK, Japan, India, UAE, Guatemala, Finland, Colombia, Hong Kong, South Korea, Australia, Saudi Arabia, Thailand and many other countries (Jaenicke and Demko 2015). Imported organic foods, irrespective of where from, are considered less valuable than domestically produced organic foods (Hempel and Hamm 2016) and are typically sold at

lower prices. An additional factor contributing to increased import of organic foods to the U.S. is the farm subsidy to the conventional farmers, which makes organic farmers experience relatively costlier production process than conventional farmers.

### **IMPACTS OF CONVENTIONAL RETAILS ON ORGANIC FOOD INDUSTRY**

The involvement of conventional retail stores on organic food business has been contentious, as it has been often perceived as deleterious as well as beneficial. It can potentially influence every sector of the industry- production, processing, distribution and retailing. However, the interlink with the processing and distribution sector is more of the opposite, as these two impact more on retail sector rather than the other way around. The impact on the retail sector itself and the production sector would be more prominent. The effect on the retail sector comes through the influence on consumers' perception, belief and confidence in the entire retail sector-which may come from conflicting reasons as it provides certain degree of positive impetus through convenience, easy access, advertisement and promotion and at the same time encourages consumers to be more suspicious about the integrity of organic foods. Although private and imported brands are more profitable for retailers, their integrity as organic foods are in doubt in most consumers' mind. Traditional organic producers get expanded marketing opportunities for their products through the conventional retailers but at the same time face unbalanced competition with large corporate vertically integrated producers.

While measuring impacts on the entire retail sector, we need to understand consumers' behavior on buying organic foods and how that influences the industry as a whole. Consumers commonly perceive organic foods as healthy, nutritious, chemical-free, ethical, tasty, environmentally friendly and as having a human touch (Gottschalk and Leistner 2013; Trauger and Murphy 2013; Islam 2014; Mohamad et al. 2014). In general, consumers' decision to buy organic or not depends on several factors in which price, quality, availability and social influence are predominant (Monier et al. 2009; Gottschalk and Leistner 2013). How these four factors are affected by the participation of conventional retail stores may indicate at least part of the bearings. Mental and emotional aspects of consumers also play role in selecting, purchasing or consuming organic foods (Zanoli and Naspetti 2002). In addition,

conventional stores are often credited to increase popularity through advertisements and promotions and through the presentation of organic and conventional foods side by side, which allows consumers to compare and contrast. Convenience plays a significant role in repeat purchasing (Gottschalk and Leistner 2013) – a consumer buying organic for the first time from a conventional store is likely to repeat if the store provides the product with the convenience the consumer wants. One can easily ascertain that the substantial increase in organic food sales is being contributed by the participation of conventional supermarkets, at least to some extent, though no comprehensive study exists to back the claim. Conventional retail stores allow consumers opportunities to access organic foods easily, to compare with conventional foods in terms of their quality, prices and other characteristics through advertisement and promotion, to be confident on the integrity through the provision of certified organics, and to offer affordability to average consumers through competitive prices. Despite these potential advantages, conventional retail stores are blamed for compromising quality and integrity of organic foods through the encouragement of large-scale and off-shore production and international trade. Conventional retailers are also blamed for providing low quality organics with lower prices to put pressure on the small organic producers and force them out of business. We present below the potential impacts of the involvement of conventional retail stores on organic foods on shopping convenience, consumer knowledge, affordability, integrity and organic producers.

### **Shopping Convenience**

Shopping convenience reflects consumers' perceived degree of avoidance of time and effort associated with the shopping process. It is a multidimensional construct and can be conceptualized using different dimensions of convenience, i.e., decision, access, transaction, benefit and post-benefit conveniences (Berry et al. 2002). Such dimensions, may present powerful reflections of many consumers, but are not necessarily applicable to every real world situation, and some researchers (Moeller et al. 2009) have adopted minor modifications replacing benefits with search. These dimensions affect behavioral and attitudinal loyalty of consumers to buy or not to buy a good. Moeller et al. (2009) showed that the prior purchase dimensions, i.e., decision and access, are more important for frequency of visits and the amount of purchases. Upon qualitative investigation of dimensions of consumer

shopping convenience based on Berry et al. (2002), Gupta and Sharma (2014) came up with a set of six dimensions of convenience – information search, access, selection, assurance, transaction and post-purchase. These theoretical analyses of shopping convenience are of value, for a more applicable analysis of convenience dimensions, consumers' perception should be in the forefront. Reimers (2014), upon surveying consumers in south-east Australia, observed that consumers have much more detailed idea on shopping convenience. Consumers rated many store characteristics, i.e., presence of trolley or basket, air conditioning, clear price labeling, prominent signs/directories, and toilets as important factors of shopping convenience.

Consumer convenience while shopping makes an important contribution to consumer retention and repeat purchase. Many consumers choose on-line shopping simply because of convenience- simple transactions and saving time and effort. Within a few years of developing the drive-through system in fast food restaurants, a huge chunk of consumers switched to drive-through from in-store orderings. In this time-precious environment, shopping convenience adds value to consumers through time-saving especially for utility oriented shoppers, who want prompt and accurate service. Lloyd et al. (2014) observed that depending on the value placed on time, shopping value on retail outcomes vary. Today's large retail stores are aware of this value system and make concerted efforts to maintain nearly all attributes consumers have identified as reflecting a commitment to offer satisfactory level of consumers' shopping convenience. Small stores have little or limited opportunity to deliver these convenient services consumers ordinarily expect, and as such befallen at the edge of the industry. It is also to be noted that most consumers shop at more than one store and they often compare stores based on their pricing strategies and shopping conveniences.

Conventional retail stores offer shopping convenience by providing consumers a wide variety of selection for both organic and non-organic foods at comparable prices. Since the vast majority of consumers buy a mixed bundle of organic and non-organic, they are better off choosing a conventional store to satisfy their entire grocery needs instead of visiting several specialty stores. Many stores shelf their organic products, including their store brands and brand name products, side by side with conventional ones so that consumers can easily compare their quality and prices and make an informed decision. Ton and Raman (2010) observe that an increase in product variety directly increases sales through enhanced consumer accessibility and improved consumer convenience resulted from increased inventory. Wan et al. (2012) found that an increase in product variety has a positive impact on sales, which

follows a diminishing trend, and too much product variety may even have a negative impact. Conventional stores consciously add product variety that maximizes their sales.

Consumers find conventional retail stores for opportunities to have one-stop shopping convenience. Reimers (2014) observes that consumers consider one-stop shopping as one of the most important desirable store characteristics. In fact, many conventional retail stores are not only grocery stores but also supermarkets offering nearly every possible necessity to consumers, including ready-to-eat foods, pharmacies, hair salons and eye care products. Shopping at those stores, consumers can satisfy their regular necessities from one shopping place, and by paying with one bill saving travel time, shopping time and transaction cost. Walmart Supercenters and Costco wholesale locations are good examples of such conventional retail stores.

### **Consumer Knowledge**

Conventional retail stores' entry into organic food retailing business increases popularity of organic foods due to the usual promotional power of the retail sector (Willer and Yussefi 2004). Van Loo et al. (2013) observe that 69% of the respondents did not recognize the widely used EU organic logo introduced on July 1, 2010, but more than half (51%) recognized a logo 'Biogarantie' provided by a Belgian private organization simply because the latter logo was introduced in 1988, long before the introduction of the EU logo, and the private company promoted the logo by backing up with maintained quality. Even if consumers are aware of the label based on well-defined attributes, they do not necessarily have complete information on the product, and often decisions are made based on subjective judgment or perceived quality (Smed and Anderson 2012). It is important that consumers are well-informed about the labeling and the quality associated with the product so that they can make an educated decision without relying on perception. Maya et al. (2011) recommend an increase in social awareness of the relevance of purchasing organic products. At times, one could not find advertisements on organic foods in mainstream newspapers or magazines or other mass media. However, due to the involvement of conventional retailers on organic foods, it is not uncommon today to see promotions of organic foods in major mass media, print or electronic. These promotions include information, sometimes detailed enough to motivate customers to buy organic products. Despite large promotional and information sharing processes,

consumers still remain hungry for information, especially on how and where the organic foods are produced and processed (Wier et al. 2008). Information on the entire process of organic food production, from the field to the consumers' plate, is a major factor for buying decision (Gottschalk and Leistner 2013). From mass media advertisement and promotion, whether one likes it or not or chooses to buy or not, one gets the information on organic foods by default. Frank and Salkever (1992) showed that an entrance of generic drugs causes brand-named producers to increase their prices due to an increase in demand, an upsurge of marginal cost and a lowering of elasticity of demand for brand-name products. The incorporation of organic foods may have a similar effect of increasing price of conventional foods through the increase in demand and lowering elasticity of demand for conventional foods contributing to extra profit. Improved consumer knowledge certainly plays a role in such a situation as a small chain of supermarkets in the U.K., Out of This World, while introducing organic brands, made a strong commitment of educating customers (Jones et al. 2001).

Retailers expect that promoting organic foods creates a positive image of themselves to their customers in terms of promoting environmental stewardship. A sign of "Eat Better Choose Organic" on top of the aisle of fruits and vegetables provides a seemingly convincing image to most astute shoppers. Shopping fliers, printed or online, contain at least some sections promoting organic foods with a positive message. Since quality and variety are two common promotional words used in most supermarkets, promotion materials carrying such claims would increase consumers' attraction towards organic foods. Mass media coverage and shopping fliers contribute to providing information on price, quality and product variety of organic foods. Bellotti and Panzone (2015), examining a large number of articles published on organic foods in British media, observe a direct correlation between the number of articles published and the amount of sales of organic foods.

### **Affordability**

The production cost of organic foods, in general, is higher for being chemical-free (labor-intensive), using high-value organic fertilizers, and employing high-cost agronomic, processing and distribution practices. Regulation and certification costs add another layer on top. Compounding with increased production, processing, distribution and retail costs, organic foods have to be sold at a premium price. The situation becomes even worse due to a

higher inelastic demand and relatively inelastic supply, making organic food prices much higher than their conventional counterparts. Higher price has been identified as an important factor for consumer decision of whether to buy organic or not (French 2003; Zanolini and Naspetti 2002; Monier et al. 2009; Hamzaoui-Essoussi and Zahaf 2012). Many consumers, though they have willingness to pay higher prices, may find organic food prices much higher than they can afford. Conventional retail stores vowed to break such barriers. Sainsbury's and Tesco, the two supermarket chains in the U.K., incorporated organic foods in their shelves with objectives to provide customers with a wider selection as well as a low-cost option of organics. With these mandates, they provided promotional materials and media interviews. Iceland, a small company, also promised to supply organic food at an "everyday price" through its business innovations (Jones et al. 2001). Walmart's 'Organics for All' shows a similar strategy to offer organic products to average consumers. This allows retailers to sell many identical food products at substantially lower prices – sometimes as low as 15 to 25% (Hausman and Leibtag 2007). A cheaper price of organic foods is likely to increase sales of organic foods, although Bunte et al. (2010) showed that significantly higher sales may not result even if the price of organic food is lowered to that of conventional product. Although results on the price elasticity of demand for organic foods are mixed and depends on food commodities, locations, demographics and many others (Rodiger and Hamm 2015), a downward sloping demand is true for all food commodities including organics, and a lower price is expected to cause higher sales. Walmart supercenters do not sell organic foods only; rather they contain substantially more conventional foods than organic. A lower price is expected to attract consumers irrespective of conventional or organic, and since Walmart sells more conventional items than organic, a promotion for lower organic prices is expected to increase sales of organic as well as conventional foods providing an opportunity to acquire added profit.

Consumers, in general, are ready to pay a premium price for organic foods (Batte et al. 2007; Islam, 2013, 2014) due to their preferred characteristics, although the willingness to pay premium price varies from one preferred characteristic to another. Cultural perspectives (Gotschi et al. 2010), political and religious beliefs (Onyango et al. 2007) and demographics (Zepeda et al. 2006) also play a significant role in choosing organic foods and, as such, willingness to pay premium prices. Since organic foods are 'goods', a lower price is expected to increase consumer surplus and for every consumer, the lower the price they can pay, the better they are, irrespective of their preferred attributes. If the price premium is too high, price sensitive consumers may

switch to conventional foods. However, a small section of consumers with strong preference towards organic would be willing to pay substantial premiums for organic foods, consistently pay high prices for quality organic foods and are less likely to switch to low priced conventional irrespective of the size of price premium (Marian et al. 2014). By and large, a vast majority of consumers are price sensitive and a lower price is expected to increase sales among them.

Resulting cheaper prices and increasing affordability due to conventionalization of retail system is a double-edged sword for the organic food industry. On one side, a lower price increases accessibility of marginal consumers and as such surges sales volume, a positive effect toward organic industry. On the other side, due to substitutability, a lower price in organic foods may result in a lower price in conventional foods, which in fact increases the proportion of price premiums for organic, resulting in organic foods becoming more expensive and, as such, unattractive. Recent low prices of conventional milk in supermarkets are a good example (Siemon 2010).

Whether conventionalization has been able to lower prices of organic foods remains questionable, especially on the retail level. Retail price data is scanty and whatever is available is sporadic and spotty. Even USDA market survey provides only farm level and wholesale price data with very little information on retail prices. Historically, average wholesale price differentials between conventional and organic fruits remain more or less the same in U.S. (USDA 2016a), rather the variability has been increased. On a retail level, anecdotal evidence pertains to the direction that the price premium between organic and conventional has not changed much. Jaenicke and Carlson (2015), upon analyzing household level data, found that the price premiums for organic food are not in danger, although a slight possibility of some degree of moderation may exist due to increased competition. If the price premium is not significantly reduced, the increase in affordability is certainly questionable. Over time, food prices have increased considerably and, if so, the prices of organic foods, then affordability may even be reduced.

## **Integrity**

The corporatization of the organic industry is allowing the production and marketing of foods that are less organic, sometimes called ‘corporate organic’ (Green 2008). The USDA’s certification process, in fact, supports this argument in that only ‘100 percent organic’ has the entire organically

produced ingredients. Whereas, as per USDA's definition, food products containing at least 95% of organically produced ingredients is called 'organic'. A similar definition has also been adopted in Canada. This creates a challenge in maintaining the integrity of the organic foods in terms of maintaining purity. The EU is more cautious about organic content and is scheduled to implement a stricter requirement for certifying organic foods. For example, from the beginning of 2016, to be certified organic fish, the entire life-cycle of fish, from hatching to the market place, has to be organic (Ankamah-Yeboah et al. 2016).

Critics of organic foods question the integrity of the certification process as USDA allows production and processing facilities of its four categories of organic products - crops, livestock, processed products and wild crops - to be anywhere in the world. The products can receive organic labels as long as they comply with USDA organic regulations. In addition, the certification can be done by a private, foreign or state entity accredited by the USDA, which lists nearly a thousand approved private and public agents spanning all over the world from Afghanistan to Zambia to certify organic foods (USDA 2016b). These organizations can certify any of the four kinds of products as organic and can use USDA organic logo to prove integrity of the product. For testing regulatory compliance, these organizations charge fees from the producers or product owners, for which there is no standard. Appropriate monitoring of the entire process is extremely hard and considerably costly. Phony businesses with unfair practices can easily slip into the market containing authentic organic labels. In Canada, a similar system exists, though not as extensive as in the U.S. CFIA, Canada's government agency to monitor and approve the certification process, accredited mostly Canadian and U.S. agencies with only one agency from Argentina (CFIA 2016). Jaffee and Howard (2010) argued that large corporations have influenced regulations and certification systems towards their advantage through regulatory capture and weakening standards by powerful lobbying.

The integrity of organic food has also been challenged due to globalized trade. Many of the organic foods we eat in the developed world are imported from the developing world, where reputable organic certification schemes are either absent or not appropriately implemented. For example, the Dominican Republic is the leading producer and exporter of organic bananas in the world, which goes through the third party certification system (Trauger and Murphy 2013). These third party certification systems are expected to be objective and unbiased due to the lack of conflict of interest. However, in most cases, such third party certification agencies are either based on the point of origin or on

the area of consumption. A majority of them do not have representatives to monitor the entire process, and rely on other certifiers through multilateral agreements (Trauger and Murphy 2013). Because of the insufficient monitoring of the complicated certification system, the agencies even simplify the process identifying a series of must-have and must-not-haves for certifiable products. The entire process is not completely transparent to consumers and many certifying agencies are not necessarily accredited by all relevant regulatory authorities.

### **Production System**

Conventionalization in the organic food marking system has influenced the production of organic foods. In fact, the organic production system has become conventionalized in the sense that large corporate businesses have been taking part in large-scale organic food production using economies of scale, relying on purchased inputs, mechanization, resource substitution (capital for land and labor) and modern organizational management features (Darnhofer et al. 2010). On one side, conventionalization of organic agricultural production allows production to be of large scale and at low cost to face the growing consumer demand and to offer organic foods at affordable prices. By producing certified organic foods in this process and selling at premium prices, farming operations can reap benefits in terms of increased profit. On the other hand, conventionalization tends to compromise the core values of organic farming- healthy food production, animal welfare, environmental stewardship and financial viability. Large crop production systems cannot maintain healthy production systems and environmental stewardship, and large animal production systems cannot guarantee appropriate animal welfare. Kastel (2006) reports that a growing number of factory farms house thousands of cows in confinement to satisfy the growing demand for organic milk. In a recent report, The Cornucopia Institute (2015) describes the industrial-scale organic egg production, where 125,000 to 150,000 birds are placed in two-story barns with very little access to outside world. In fact, the corporatization of production system has shifted the culture of 'farm' (... an all-encompassing lifestyle whose purpose was sustaining families and communities in addition to fields and pastures – Thomas Jefferson) to 'firm' (an entity providing goods and services to consumers with a view to earn profit).

Organic farming enjoys a reputation from consumers and policy makers and receives public support for its potential contribution to environment and community development (Darnhofer et al. 2010). If it comes to resemble conventional farming through the adoption of nearly all characteristics of the latter, it has the potential to lose the credibility and support it enjoys and the premium price it receives for its products. An extreme scenario of such a case would be entire farming be conventional and not organic or no difference between organic and conventional farming.

Conventionalization of organic production has been blamed for threatening the existence of smaller organic farms and retailers to out of business (Johnston et al. 2009). Corporate farms, through their strategic behavior and economies of scale, can achieve a cost advantage that small farmers cannot. The field of competition between these two categories of farms is not plain and is biased toward corporate farming. Corporate farms, through their immense market power, can practice predatory pricing behavior and buy out small organic farms as in the case of the processing sector. Large corporations make substantially higher offer to acquire existing organic operations to gain credibility as well as market power. Such practices are in existence as many smaller operations are being sold to large multinational companies.

### Conventional Retailers: The Case of Loblaw IN CANADA

Loblaw Companies Limited is a leading food retailer in Canada operating over 1000 retail grocery stores across the country consisting of both discount and full-service supermarkets. Its full-service supermarkets are tailored to demographic needs of local markets, delivering varieties of products including local, fresh and organic foods. Providing innovative products is always in its mission and accordingly it first incorporated few organic items in its shelf in around 2000s. Within the last 15 years, it has become one of the largest providers of organic foods. Today, many of its grocery outlets maintain separate and dedicated aisles for organic foods, although shelving side-by-side with conventional foods for easily locating and comparing by customers is also present.

Although Loblaw Companies Limited was originally thought to be grocery stores for low-income consumers, it evolved itself for a wide range

customer groups based on income, ethnicity and demographics. One of its major impetuses was on brand labeling. Loblaw, though retails many brand names grocery items, has been creative in developing its chain stores in various names – No Frills, Superstores, Extrafoods, etc. In general, No Frills are considered discount stores with lower price points, whereas, Real Canadian Superstores are considered mid-range price-points selling food products with a range of price points.

Aside from its store brands for targeting community groups, Loblaw has been successful in developing its own labels. Its private labeled products in the name of ‘No Name’ and ‘President’s Choice’ have been widely known. No Name brand is considered for general customers sold mostly through discount stores. President’s Choice (PC), as the name implies, is intended for customers with mid- to upper-echelon income groups, for purchasers with greater product sensitivity and lower price sensitivity. Loblaw’s launch of the Blue Menu brand for exclusive customer concern with calories and fat content and Mini Chefs for those who seek convenience in cooking are also similar examples of market strategy. Along with these products, Loblaw incorporated its own brand organic, PC Organic, in 2001 with a small set of products (Loblaw Companies Limited 2016). In the following year, it launched PC Organic baby food. Very quickly it jumped into many more organic products, mostly with its own private label but also incorporating other organic brands. Within the first six years, its organic product inventory went to over 300 and now literally thousands. In any of its high-end grocery retail stores, one can find a whole range of organic foods – from fresh fruits and vegetables (raw or pre-packaged) to dairies to dry snack foods to boxed hot and cold cereals to canned fruits and vegetables to beverages (including tea and coffee). Its website lists nearly 300 PC Organic foods – from raw to processed and packaged.

Loblaw, not only incorporated organic food items in its stores in 2001, but also promoted those products for creating image and maintaining integrity. While introducing, it vowed to customers to work with organic farmers and to ensure that organic food items are produced through holistic practices considering human health and productive environment- soil, crops, livestock and ecosystem. It also conveyed to customers that these organic foods are certified by a third party certification agency following strict guidelines of the National Standard of Canada on Organic Agriculture (Loblaw Companies Limited 2016). It sometimes even named the certification agency in their promotional material or packaging (Quality Assurance International, for example) and created more lucrative brands with specific descriptions. PC

Organics 7 Reasons Multigrain Cereal is claimed to be low in fat, no sugar added, a good source of fiber, low calorie, low sodium, wonderful tasting and have superb texture, and all of its ingredients are organic. It also created PC Organic Ancient Grains Cereal and PC Organics Swiss Muesli to attract more customers.

With criticisms of industrial organic production, Loblaw effectively responds back. For example, it claims that all its organic eggs are collected from free-range chickens (raised inside with sufficient room for chickens to roam around and nest). It also claims that all of its organic meat products are GMO, hormone and antibiotic-free. As for variety, organic product range varies from human food to pet food and from fresh to frozen, and from raw to ready-to-eat foods. In a recent advertisement in Canadian Living magazine, Loblaw claims that it provides “organics of all kinds, for tastes of all kinds” and “when it comes to organic, we produce more than produce”.

Despite all these marketing efforts, Loblaw’s total market share of grocery sales in Canada declined due to a combination of several factors (Tyghe and Kohbodi 2012) primarily losing to Metro, Costco and Wal-Mart. Walmart’s aggressive expansion and creation of ‘Supercenters’ and Metro’s loyalty program provided a substantial challenge. Loblaw, however, remains the leading retail grocery outlet in the country. Loblaw’s competitors, i.e., Safeway, Sobeys, Overweatea Foods, all introduced organic brands, mostly from other organic brands and relatively small from their own brand. Canadian grocers are in general price sensitive, though there are variations among ethnic groups. The ethnic group that spends the highest amount on grocery items, South-Asian community, also happens to be the most price sensitive (Tyghe and Khobodi 2012). Does Loblaw’s introduction and expansion of organic food cause its demise in market share? Likely not. Rather, if it did not introduce its own brand of organic and bring organics from other brands, its market share would have been further reduced.

## CONCLUSION

Retailing organic foods through conventional channels is a reality and is not only likely to remain, rather to continue to rise as the entire organic sector is driven by growing demand. Amplified concerns of food safety and increasing information on organic foods available to the general populace contribute to bigger demand, resulting in further escalating involvement of conventional production, processing, distribution and retailing. This also leads

to increased competition and is likely to put pressure on retail prices. Although it has not been proven through rigorous research that the increased competition as a result of conventionalization of retail sector, in fact, reduces price, many consumers indeed have the same perception, which by itself encourages more consumers to buy organics, resulting in a possibility of further increase in sales. Over 90% of organic food sales now happen through conventional and natural food retails and chains (USDA 2016). In Australia, nearly two-thirds of all consumers buy organic (Pearson et al. 2013).

The conventionalization process of the entire organic industry is likely to continue as the impetus has been from all fronts - from industry participants to exercise market power, from the regulatory authority to protect consumers and to ensure free markets to function nationally and globally, and from the general populace to enjoy competitive price and shopping convenience. Through the conventionalization process, production, processing, distribution and retail sectors are becoming more concentrated with smaller number of players. Each player is getting bigger and bigger to reap the benefits of economies of scale as well as market power. More applied regulations to the certification process and multilateral equivalency arrangements are also helping additional commoditization and international trade, which will eventually further accentuating the conventionalization process.

Along with the increase in organic food sales through conventional retail stores, concerns over food safety continue to grow as more and more research becomes available on the drawbacks of consuming industrial foods. More and more industrial foods are becoming available with variable labels, contents and health claims. Even the fast food restaurants and sugary drink producing companies are coming up with their respective healthy brands. Processed foods labeled with healthy, sugar-free, fat-free, trans-fat-free, and many others are common in the marketplace. Many retail chains have created their own brands, i.e., 'healthy choice', 'blue menu', 'natural', etc. Although some consumers do get attracted to these 'healthy' food brands, a majority of consumers remain skeptical on those claims of processed foods, as they have little information on what those mean. Organic foods, however, remain popular as a result of the promotional activities offered through retailers and the existence of institutional certification systems, which increase consumers' confidence and trust on organic foods.

Despite an ample amount of trust on organic foods by consumers, conventionalization has incorporated doubts. The total sale, consumption and the proportion of consuming organics within the entire food category are all growing, though at different paces at different locations despite premium

prices to be paid. In reaction to the conventionalization effect and the potential for compromising integrity of organic foods, consumers explore other alternative marketing channels to obtain real organic foods. The growth of direct marketing through farmers' markets may be an outcome of such exploration. At times, farmers' markets were scanty and existed for a few hours on weekends, targeting a certain group of customers. Now, one can find farmers' markets nearly every day somewhere in the city. In the U.S., the number of farmers' markets grew from 1,755 in 1994 to 8,144 in 2013 (USDA 2016). One may claim that farmers' markets are simply to provide local and fresh foods and organic foods have little to do, but it is proven that the demand for organic foods in farmers' markets is substantial (Kremen et al. 2004). Although farmers' markets may provide some relief to some consumers, the vast majority of consumers still have to rely on conventional retail stores for their organic groceries, and as such the conventional retail groceries are going to remain around to supply organics.

Organic food retail sector has substantial challenges ahead to continue its growth. Such challenges, in an extreme situation, may cause the entire organic sector to lose its identity and integrity, and may force organic to merge with conventional food industry. Every challenge, however, has its opportunities, and appropriate strategic directions may make the challenges into opportunities in a way that the organic food industry may continue to flourish nearly the same pace as it is now, if not more, throughout the coming decades. In the following subsections, we present a brief account of potential challenges organic food retail sector may face followed by what can possibly be done by different stake-holder groups to maintain trust, integrity and growth of the industry.

### **Challenges Ahead**

The most important challenge the organic food retail sector is expected to face at this time is at the core of the industry- the credibility of the labeled organic foods themselves. The entire industry has thrived based on the credibility and trust (real or perceived) placed by consumers on organic foods. The conventionalization of the industry- from production to retail, the imperfect and inconsistent certification system, global trade and transportation, and bi-lateral equivalency arrangements of organic certification systems contribute to accumulate doubts in consumers' mind. Through the conventionalization process, if the trust on organic foods is broken and the

reliability becomes doubtful, the entire industry may be affected. The primary reason for buying organic food is to get 'pure' organic and 'free from' chemicals and all other artificial and unethical influences. The development of the entire supply chain and consumers' willingness to pay premium prices are based on the response of such demands. If the integrity and conviction of consumers on organic foods are contaminated, consumers' confidence and willingness to pay premium prices may evaporate, and simultaneously sales may decrease, affecting the entire organic food industry. Potential challenges specific to the retail sector can be grouped into three categories- marketing, regulatory and financial challenges.

An important marketing challenge the organic food retail sector is facing is its competition with several other similar food brands and labels. Walking into a retail grocery store or a supermarket, one can easily see brands identified as 'natural', 'locally produced', 'blue menu', 'healthy choice', 'naturally grown' and so forth. Consumers often become confused and find it hard to come up with which labeled food they would buy. Although all these labels try to portray a positive message, very little information is available to judge what those exactly mean and as a result consumers become uncertain of how to find out which one is better than which one and why. A plethora of questions may arise in front of consumers. Is a natural food better than an organic food or vice versa? Is a local food better than an organic (but non-local) food? What does natural mean? How is local defined? Of course the answers depend on the individual consumer's knowledge and perception of all those seemingly analogous food categories and their comparable prices. In general, consumers prefer domestically produced foods over imported ones and local over organic if they have to choose one or the other (Hempel and Hamm 2016).

Another marketing challenge for organic foods is the price premium. Although highly organically minded consumers are expected to pay high price premiums, average consumers are still price sensitive and regard price as an important barrier to buying organic foods (Buder et al. 2014). Although many conventional retailers promise to deliver organic foods at lower prices (Wal-Mart's promise to deliver at 10% premium and Iceland's promise to deliver organic at 'everyday price', for example), very little evidence of such an undertaking is evident. Price premium remains an on-going challenge for most consumers. As mentioned earlier, this is a double-edged sword for the industry in the sense that lower prices increase customer base for organic foods but drive smaller farmers producing pure organic foods out of business, as they cannot compete with large corporate farms despite innovative practices.

Other marketing challenges include supply shortage, lack of authentic information, poor presentation, lack of availability and access, and credibility of organic foods to consumers. Retailers will face continuous challenge of providing appropriate organic food products in their shelves with acceptable prices. Buder et al. (2014) recommend that retailers should consider making a range of organic foods available in their shelves and conducting research for the most demanded products so that customers do not feel the lack of availability. Since most customers do not shop at a specific store, rather a variety of stores seeking quality products and better prices, it is of the interest of the retailers to ensure credible variety with appropriate pricing. It is also to be noted that organic foods being chemical-free typically have shorter shelf life and are subject to more waste (Eriksson et al. 2014).

The organic retail sector is expected to face substantial regulatory challenge. The regulatory prevalence, especially organic certification systems and bilateral organic equivalency arrangements, initially contributed substantially to accelerated sales. However, as more and more countries and jurisdictions are implementing such labeling systems for more and more organic products, harmonizing the labeling systems becomes complicated and poses a substantial challenge. Because of jurisdictional differences, organic standards are different and a common standard is unlikely to be established (Sawyer et al. 2009). Substantial differences among products are in existence. Aquaculture production systems may have a different set of required standards than a crop production system. In the EU, the aquaculture certification system requires that the entire life-cycle of fish to be organic (Ankamah-Yeboah et al. 2016), but the crop production system in the U.S. requires a minimum of 95% organically produced ingredients. Similarly, the same product produced in different locations may have different credibility based on the implementation of certification systems and labeling.

The asymmetry in the regulatory systems among jurisdictions and among products poses a challenge in creating credible bilateral equivalency arrangements and, as such, international trade. Such an inconsistency impacts consumers' confidence and demand. The entire industry of organic foods is driven by demand and any tainting on demand poses a substantial challenge to the industry.

The organic food production sector is, in general, financially and logistically supported by public (government and non-government) institutions due to its positive contribution to environment and society. However, if conventionalization becomes the norm of each sector, such support may not

exist (Darnhofer et al. 2010). Organic production systems invariably produce lower yield than conventional production systems for obvious reasons, and under most comparable situation, the yield gap can be as high as 34% (Seufert et al. 2012). Although efforts of minimizing such a large gap are seen among researchers, and no matter where future technology takes organic farming to go, substantial yield gap is expected to remain. Ponisio et al. (2014), upon a recent meta-analysis, observed that the average yield gap is 19.2%, much lower than reported in earlier studies, and for some crops, yield gap is even much lower (i.e., legumes and perennials). They also observe that by using appropriate agronomic practices - multi-cropping and crop rotation for example - can reduce the yield gap to below 10%. Irrespective of how much minimization can be done, yield gap continues and with no public support, the organic production is at a financial disadvantage.

Specialty organic producers and retailers are to face competitive disadvantages of receiving finance through commercial business loans simply because of their smaller size. Large corporate businesses can easily obtain business loans with competitive interest rates. Whereas, small organic producers and retailers are considered high-risk businesses as they have little collateral to support financing, less competitive ability compared to large producers and retailers and less capital accumulation. So, the organic industry has limited access to financing through business or commercial loans, and certainly not as much as conventional production and retails.

### **Possible Policy Implications**

The organic food retail sector is becoming more and more popular and is becoming integrated with the mainstream marketing channels and traditional grocery stores. This process provides consumers convenience, competitive price and other benefits, but at the same time invites challenges. The benefits and challenges are expected to continue and the impacts on both sides are likely to become more and more intense. The organic food retail sector is not mature enough and requires appropriate support from all sides- producers, consumers and policy makers. Producers and consumers support may come from private sector due to several motivations of being involved in organic foods. Policy supports, however, have to come from institutions and governments, which can support the industry directly or indirectly through producers or consumers. Johnson (2013) advanced six recommendations along

with some explanations and justifications to support small-scale producers, farmers markets and small retailers so that they remain the industry and provide standard of comparison of classical organic foods. These recommendations are: (1) do not rely on market forces to dictate control of organics, (2) clarify and refine standards for organic production, (3) develop product-based standards, (4) revise standards for imported organics, (5) develop consolidations for small farmers and public welfare, and (6) revise labeling requirements. These are all worth considering, but all of them may not necessarily be put into practice in their recommended forms primarily due to their difficulty in implementation.

Government support to the industry is crucial, as the USDA makes a concerted effort to increase domestic organic production. However, due to comparative costs of production in the U.S., overseas production remains cheaper, resulting in an increase in import of organic foods from abroad. Recently, the 2014 Farm Act extended its support to the organic sector through the provision of research services and risk management, and support for conservation practices and certification cost-share assistance (Green 2014). The organic food industry deserves such support, and all jurisdictions should be considering similar policies so that competition between organic and non-organic is on a level plain field.

Market forces cannot be avoided in the western world, although some degree of influence can be made through the implementation of appropriate regulations. Much of the regulatory process in the food industry is still influenced by corporate producers, processors, distributors and retailers with little influence from actual organic producers and consumers. In addition, many of the regulations are implemented voluntarily and very little consequences are available to violators. With a set of appropriately designed regulations with tight implementation and monitoring, this problem can be avoided. Of course, this is not going to be cost-free, and if the cost is to be compensated by the organic industry, then the organic sector will become even more marginalized, as it is already under high pressure from competition and easing up price premiums. Public support through the provision of implementation and monitoring of such regulations should be placed, considering the fact that organic food sector is expected to contribute public goods through its environmentally friendly production and consumption practices.

Organic foods placed in shelves should contain sufficient information, from production in the field to processing to distribution and storage, so that

consumers can get a complete understanding of the integrity of the organic food, rather than to rely only on the organic logo. This gives consumers a clear choice of organic foods over seemingly analogous food categories (natural, locally produced, healthy choice, etc.) available on shelves. Over time, it has become apparent that consumers are becoming more and more educated and are seeking more and more information on the entire process of producing the food they buy from retail stores. For any imported foods or ingredients, the origin of the product should be reported. Since the quality differences between organic and conventional foods are not apparent, most consumers rely on labeling and it has been reported that locally produced foods are more valued than imported ones (Hempel and Hamm 2016).

Information on the organic food industry is provided by conventional producers, processors, distributors and retailers through advertisements and promotions. This provision of information plays a significant role in educating consumers on organic foods. However, such information is often biased, conveyed with specific business objective, not necessarily educational and may even contain misinformation. An institutional and legally binding provision of information or education system can provide unbiased, true and objective information. Although buying organic may still be partly influenced by perception, the provision of objective education provides rational consumers tools to make informed choice on buying organic or not. This also helps them to effectively consider costs and benefits of organic foods.

Organic food industry requires better integration and transparency among all participants, producers, consumers, regulators and traders to maintain integrity. Many organic foods are produced in a country where effective regulatory systems for certifying organic foods are absent. Certification is often done through a private third party approved by a government-led system and using a similar voluntary disclosure system of producers practiced in the EU, the U.S., Japan and Canada. Worldwide, organic certification is primarily controlled by three government-led systems, the EU, the U.S. and Japan. The USDA, the government agency responsible for approving certification agency in the U.S., has permitted organic certification agencies nearly all over the world (USDA 2016b). To maintain integrity, such foods need to be monitored at each step and should not be relied on voluntary disclosure, which requires integration, inter-agency monitoring and information-sharing among all participants.

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