

# ORGANIC FOOD SOURCING, PROCESSING AND DISTRIBUTION: A CASE OF SATISFYING A GROWING MARKET

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**Abstract:** A case study of an organic food company in the Slovak Republic involved in producing and sourcing inputs, food processing and distribution is presented. The case is based on a June 2014 “live” case study prepared for students in International MBA in Agribusiness programs at the Slovak University of Agriculture in Nitra, Warsaw University of Life Sciences and the National University of Life and Environmental Sciences of Ukraine, Kiev.

The company was established in 2001 with the objective to bring organic food to health conscious consumers. The company grows organic spelt grain, wheat, rye, buckwheat, herbs and apples on its 156 ha and 400 ha of owned and rented farmland. The company further processes these crops into more than 40 finished products.

Students are presented with company information and summaries of a company visit and discussions with management. Students perform PEST and SWOT analyses, identify a shortage of owned and leased land as a problem the company must address, conduct research and analysis, and recommend product specification contracts as a solution to the problem.

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## Organic Food Sourcing, Processing and Distribution: A Case of Satisfying a Growing Market

### Introduction

The purpose of this article is to improve the attractiveness of studies in the field of business administration with special emphasis on agribusiness. The article contributes to the exchange of experiences in course management and teaching processes by presenting and discussing a case that enhances the attractiveness of educational programs. In particular, the case study utilizes political, economic, social and technological (PEST) and strengths, weaknesses, opportunities and threats (SWOT) analyses applied to an organic food company in Slovakia.

### Case Study Background

#### *Day 1: Getting Started*

Twenty-five students have gathered to participate in the joint study week of the International MBA in Agribusiness and

Commerce (AGRIMBA). The students come from AGRIMBA programs at the Warsaw University of Life Sciences, Poland, the National University of Life and Environmental Sciences of Ukraine, Kiev, and the host for the week, the Slovak University of Agriculture in Nitra. Most students arrived only a couple of hours earlier and have checked into the pension where they will stay for the next few days. The early evening light is quickly fading to darkness as introductions are made and students meet each other around tables lit by candles. The students are presented with the objective of the study week which is to provide a recommended course of action for a company to improve its business. Each student then signs up to be a member of one of four multinational teams. The next morning two teams will visit a joint stock company with both crop and livestock production as well as non-agricultural interests, although the company primarily specializes in milk production. The other two teams will visit the Company Ekotrend Myjava, Ltd., which is the focus of the case presented here.

### **Day 2: Company Visit**

It is a bright, sunny, warm day in Podkylava located in the western part of the Slovak Republic. Two teams consisting of a total of 13 students set out from the pension for the short drive to visit the company Ekotrend Myjava. The company is located in Rudnik in the Myjava region not far from the Czech Republic border. The students begin with a tour of the operation when they arrive followed by a detailed discussion with management (Figure 1).

Ekotrend Myjava was established in 2001. The company's vision (Ekotrend Myjava, 2014) as translated from Slovak to English is:

We want to bring organic food as an alternative to conventional food for those people who care about healthy lifestyles; the countryside in which their children will grow up and develop native country - Slovakia. This lifestyle is knowledge of the positive benefits of organic food and commune with nature. Organic method of farming to protect soil, water, air, biota, animals, plants, and so actually ourselves and our children. Production of organic products we are trying to achieve by using the right approach and not artificial fertilizers and chemicals. Our goal is to help the return of man to nature, and therefore the motto of our company is: Discover the taste and the power of nature!

The company started out by producing herbs and later expanded with the planting and processing of spelt grain into flour and eventually pasta products as well as the production of other eco products. In 2005 the company became the exclusive distributor of the products it manufactured. Ekotrend Myjava has continued to grow into a company with many activities. It owns and operates an organic farm with an area of 156 ha as well as operating 400 ha of leased land. Slovakia is a country with a sizable 8.6 percent share of its agricultural area in organic production in 2012 (Katsarova, 2015). Neighboring Austria and Czech Republic have greater shares (18.6 percent and 13.1 percent) while Poland and Hungary have lower shares (4.6 percent and 2.4 percent) of agricultural area in organic production. Ekotrend Myjava's operation includes the cultivation of spelt grain, wheat, rye, buckwheat, herbs and an apple orchard. Besides organic production, the company undertakes food processing (Figure 2), packaging of pasta and tea, distribution, and wholesale and retail sales including the purchase and sale of other producers' products (Ekotrend Myjava, 2014). The company is one of seven processors in Slovakia manufacturing organic grain products in 2014 (Eurostat, 2015). Moreover the company has: 1) freight vehicles to assist distribution, 2) agricultural machinery for primary production, processing and packaging operations to add value, and 3) brokerage, consulting and advisory services.

The workforce of Ekotrend Myjava consists of 28 people. The company has a team culture which seeks to instill direct, honest and timely communication, mutual trust and cooperation.

The company produces its own brand of organic food under the Biomila® brand. The Biomila® brand product line has more than 40 products including teas, grains, flour, cereal, pasta, bakery products, dried apples, beverages and sunflower oil (Figure 3). In addition to its own line of products Ekotrend

Myjava handles about 800 products with different brands and countries of origin. However, the main production is spelt grain (Figure 4). Spelt is a historical grain which has higher fiber, gluten, vitamin and mineral content than standard whole-grain, soft wheat (U.S. Department of Agriculture, 2015). According to the company, spelt grain helps digestion and improves immunity while at the same time it has a pleasant nutty flavor.

Ekotrend Myjava's organic farming is registered by the Central Control and Testing Institute of Agriculture. It is regularly inspected by Naturalis SK, sro. This allows all certified products to bear the Euro-leaf green logo of the European Community (code BIO-E-002). The logo signifies the organic origin of the product and allows consumers to easily distinguish the product from conventionally produced products. All production and processing meets the quality system requirements of Hazard Analysis Critical Control Point (HACCP). And the company's Biomila® branded products have received the certified quality control system ISO 22000:2005 since 2010.

During the discussion with management, the students were told that the company uses various distribution channels which includes 80 partners. Ekotrend Myjava deals directly with supermarket retailers such as Tesco, Lidl, Metro, Billa, CBA, COOP Jednota, Kaufland and others. The retailers account for distribution of 65 percent of the company's sales. Specialized shops which handle bio products are another important point of sales for the company's products accounting for 27 percent of sales. The remaining eight percent of sales are processed through E-shops including its own. The distribution of products is partially supported by two freight vehicles owned and operated by the company. The distribution of sales is a good match to the places where Europeans purchase organic food. The main purchase points for Europeans are specialized shops (67 percent) and supermarkets (65 percent), but they also use the internet (7 percent) to purchase organic foods (Katsarova, 2015).

Most of the company's production and sales take place in Slovakia, although it also exports products to the Czech Republic and Bulgaria. Ekotrend Myjava is a leader for bio products in the Slovak market. However, there is strong competition from foreign countries such as Hungary, Poland, Czech Republic and others.

The company would seem to be in an excellent, growing market with Europeans spending 6 percent more on organic food in 2013 (Katsarova, 2015). However, it is difficult to meet the growing demand for the company's products as the demand for its inputs also increases as indicated by the price per ton of wheat increasing from 400 Euro in 2013 to 700 Euro in 2014. This situation was highlighted for a company in the United States in the article, "Hunger for Organic Foods Stretches Supply Chain" (Wall Street Journal, 2015). Also, price stability for organic products can be an issue (Su and Cook, 2015).

The students ended the second day of the joint study week realizing they had much work ahead of them over the next few days.

### Days 3 and 4: Research, Analysis and Recommendation

Cases synthesize the core sequence of the agribusiness and agricultural economics degree by requiring students to draw on all previous courses and experiences. Cases, such as the one presented here, are true-to-life. Students must formulate a solution. It is here that the principles of agribusiness, economics, management and marketing are applied. Not only must the students identify a solution to the issues in the case, but their decision must be supported through rigorous analysis.

The objective of each case is to develop solid support for whatever decisions are made. The case functions primarily as a catalyst for developing skills in decision-making, policy analysis, strategy formulation, and communication.

Each team of students was instructed to prepare a presentation and report. The students were reminded they were providing the presentation and report to the management of the company. They also needed to frame the issue in the proper context so the management can understand the importance of the question at hand. Although there may be multiple issues, each team was to focus on a single issue. Once the issue was identified, each team was to make recommendations for how the company or institution should proceed. Each team was to support its recommendations with analysis and persuasive arguments.

## Methodology and Analysis

The students evaluated the external environmental forces impacting Ekotrend Myjava so they may formulate recommendations to capitalize on strategic opportunities and contain any potential threats (David, 2013, page 63, and Healey, 1994). The analysis included four external forces: political, economic, social and technological (PEST). The PEST analysis is presented in Table 1.

Table 1. PEST Analysis for Ekotrend Myjava

<i>Political</i>	<i>Social</i>
Complicated procedure to obtain EU funds	Diverse demographics
Tax system and the high cost of maintenance workers	Fashion for healthy food
High labor costs	Increased awareness of nutrition importance
	Improving standard of living
<i>Economic</i>	<i>Technological</i>
Weak economic situation in Slovakia and Europe	Modern technologies are in the market
Economic trends	Reducing costs through use of more efficient energy technologies
Increasing input prices	

The students recognized as a political force that the European Union has funds to support activities such as those undertaken by Ekotrend Myjava. However, the process for obtaining these funds is complex. Moreover, the tax system and high labor costs were identified as impediments to the company's progress. A key economic force is the weak economic environment in the Slovak Republic and much of the rest of Europe. And more specific to Ekotrend Myjava is the relatively high price of its inputs. The social environment is viewed as a very positive force impacting Ekotrend Myjava. The consumption of healthy food is much in fashion and there is an increased awareness of the importance of quality nutrition. The consumption of a healthy, quality food diet is made possible by a general improvement in the standard of living among consumers in Ekotrend Myjava's market area. Finally, Ekotrend Myjava has the technological knowhow to produce quality inputs and products for the bio food market.

SWOT analyses were performed by the two teams and are summarized in Table 2.

Table 2. SWOT Analysis for Ekotrend Myjava

<i>Strengths</i>	<i>Opportunities</i>
BIO production and good product	High demand; Healthy food in fashion
Vertically integrated and many distribution channels	Produce inputs locally and abroad
Leader in market	Obtain EU funds
Good location, knowledge, experience, and brand	New products; Export possibilities; Agro tourism
<i>Weaknesses</i>	<i>Threats</i>
Capacities: small area of owned land; limited possibility to lease land	Import of products from other countries at lower prices; variable input prices
Older equipment	New companies will start to grow bio spelt grain and wheat
Dependence on trade suppliers and weather	Stronger legislation/law about controlling the production

Given the short period of time the students had to work on the case study, they were told to focus on one problem and develop one recommendation to correspond with one plan of action for the company to take. The students focused on the general lack of owned and leased land as a key weakness and, therefore, problem for Ekotrend Myjava. The problem arises because the company has an inadequate quantity of quality inputs, i.e., organic crops, necessary to operate under the Biomila® brand.

## Results: Recommendation and Strategy

The students recommended Ekotrend Myjava locate organic farms in Slovakia and the EU to produce under contract the organic crops needed to meet the growing demand for the Biomila® brand. Their recommendation follows many research studies and findings that the interest in organic food has grown remarkably as consumers and marketers react to popular media about health and environmental effects of pesticides, genetically-modified organisms and food safety. However, the rising popularity of organic foods raises important questions of interest also to governments, growers, distributors, retailers, industry planners and marketers. Consumer purchase decisions are based on subjective experiences and perceptions of organic foods (Hughner et al., 2007, p. 2), including factors affecting consumer attitudes towards food products with sustainable attributes, such as Organic, Fair Trade, and typical products (Annunziata and Scarpato, 2014) and, moreover, consumer approach while buying food in retailing (Paluchová and Benda Prokešová, 2014). Organic foods are occupying more of a central position in the global food market and in global consumption patterns. The global production of organic food is expected to grow substantially and the organic market is frequently regarded as one of the biggest growth markets in the food industry (Baker et al., 2004, Gifford and Bernard, 2006) with global sales increasing 374 percent from 1999 to 2013 (Sahota, 2015).

Contract production will address the problem of not enough production from the small amount of owned and leased land currently operated. Contract production as a strategy allows Ekotrend Myjava to seize the opportunity, at least indirectly, to produce inputs locally and abroad. Contract production could also accommodate geographic dispersion of organic crop production and, potentially result in less production risk from weather.

Instead of contracting farmers to produce organic crops, Ekotrend Myjava could consider purchasing organic crops in the open market. However, product specification contracts may have distinct advantages over open market purchases as a means of acquiring inputs (Jang and Olson, 2010). Jang and Olson discuss food product quality attributes that originate at the farm-level: sensory (e.g. appearance, smell and taste), health or nutrition, and process (e.g. organic products). These three quality attributes can be used to differentiate food products by processors and retailers. If food product quality is dependent on the quality of the inputs, processors have an incentive to control the design of the attributes. This can be better achieved by the use of production contracts instead of purchasing inputs in the open market. The advantage is driven by greater communication and price discovery costs of obtaining the unique product attributes in the open market. The lower communication and price discovery costs of production contracts are obtained by direct transfer of production specifications, i.e., quality, quantity, price and process, from the processor to the producer.

Food products produced by Ekotrend Myjava certainly have quality attributes that rely on quality inputs. For example, its

branded spelt grain products are proposed to have a different taste (sensory), better nutritional characteristics (health and nutrition) and are organically grown (process).

Ekotrend Myjava could also consider purchasing and leasing additional land instead of using production contracts to meet the growing demand for its products. However, it is difficult to purchase and lease land in the area. Even if land is located, it is difficult to raise investment funds to purchase additional land. Any investment funds raised could be more effectively used in the processing and distribution of organic foods.

Production specification contracts can be advantageous to both producers and Ekotrend Myjava. The benefits for producers are: 1) gain knowledge of organic crop production from Ekotrend Myjava, 2) assured market for producers, and 3) reduced output price variability. The benefits for Ekotrend Myjava are: 1) quality control of inputs through the product specification contract, 2) assured access to inputs to produce Ekotrend's high-value, Biomila® products, 3) less input price variability, and 4) increased geographic diversity resulting in less weather risk. These advantages are consistent with those identified by Jang and Olson and Eaton and Shepherd (2001).

The strategy of sourcing more organic crops with production contracts will allow Ekotrend to increase processing capacity. This will lead to an increase in products sales and availability which will strengthen its brand and increase visibility. Moreover, Ekotrend will be in a better position to explore additional market opportunities, ensure steady company growth, and maintain its position as a market leader in the production, processing and distribution of organic foods.

During the case study the market opportunity for healthier food products was also identified (Table 2). Support for such an opportunity is found in many studies in the literature. Kretter (2005) states that "the need of a product is the decisive factor in the purchase of the product and the need reflects the motives which stimulate the buyer." He also defines the predominant motive for bio-products purchase as protection of the environment, health reasons, healthy lifestyle, promotion of organic farming and no chemicals used in manufacturing (Kretter, 2005). Topics related to proper communication of not only bio-products but also sustainability issues can be found in many other research papers. Grunert (2011) states that consumers have, through their food choices, a major role in bringing about a more sustainable food production. However, this presupposes that the differences in sustainability are communicated to consumers, including eco-labelled products. Communication of eco and sustainability issues interconnected with a proper brand communication can bring positive effects to Ekotrend Myjava's products.

## Conclusions

The case method is perhaps the most relevant and practical way to learn managerial skills (Hammond, 2002). The case method also contributes to the exchange of business experiences and enhances the attractiveness of educational programs. The business case can take many different directions. In the case presented here, AGRIMBA students from multiple universities

and countries were presented with the case that demand for Ekotrend Myjava's products exceeded supply. The students could have recommended increasing price and marketing efforts and/or increasing production efficiency of organic inputs among many other strategies. The students instead recommended the company use product specification contracts as the strategy to increase and assure availability of quality, organic inputs and permit the company to increase production of value added, branded organic products.

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Figure 1. Student visit to Ekotrend Myjava



Figure 2. Processing at Ekotrend Myjava



Figure 3. Biomila® Products



Figure 4. Biomila® Spelt Grain