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Into the mainstream

Organic food: no longer a niche in France

A LONG-TERM TREND

Long seen as a niche market, organic has become well-established across the Western world, especially in France. The figures speak for themselves:

67%
of French people
consume organic products
at least once a month

47%
of French people
live less than 10 minutes
from a **specialized organic store**

With more than **EUR8bn** of sales, **organic represents**

4.1%
of the **fast-moving consumer goods** market in France, split between **food (5.3%), liquids (1.7%)** and **home & personal care (1.3%)**

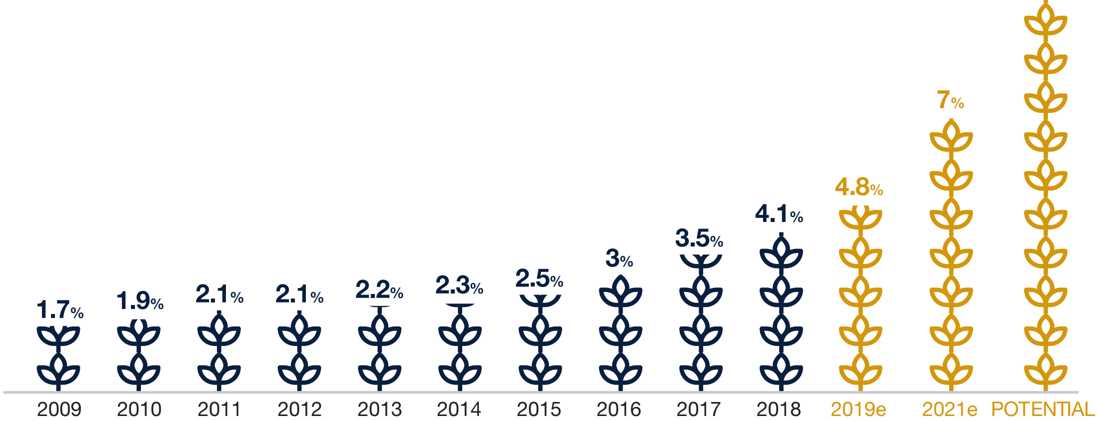
The rise of organic is part of a broader trend towards "naturalness". Led by younger generations, this trend has now been adopted by all ages. It advocates consumption that is both respectful of health, with consumers seeking greater transparency and fewer ingredients/additives/pesticides; and the environment, where people demand reduced packaging and national or even local products.

TOWARDS 11% PENETRATION

The rise of organic is not over yet. Nielsen estimates it has the potential to reach 11% of the FMCG-fresh products market in France. The path to this threshold will be driven by a continuous expansion of the distribution network and a higher allocation of organic in the consumer's basket.

Younger generations have led the organic growth trend, now adopted by all generations.

Penetration of organic among the FMCG-fresh products in France



Source: Nielsen

Specialist organic chains have to rethink their model in the face of generalist retailers

SPECIALIST ORGANIC CHAINS ARE NOW UNDERPERFORMING GENERALIST RETAILERS ON ORGANIC

While specialist organic chains previously outperformed generalist retailers in the sale of organic food, the situation has been reversing since 2017.

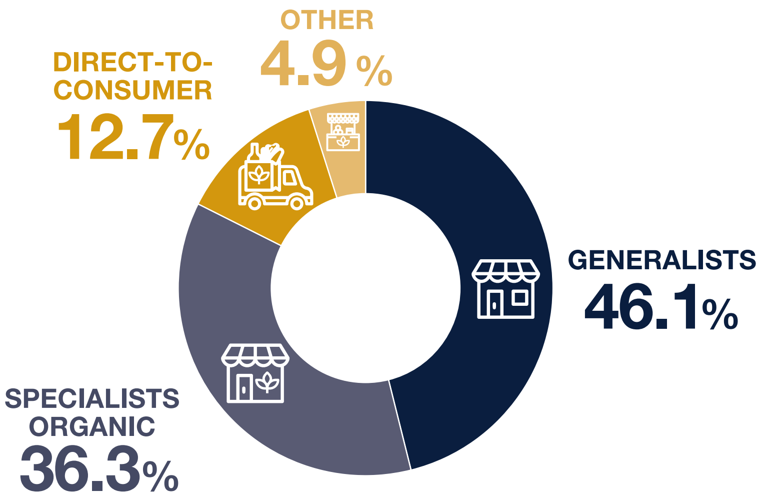
In 2018, generalist retailers recorded 23% growth in the organic segment compared with only 8% for the specialists. This 8% figure masks uneven performance among specialists, with store openings driving growth for the best performers. Out of Biocoop's 11% growth, 7% came from store openings and 4% from like-for-like*. If we compare this to Naturalia; out of its 12% growth, 9-10% was driven by store openings while only 2-3% was like-for-like.

Specialist retailer – growth in 2018

biocoop LA BIO NOUS RASSEMBLE	NATURALIA	les nouveaux Robinson	Bio monde
11% ↗	12% ↗	-6.5% ↘	-2.8% ↘

*Like-for-like is the growth generated excluding M&A and store openings

Competitive landscape in organic in France, 2018



Source: Agence Bio

GENERALIST RETAILERS PULLING AHEAD OF SPECIALISTS

Benefitting from their more mainstream approach, generalist retailers have emphasized:

1. Expanding the organic product ranges in stores. Organic product assortments increased by 20% in 2017 and 25% in 2018 in hypermarkets and supermarkets;

2. Accelerating the opening of stores dedicated to organic. Carrefour launched Carrefour Bio and is rolling out So.bio; Leclerc is opening Leclerc Bio; Auchan created Auchanbio and Coeur de Nature.

Organic is now the main growth driver for generalist retailers, accounting for almost 70% of their growth, and they have not yet saturated their offer with organic products in supermarkets and convenience stores. Although specialist chains have experience, knowledge of their local markets and customer loyalty, they will lose both market share and expansion potential as generalist retailers build their presence in organic.

As well as the impact on specialists retailers' like-for like sales growth and opening potential, this growth gap may also encourage some national organic brands to reverse their opposition to selling on the shelves of generalist retailers. And it goes without saying that purchasing negotiations with major brands will become more difficult for specialist chains that are facing declining sales.

MORE SERVICES ARE NEEDED TO DIFFERENTIATE SPECIALISTS FROM GENERALIST RETAILERS

To keep up, specialist chains need to go beyond just selling organic products, and improve and differentiate their offer versus generalist retailers or farms that sell direct to consumers. For the time being, specialists are still struggling to build a real customer experience and are offering too few services.

A specialist chain typically doesn't offer e-commerce features such as "Click & Collect", home delivery, subscription programmes or loyalty programmes. The transparency on traceability and its use of big data are underutilized and would benefit from being leveraged. Generalists are already beginning to offer all of these attributes to consumers, who now expect to find them in other, more selective distribution channels. As an illustration, e-commerce already generates 6.1% of the whole FMCG/fresh products market in France, split 5.2% drive-through and 0.9% home delivery.

So to retain existing customers and attract new consumers, specialists need to transform their stores and adapt their offer by implementing new digital tools and testing new concepts such as veganism, local products, bulk (unpackage) products and on-site catering.

Investment will be needed and size will matter

DIGITAL TOOLS ARE KEY BUT REQUIRE INVESTMENT

Deploying new concepts in stores to promote a more committed and differentiated offer versus generalists is manageable for all specialists, given the relatively limited amount of investment required.

Connecting Food is working with food producers, branded manufacturers and retailers in several countries to track in real time and digitally audit 100% of their production. The combination of the unique digital LiveAudit solution, a rules engine using mass-balancing at each level of the supply chain to ensure that every product is in line with its promises, and blockchain, ensuring data remains tamper-proof, allows food actors to audit quality in real time. This is key to protecting brand equity and avoiding damaging product recalls, which is currently a major problem with physical audits carried out on a sporadic and post-event basis. A QR code on the food label can showcase the transparent supply chain and prove that promises have been audited by a trusted third party, the blockchain; a major step towards restoring consumer trust in the food they purchase.

MAXINE ROPER & STEFANO VOLPI
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COMPANY TO WATCH

But providing more services and transparency will require significant digital investment that smaller specialists will not be able to afford.

"Click & Collect", drive-through and even home delivery options require the creation of a merchant website, a mobile application and above all a costly upgrade of the logistics network as a whole. Some specialists can try to partner with e-commerce giants, as Casino Group did with Amazon and Ocado, which is less capital-intensive but it requires a strong brand image. E-commerce will be all the more complicated to set up for cooperatives, whose members will first need to agree between themselves on the investment process and the mechanisms for sharing added value.

Greater transparency is also essential to rebuild consumers' confidence as some organic products also face "over-processing". The use of audit and certification technologies will be essential and electronic labels are a way to make it easy for consumers to consult relevant data. Connecting Food is leading the trend in this respect.

PROCUREMENT AND PRICING PRESSURES ARE ALSO EMERGING

This costly need to overhaul business models takes place in a tough environment for procurement and prices, which has been exacerbated by the arrival of generalists in the organic segment.

In 2018, 69% of organic products consumed in France were produced in the country. For growth in organic to continue with a high share of national produce, ensuring the supply of organic products in France will be crucial in the coming years. Each retailer will need to contribute to the structuring of organic farming. This implies:

1. Accompanying farmers during their 2 to 3-year conversion phase to organic farming with a purchasing commitment at higher prices, which then grants the retailer a more or less exclusive access to the farmer/producer's goods;

2. Creating new organic labels that also take into account environmental and social criteria.

Price pressures are also emerging, with generalists being on average 30% cheaper than specialists and still having room to increase promotional intensity.

> *In an increasingly tough environment, the largest specialist chains are equipped to adapt. However, it will be more difficult for the smaller retailers.*

Around 13.5% of their organic sales are made under promotions compared with around 20% in non-organic. Although this difference is partly explained by the weight of private labels within generalist retailers' organic assortment, consumers will eventually demand at least a partial realignment of specialist prices with those of generalists. Especially if the specialists' purchasing experience and assortment does not differ significantly from the generalists.

LARGEST SPECIALIST CHAINS ARE THE BEST EQUIPPED AND THE MOST REACTIVE

Most of the largest specialist organic chains benefit from their efficient centralized purchasing structure and have the financial and operational firepower to react. They are already adapting through a range of initiatives.

Biocoop, the largest specialist in France with EUR1.2bn sales and 600 stores, announced partnerships with high-end organic burger restaurant chain Bioburger at the end of 2018 and meal-kit delivery platform Rutabago in early 2019. A new concept "Biocoop Anti Déchet Nation" was opened in Paris in June 2019. This means that over 20% of the assortment is sold in bulk, with a global objective of reducing packaging in the store as much as possible. "Click & Collect" has also been available in Biocoop stores since summer 2019. However, the dismissal of Biocoop CEO in September 2019 should be closely watched as it could be the sign of an internal revolt led by the most conservative members and a step back in the chain's modernization strategy.

In addition to "Click & Collect" in 47 of its stores, Naturalia (EUR260m sales) has entered into a partnership with Amazon for express home delivery and could soon team up with Ocado on home delivery at D+1 thanks to its parent company Monoprix. Naturalia has also recently launched two new concepts, Bio & Vegan (dedicated to veganism) and Origins (dedicated to alternative medicine and well-being).

Towards a wave of consolidation in the French organic retail world

The specialized organic retail landscape is still very fragmented in France with about 30 networks, including only five chains with a genuine national network (i.e. from 200 to 600 stores). Bearing in mind the emerging challenges for specialized organic retailers and the pressure from generalists, we anticipate a wide consolidation in France. Some private equity funds have already led a “Buy & Build” approach by acquiring stakes in some small chains as they identified organic retailing as a promising market for consolidation.

The smaller specialists will seek to come together, whether through the creation of buying structures or mergers, in order to buy better, become more competitive on selling prices and to be able to improve the whole commercial proposition.

In addition to potential groupings between specialists, we are also likely to see the takeover of small specialists by generalists seeking to develop their own chain of stores dedicated to organic products. Carrefour and Auchan emerge as the natural consolidators. Intermarché has already acquired a 16% stake in Les Comptoirs de la bio and Carrefour took over So.bio in 2018. Their objectives are to:

1. Better target the most conservative organic customers, who are also the most concerned about the distribution channel they buy from;

2. Leverage the relationships that specialist chains have established with renowned organic brands and producers to bring them to the shelves of specific supermarkets and hypermarkets;

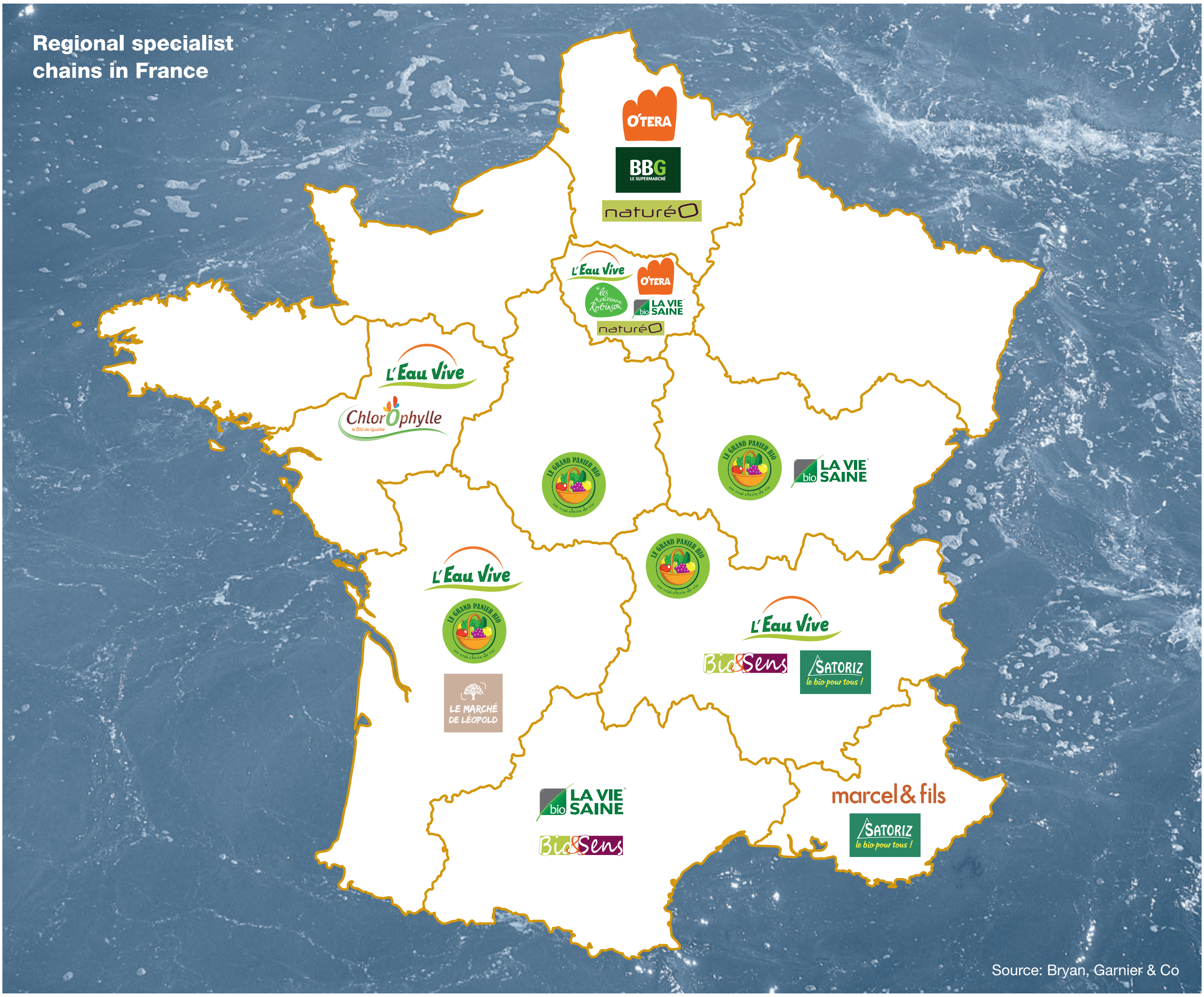
3. Try to open “shop-in-shops” of these specialist brands (e.g. Naturalia) in their hypermarkets and supermarkets.

Looking further ahead, it is clear that the trend towards naturalness that is now impacting food will eventually affect cosmetics – where currently it accounts for only 1.9% of sales at hypermarkets, supermarkets, drive and convenience stores in France – and fashion as well.

National specialist chains in France

SPECIALIST ORGANIC CHAINS	Nº STORES	STRUCTURE	GROWTH TREND 2018
biocoop LA BIO NOUS RASSEMBLE	600	COOPERATIVE	↗
La Vie Claire	355	INTEGRATED	↗
Bio monde	206	COOPERATIVE	↘
NATURALIA	200	INTEGRATED	↗
GROUPEMENT ACCORD-BIO ASSOCIATION DE MAGASINS INDÉPENDANTS	200	COOPERATIVE	→
Bio c' Bon	150	INTEGRATED	↗
les comptoirs de la bio par passion Groupement de magasins indépendants	145	COOPERATIVE	↗

Source: Bryan, Garnier & Co



Regional specialist chains in France

Source: Bryan, Garnier & Co

Conclusion

The organic market still has significant development potential. However, the emergence of supply-related challenges and the need to overhaul the business model could polarize the growth of the market. Size will matter in a specialized organic retail landscape that is still very fragmented and impacted by national issues. Consolidation therefore seems inevitable. The smallest chains are in the front line for this, as they lack the resources to invest and adapt quickly enough.

As organic products represent their main source of growth in a lacklustre environment, generalists should be willing to invest money acquiring specialists, whose commercial and supplier positioning could be leveraged. Carrefour and Auchan could lead the way despite their respective restructuring plans. Casino is already running Naturalia while the associative structures of Leclerc, Système U and Intermarché make any M&A move more complex.

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