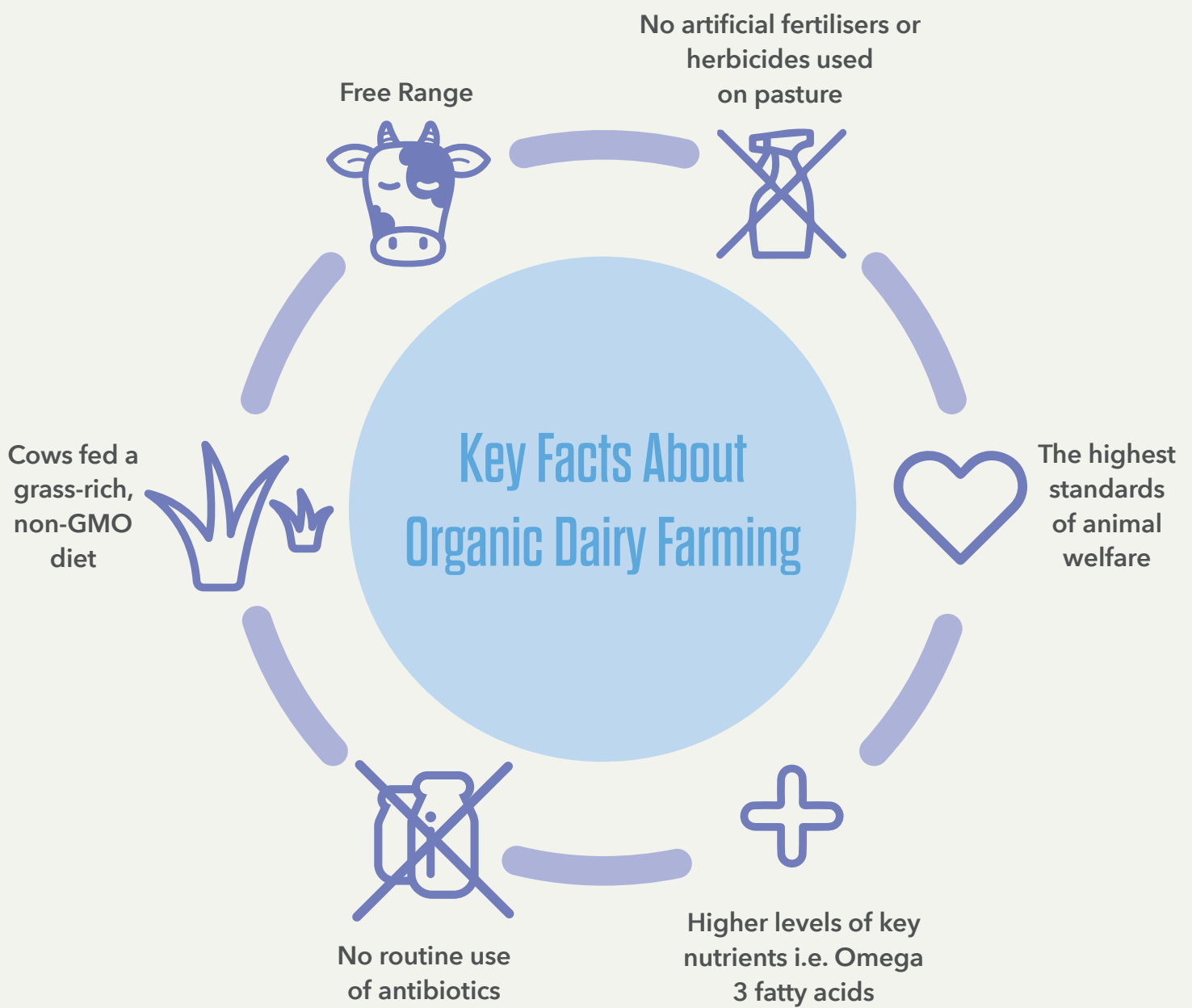




ORGANIC MILK MARKET REPORT 2017





Foreword



Nicholas Saphir
OMSCo Chairman

Strong growth in demand for organic dairy products in many developed and developing world markets is being driven by a common consumer focus on health and wellness.

This is understandable in countries with fast growing wealth such as in parts of Asia, but even where austerity has patchily eroded disposable income consumers have sustained lifestyle choices such as eating out and buying food of choice. However, growth in consumption of organic dairy products has not been homogenous, with demand in the USA for organic cheese and butterfat a key driver, while yoghurt in the UK and infant formula in China have led demand. National variations in growth also reflect local government and retail policy, with liquid sales in the UK only recently increasing, having battled for some time against very low conventional milk prices, while in France government public procurement policy requires support for organics. Despite these national differences, it is clear that where retail shelf space or online offers are available, sales grow significantly. This is particularly the case when brands or retail own label demonstrate innovation and focus on quality rather than just basing their claims on organic credentials.

Trends in consumer demand have many diverse drivers, but a common current feature is the desire to seek products that are simply 'without' such as foods that claim 'as nature intended', pasture fed and especially in the USA a strong demand for certified 'GM free'. In China the main demand is for safe, unadulterated foods. In addition, with the increasing patchy imposition of regulations surrounding Health Claims, on pack scientifically based claims have become harder to substantiate and this has opened the door for products that simply imply improved health such as 'alternative milks'.

While all of these trends currently support the demand for organic dairy, it will be vital for the organic industry to recognise that quality control and science based evidence will increasingly alleviate consumer fear and organic dairy must continue to develop its own positive evidence to

warrant increasing consumer demand. It is important to reinforce the message that organic dairy is pasture based, and managed well leads in providing balanced Omega 3 and trace elements resulting from modern organic pastures and stock management.

This is a good time for organic dairy with encouraging underlying consumer trends, increasing innovation and new product development. If there are clouds on the horizon it will be the tendency to suffer periods of oversupply caused by the very nature of the extended conversion period from conventional to organic often resulting in large amounts of milk arriving at the same time and ahead of market growth. Underlying market growth will absorb emerging new supplies. The only question is how quickly. The UK is in balance and farmers appear to be sensibly evaluating the advantages of conversion against the absence of conversion grants, expensive organic feed and an adequately supplied home market.

It would be impossible to end this short overview without mentioning the uncertainty surrounding Brexit, which hangs over the organic dairy industry as with the rest of agriculture and food as well as other manufacturing and service based industries. Perhaps the biggest uncertainty for organic dairy is not so much trade talks, tariffs and non-tariff issues, but the rather arcane subject of 'equivalence' in standards. This seemingly peripheral issue needs to be addressed before the end of the Article 50 timetable and outside of Trade Agreements. If cheeses are to be produced for export markets extra mature and mature cheddar will need to be produced and matured in 2018 if it is to be available to support ongoing successful exports. This requires acknowledgement that current equivalence regulations will continue to be recognised.

In summary, the indications are that the future remains bright, but it will undoubtedly provide ongoing challenges that will need to be met by one of the most innovative sectors of UK farming and food manufacturing.

Executive Summary

The global organic food and drink market continues to show strong growth worldwide.

- The market is valued at \$82bn and grew 37% over the 5 years, from 2010.
- Globally, the largest single market for organic is the USA, worth an estimated \$38bn and growing at an annual rate of 10.6%.
- The European market is worth \$29bn and is growing by 15% year on year.
- The growth drivers are similar across the world: Health & wellness and an increase in availability and choice.
- Another common feature of countries with a fast growing organic sector is the presence of a vibrant specialist organic retail network.
- There is no direct correlation between the largest markets and per capita consumption: The USA, the largest market, ranks in 7th place in terms of per capita consumption compared with Switzerland, in 8th place in the size stakes but 1st place for consumption.
- Organic exports are a growth area for many countries, in particular the Oceania region where exports out-perform domestic sales.
- The UK market performance has improved over the last 5 years. Valued at £2.09bn, and up 7.1%, it continues to perform ahead of a non-organic food market which is in slight decline.



Globally, organic dairy is one of the largest sectors within organic food and drink worth \$9.5bn and is also showing strong growth. UK retail organic dairy growth is however trailing that of other key markets.

- The USA is the largest market with sales estimated over \$6bn and growing 10% year on year.
- Within European markets, Germany and France are the largest and both are in strong growth.
- The growth drivers of the dairy sector vary by country, for example, in Germany cheese is a dominant and growing sector, but in France the driver is milk.
- In China organic dairy still has a very small share of total sales but this represents a significant opportunity, subject to meeting changing Chinese regulations.
- UK organic dairy is worth £344m, and is growing at a rate of 2.2%, behind total UK organic growth.
- Low relative conventional milk pricing and range rationalisation in organic yogurt have hindered growth over the last year.

UK organic retail milk sales have recovered and over the last year there has been a significant increase in household penetration.

- Last year, the organic milk category attracted more new households than any other milk sector in the UK.
- 1 in 4 UK households are now purchasing organic milk.
- UK organic milk volumes grew by 4.4%, and sales are now back up to where they were before the drop in conventional milk retail prices in 2014.
- Retail distribution increased by 3% year on year, thus like for like retail sales also increased during the period.
- In contrast the standard milk category fell by 1.9%.

Exports have become an increasingly important market for UK organic dairy products and play a key role in balancing the UK market and providing a stable return to producers.

- Organic dairy exports are estimated to account for 20% of total sales versus 9% for total organic food and drink.
- UK organic milk is increasingly sought after to feed growing export markets in addition to covering UK domestic demand growth.
- Exports have become more premium – beginning with simple exports of raw milk to the continent 10 years ago, and now comprising of added value products and dairy specialist ingredients sold across the world.

Global organic farmed land is still behind demand growth.

- Despite growth of 15%, organic farmed land still only represents just 1% of total agricultural land, versus organic sales which represent 4% of total food and drink.

- The distribution of supply is not always in line with demand.
- The supply demand balance varies by country and is cyclical.

There has been an acceleration in global organic dairy production to meet rising demand.

- Over recent years supply in the biggest market, the US, has increased significantly.
- Supply is forecast to increase significantly in Germany, France and to a lesser extent Denmark over the next few years through conversions. This is to meet significant domestic market demand growth, as well as export opportunities both inter-community and further afield.
- A key challenge for further organic dairy expansion is securing adequate global organic feed supplies.

UK supply will increase slightly over the next few years to meet export demand but no further conversions will be required to meet demand forecasts.

- Conversions totalling 60m litres have been secured to meet new export contracts.
- Expansion of existing suppliers is sufficient to meet forecast UK market growth.

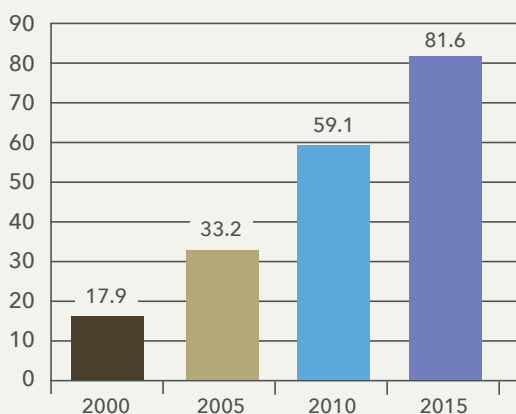


Demand Review

Global Organic Food & Drink Market

The global organic market is currently worth \$82bn, up 37% since 2010. Organic now represents around 4% of worldwide food and drink sales.

Figure 1: Global organic sales 2000-2015 (\$bn)



Source: Organic Monitor

This growth has been driven by a number of factors in recent years: Consumers across the world are becoming more focused on health and wellness, where their food comes from and how it is made. They also have access to more information than ever before to assist their choice. Organic can offer reassurance in this regard. In some countries, it even represents the 'safe' choice, for example in Asian markets where there has been a history of food safety scares. Common to many countries is its relevance in the infant formula market, where pure and natural benefits rank highly.

Increased availability has also facilitated growth, with organic produce on sale across a wider distribution base in most countries. In addition, in certain countries an extra drive towards organic is provided by supportive government procurement policies, for example in France.

Figure 2: Organic retail sales by market 2015



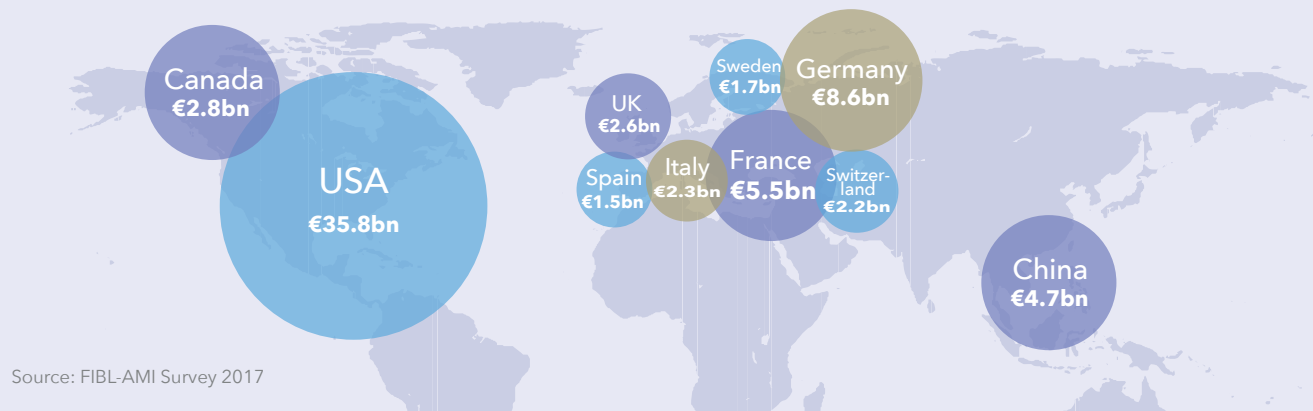
Source: FIBL-AMI Survey 2017

USA



The USA is the biggest market for organic, valued at €35.8bn and representing 47% of total global organic retail sales. Organic food accounts for 5% of total food sales and this grew by 10.6% in 2015. The three West Coast states are particularly loyal organic markets, accounting for over half of natural and organic product sales in the USA.

Solid consumer growth is expected to continue, with strong brand presence, a diverse retailer base and new categories and product ranges featuring organic options, all playing their part.

Figure 3: Top global markets for organic food - retail sales (€bn)

EUROPE



The EU-28 account for the second largest proportion of global organic sales, valued at \$29bn and representing 36% of the market in 2015, up 15% on the previous year.

After the USA, Germany and France continue to hold second and third spot in the rankings for organic food with sales of €8.6bn and €5.5bn respectively in 2015. To note, as well as growth being across retail channels, both these countries have a thriving specialist retail sector. For example, in France, this sector accounts for 36% of organic sales and the majority of these are through specialist retail chains i.e. Carrefour Organic and Biocoop. Sales in this sector grew by 19% between 2012 and 2015.

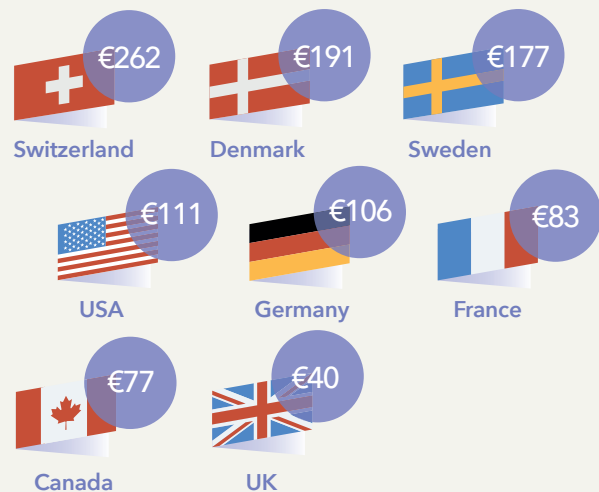
Switzerland is the eighth biggest global market for organic food and drink but has the highest per capita spend on organic products. Organic has successfully infiltrated everyday essentials such as bread and milk where organic accounts for 20% of sales.

The country with the second highest per capita consumption is Denmark and the Danish organic share of total grocery sales is higher than in any other country (8.4%).

CHINA



With sales of €4.7bn, China is the third largest market for organic after the US and Europe. Strong growth seen over recent years is largely attributable to Chinese consumers valuing the integrity of Western organic food following a history of food scares and the growth of affluent middle classes.

Figure 4: Per capita consumption country comparison

OCEANIA

Domestic sales of organic food and drink in Australia were \$1.2bn in 2015 and in New Zealand were \$0.2bn. Both markets are in growth – the Australian domestic organic packaged foods and drinks market (valued at \$540m in 2016) showed moderate growth of 5.4%. Overall domestic sales in New Zealand were slightly ahead of this and between 8-20% depending on the sector.

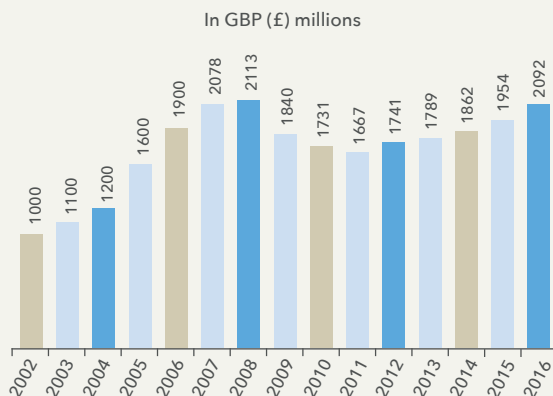
The key point to note for both of these markets is their significant and growing export organic food and drink businesses. In the case of New Zealand, organic food and drink exports are greater in value than domestic sales.

UK ORGANIC FOOD AND DRINK MARKET



Over the past year, the UK organic market has continued to grow and is now worth £2.09bn, up 7.1% year on year. This is the 5th consecutive year of growth and is especially impressive considering non-organic sales fell 0.6%.

Figure 5: UK organic product sales 2002-2016

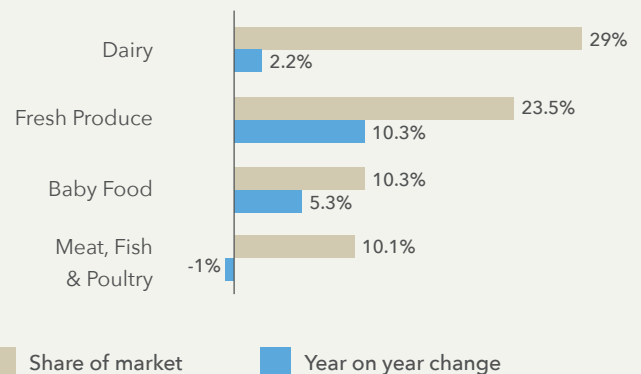


Source: Soil Association Organic Market Report 2017

- Organic now represents 1.5% of the total UK food and drink market.
- The UK holds 6th place for the largest organic market globally.
- UK per capita consumption is roughly half that of France and one sixth of Switzerland.
- Dairy, fresh produce and baby food combined account for around two thirds of organic sales. All three of these sub-sectors achieved growth last year.

- Supermarket sales continue to dominate the organic category, accounting for 68% of value sales, but this share is gradually being eroded.
- Although growth driven by supermarkets (+6.1%) is responsible for most of the sector's expansion, foodservice and home delivery recorded the highest percentage growth last year.

Figure 6: Organic product market share



Source: Soil Association Organic Market Report 2017

Growth Drivers

Health and wellbeing - There has been an increase in consumer mistrust and consumers are more concerned with where their food comes from and what goes into it. The organic label has also featured as a key additional benefit in many healthy food launches (i.e. free from, high protein, dairy substitutes etc).

Wider availability and choice - Supermarkets are increasing their organic ranges, including the discounters who see this as an opportunity to attract more high-end consumers, improve their quality image, and move organic towards a wider consumer base.

Ocado continues to champion organic with the widest organic range of 3000 products while nearly 30% of sales now go through independent retailers and box schemes.

Global Organic Dairy Market

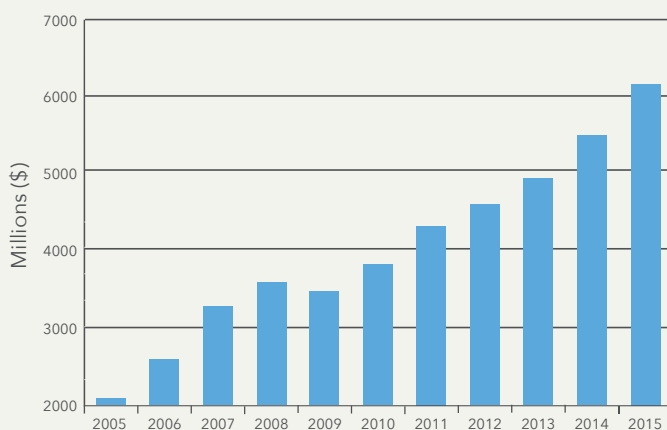
Globally, dairy is one of the most dominant categories within organic and is in strong growth in many countries.

USA



- The USA is the biggest market worldwide for organic dairy products with sales estimated over \$6bn in 2015, up 10% vs 2014.
- Dairy is the second biggest organic food category in the USA behind fresh produce, and accounts for 15% of total organic food and drink.
- Milk is the largest sector within organic dairy with sales of \$3.3bn in 2015, up 6.3% on the previous year. While the regular milk market is forecast to decline 5% by 2020, organic milk is predicted to increase 18%, so that organic product will account for 11% of milk sales.
- The fastest growing organic dairy sectors are cheese, butter, cream and ice cream.
- Growth in the market is largely down to a combination of increased distribution in mainstream retail as well as an increasingly diverse range of foodservice offers and the growing consumer trend for natural, minimally processed foods.
- There are many competing food claims in the US that offer less benefits to the consumer overall but are striking a chord with simple messaging i.e. the non-GMO movement. Facing this, the challenge for organic is to ensure its benefits are even more clearly communicated.

Figure 7: US organic dairy market size and growth 2005-2015



Source: OTA Organic Industry Survey 2016

GERMANY



- The German organic dairy market is valued at €1.1bn and is the second largest global organic dairy market.
- Organic milk is the largest sector within organic dairy in Germany. Compared to the overall milk market, which lost 10% of its value in 2015, organic milk grew 15%. While it now accounts for 13% of milk sales, by 2020 it is expected to account for almost a quarter of the market.
- The total German cheese market is worth around €7.8bn – more than the value of the butter, milk and yogurt markets combined. Organic product accounts for around 4% of cheese sales and value is growing strongly with a 9% increase in sales in 2015.

FRANCE



- The French organic dairy market is valued at €711m.
- The French organic dairy market is amongst the largest in the world and is growing strongly, with sales increasing 9% in 2015.
- French consumers have a strong appetite for organic milk which accounts for half of organic dairy purchases, 11% of all milk sales and €282m of the market. The organic cheese market is relatively small, accounting for just 1% of total cheese sales.

CHINA



- The organic dairy market is growing, although it still only represents 1.3% of total milk value sales. The market share is greater in the infant category where organic represents 7% of volume sales with much of this imported from Australia, New Zealand and Europe.

AUSTRALIA



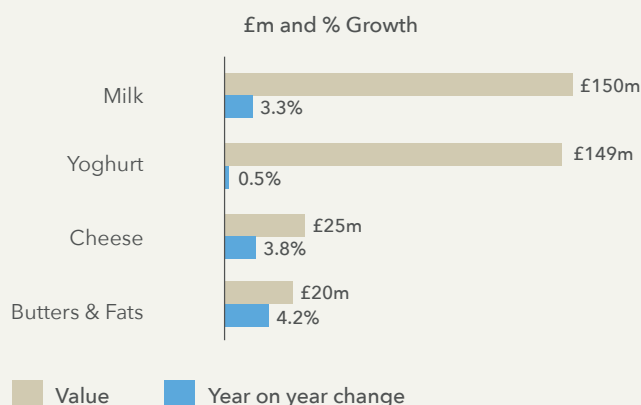
- The Australian organic dairy market has nearly doubled in size from 2008 to 2013.
- Yogurt makes up the largest proportion of organic dairy sales, and products in this category are experiencing solid growth. Organic milk accounts for just 2% of total milk and 22% of organic dairy, low figures in comparison to other countries. Furthermore, the market is declining with sales falling 6% last year, partly down to strong competition from other 'healthy' milk products such as a2 milk.

UK ORGANIC DAIRY MARKET



Dairy is the biggest organic food and drink sector, worth £344m in retail sales and representing 29% of all UK organic food and drink sales. Sales of organic dairy grew 2.2% in 2016 and this was mainly driven by organic milk, as yogurt remained relatively stagnant and other dairy segments grew, but from a low base.

Figure 8: Organic dairy segment product value (£m) and % growth



Source: Soil Association Organic Market Report 2017

Although up 2.2%, organic dairy growth was behind that of total organic food and drink over the same period (+7.1%). Factors constraining further growth were:

1. Yogurt performance was flat (+0.5%) due to a loss in distribution suffered by the Rachel's brand, as well as a reduction in promotional activity overall. Comparatively, Yeo Valley accounts for 74% of organic yogurt sales and the brand's yogurt sales were up 3.3% in 2016.
2. Organic milk continues to be priced at an excessive premium following the retail war led drop in standard milk pricing a few years ago. Organic milk costs nearly twice the price per litre compared to non-organic milk.

Spotlight: UK Organic Milk

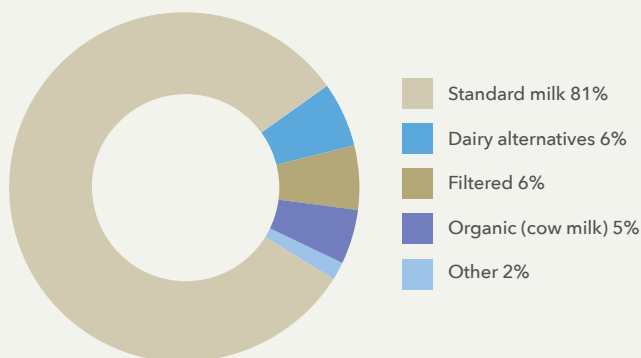
UK MILK MARKET IN CONTEXT

The total milk category is currently worth £2.9bn and while value has grown 0.2% over the past year, volume has fallen 1.8%.

Over the last year there has been more activity in the milk category and attempts to add value to one of the largest remaining commodity sectors. There has been increased press coverage, from the price farmers are paid for their milk, to health benefits and animal welfare, i.e. the launch of free range dairy. However standard milk is still overall a low involvement purchase, driven in the main by fat choice.

There has been new product innovation and total milk category advertising has increased by 50% to £15m. Whilst still a long way short of the NPD and advertising expenditure in similar sized grocery categories, it is a positive move.

Figure 9: Milk segment value share

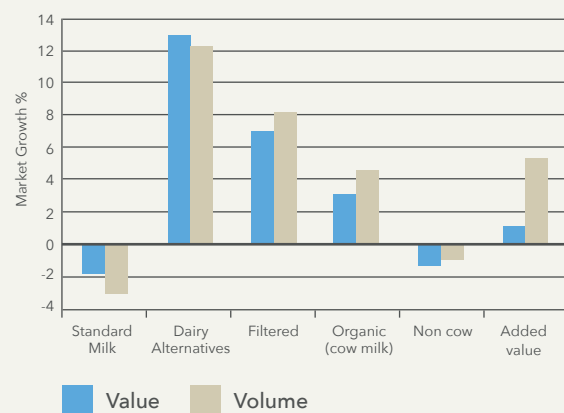


Source: Nielsen Scantrack MAT 25-2-17

Standard Milk

Standard milk accounts for 81% of total milk. While value sales have fallen 1.9% yoy, volume sales have declined slightly faster (-3.0%), due to a slight recovery of the standard 4 pint price in certain retailers (i.e. Asda 95p to 99p) leading to an overall 2% increase in the standard milk average selling price over the last year.

Figure 10: Market growth by product type



Source: Nielsen Scantrack MAT 25-2-17

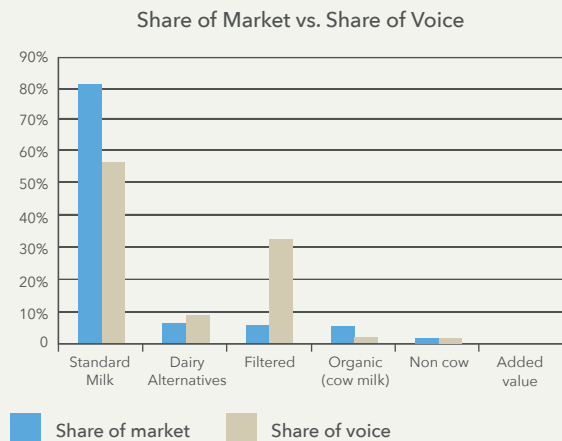


The total milk category is currently worth £2.9bn

Dairy Alternatives

One of the key sectors which is driving growth in the market continues to be dairy alternatives, now worth £191m, up 13.4% on last year. The main reasons behind the growth of dairy alternatives include a continuing consumer health trend, and extensive advertising and NPD which has helped to fuel distribution growth. Sector advertising spend is nearly double the market share, which has undoubtedly played a role in bringing in new consumers to the category.

Figure 11: Total coverage, milk by product sector



Source: Nielsen Scantrack MAT 25-2-17 & JAA Media

Filtered Milk

Another sector which is experiencing strong performance is filtered which is currently worth £186m, up 7.2% yoy. This has been driven in the main by the Arla Best of Both which is now worth just over £10m. Cravendale continues to be the main brand in this sector and although flat year on year, has found a loyal customer based on its extended shelf life POD, of particular relevance to consumers when buying milk from independent or corner shops.

Organic Milk

Organic is valued at £150m, and has grown 3.3% yoy. It is worth noting that in contrast to most premium sectors of the milk category, organic milk is a private label dominated sector (77%) so in general there is less NPD and advertising.



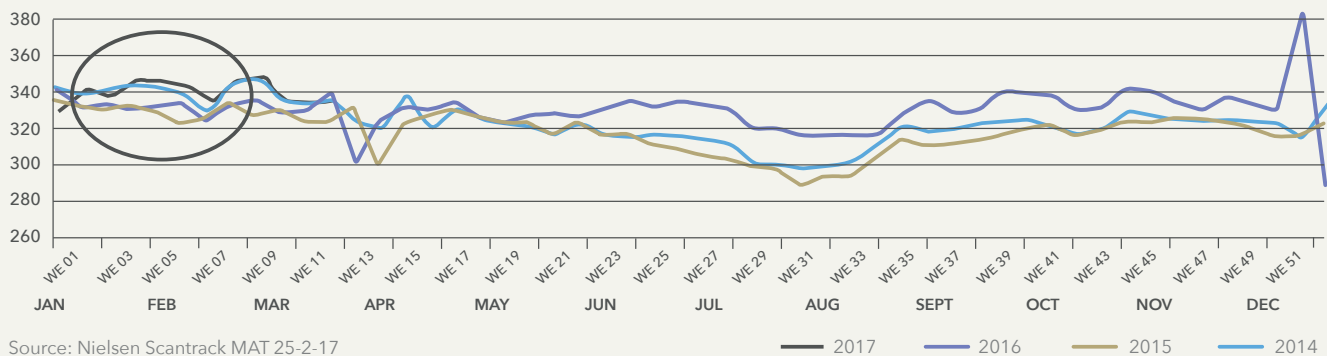
**THE UK HOLDS 6TH PLACE FOR THE
LARGEST ORGANIC MARKET GLOBALLY.**

UK ORGANIC MILK MARKET

i. RETAIL

UK organic milk retail sales increased 3.3% in 2016, bringing the value of the market up to £150m. Volume sales were also up on the previous year by 4.4% to 169m litres. Sales are back up to 2014 levels, having now recovered from the impact of the retailer price wars which caused a retail-wide major drop in the conventional milk price.

Figure 12: UK organic milk volume sales (000's litres)

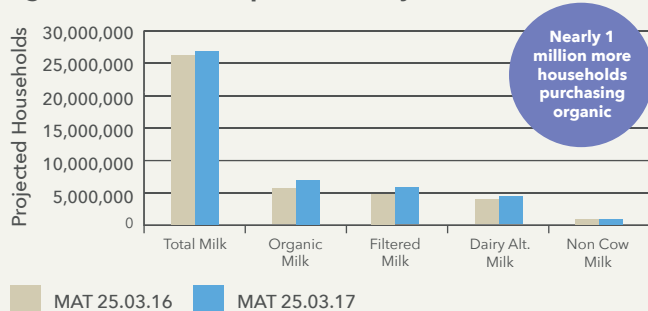


KEY GROWTH DRIVERS

Increase in Households Buying

Most of the growth has been driven by new consumers entering the market across all demographics. There was a 15% increase in household penetration over the last year and the absolute increase in households purchasing organic milk was higher than for any other of the milk sectors currently in growth (i.e. filtered milk and dairy alternatives).

Figure 13: Household penetration by milk sector



KEY FACTS



£150m

Size of market



1 in 4 UK households purchasing



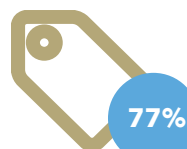
3.3%

Up 3.3%



50%

Tesco & Sainsbury's account for 50% of organic milk sales



77%

77% of sales are private label



17%

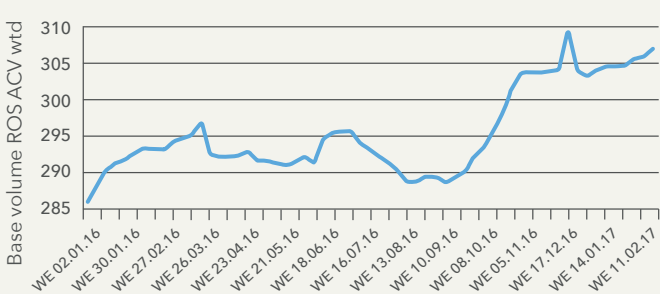
17% of sales are Yeo Valley

Healthy Underlying Sales Trend

This increase in household penetration is reflected in an upward trend in base sales per point of average distribution. In short, even when removing the effect of any increases in distribution and promotional volume, organic sector volume sales still have increased.

Central to this increase is the gradual overall switch of consumers to organic for perceived health, provenance and integrity benefits.

Figure 14: Organic milk base sales trend

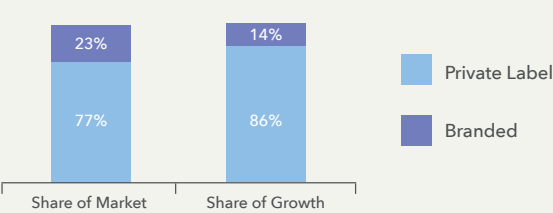


Source: Nielsen Scantrack MAT 25-2-17

Both Private Label and Brands Driving Growth

Compared with the other growing milk sectors of filtered milk and dairy alternatives, organic has the highest private label share with 77% of sales private label. In other such grocery sectors where private label dominates, this typically means less investment in advertising and NPD and this in turn often means lower levels of growth. However, organic has still managed to attract more new households than other heavily branded segments like filtered milk and dairy alternatives.

Figure 15: Organic milk share of market vs. share of growth

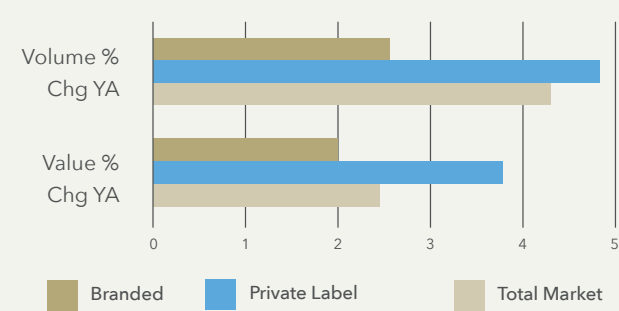


Source: Nielsen Scantrack MAT 25-2-17

While private label accounts for 77% of the market, it has been responsible for 86% of the growth seen over the past year. This has largely been driven by competitive organic own label pricing in Asda and Tesco.

That is not to say private label is single handed in driving growth - branded performance has also improved on last year with Yeo Valley, Calon Wen, Grahams and Arla all in growth, to the detriment of the Nestle Rachel's brand.

Figure 16: Organic milk branded vs. private label growth

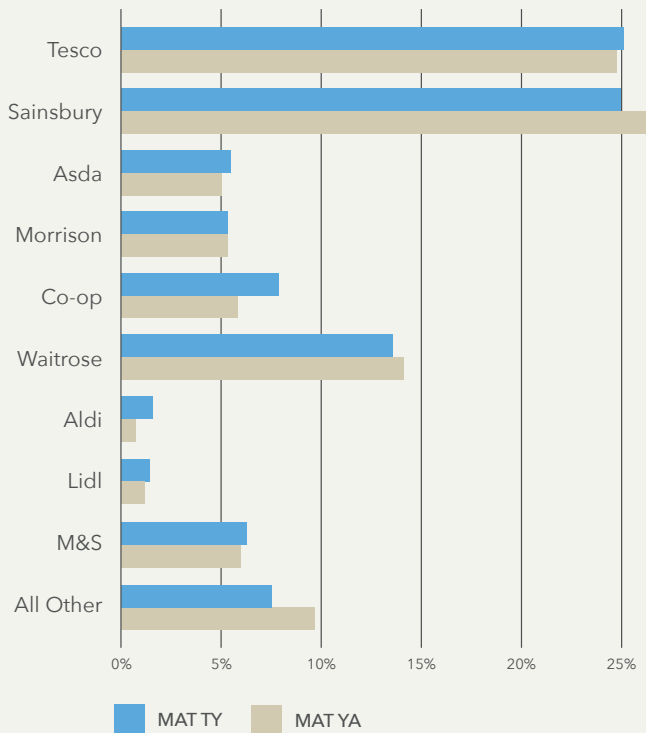


Source: Nielsen Scantrack MAT 25-2-17

Increased Retail Distribution

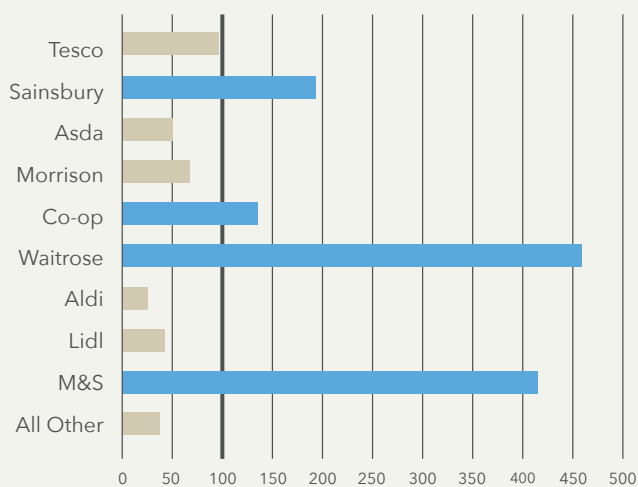
Tesco and Sainsbury's account for the majority of UK organic milk sales with around 50% of sales coming from these two retailers alone. While Tesco's performance in organic milk has been supported by its ongoing 2 for £3 promotional offer, Sainsbury's share of the market has dropped slightly as it has moved away from multi-buys, and Co-op and the discounters have gained share as they have made a conscious push on organic.



Figure 17: Organic milk share of retail trade

Source: Nielsen Homescan MAT 25-3-17

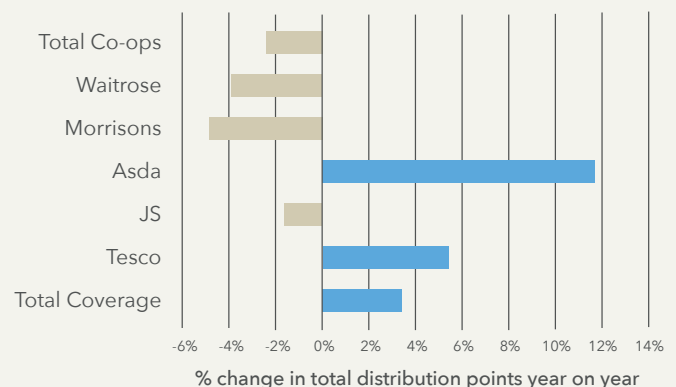
Waitrose, Sainsbury's and M&S continue to over-trade in organic milk, a reflection of their tendency to attract more AB consumers.

Figure 18: Index organic sales to total category

Source: Nielsen Homescan MAT MAT 25-3-17

Overall distribution points for organic milk increased by 3% driven by Asda and Tesco due to their ranging of the new Arla Organic Farm Milk product.

At the time of writing this report, the latest branded organic launch, and the first one in several years, has been on sale for four months but the effect of the advertising campaign is not yet available in the retail data supplied. It is too early to suggest therefore how successful this product is likely to be, however the very competitive RSP of £1.25 for 4 pints, cheaper than both private label and branded organic products, does provide a response to non-buyers who cite their main reason for not buying organic is that 'it is too expensive'. However, the challenge that still remains for any brand in the milk category trying to attract new consumers, is to 'break the trance' of mainly auto-pilot, cap colour purchasing.

Figure 19: Distribution trend

Source: Nielsen Scantrack MAT 25-2-17



ii. EXPORT MARKETS

UK organic exports are on the rise with exports accounting for on average 9% of organic producer sales, as companies capitalise on the British organic reputation for quality and integrity.

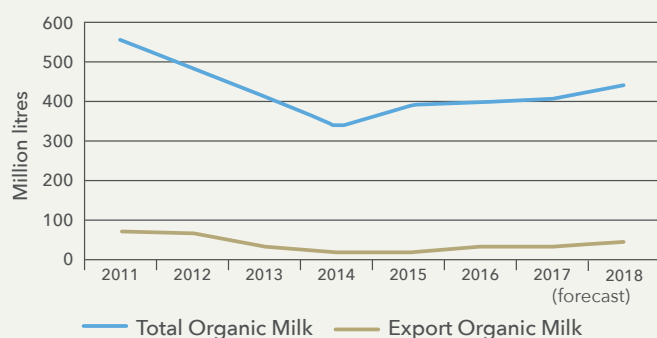
For dairy/chilled/frozen products in particular, exports account for 13% of sales.

With demand for organic dairy rising in almost every major market, there are extensive opportunities for UK organic dairy exports in particular. While the impact of Brexit on organic exports is yet to be fully understood, what can be said is that it is likely to open the door to new, potentially more favourable, trade deals with non-EU countries. Therefore, an export strategy which focuses on destinations outside of the EU and that spreads risk across different geographical markets would be a logical response.

Dairy exports have transitioned over the years from commodity raw milk sales to mainly Europe, to added value products including cheese and more specialist products (i.e. infant formula grade powders and whey) now sold across the world. UK production of organic cheese for export is now in excess of production for domestic sales.

However, expansion of organic dairy exports has been constrained in the last couple of years by a lack of supply due to the UK market recovery.

Figure 20: UK organic milk production vs. UK organic milk exports



Source: OMSCo estimates

Top 5 Global Organic Markets of Interest

USA



Organic is the fastest growing sector in the US food industry with sales up 11% in 2015, far surpassing growth in the wider food market of 3%. US organic production is struggling to meet this rapidly increasing demand and there is a significant reliance on imports.

CHINA



Widespread distrust of domestic dairy is driving the demand for foreign imported milk. Organic dairy is growing fast and this is expected to continue over the next 5 years. There have been some challenges for exports based on changing government regulations and this is likely to continue.

CANADA



The Canadian organic market is of similar size to the UK and the possibility of a free trade deal between Canada and the UK looks plausible.

THE NORDICS



With good growth and some of the highest per capita spending on organic in the world, there is a substantial opportunity for exports to the Nordics where consumers typically respond favourably to UK products.

WESTERN EUROPE



Western Europe is an organic market of undeniable importance with sales in France and Germany alone amounting to €14.1bn.

Demand Outlook

- Organic benefits are in line with the broad consumer trends of health, provenance and animal welfare and therefore the sector offers significant opportunity for growth.
- The UK organic dairy market is in growth, but compared to key European countries and the US, this growth is off pace.
- To unlock the growth potential there continues to be a need to communicate the organic benefits to consumers in a more compelling way and / or to offer a better price:value proposition.
- Export demand for British organic dairy continues to offer significant growth opportunities and is currently outpacing that of the domestic market.



Supply Review

Global Organic Food & Drink Production

Although global land farmed organically increased by 15% in 2015, it still only represents 1% of global agricultural land.

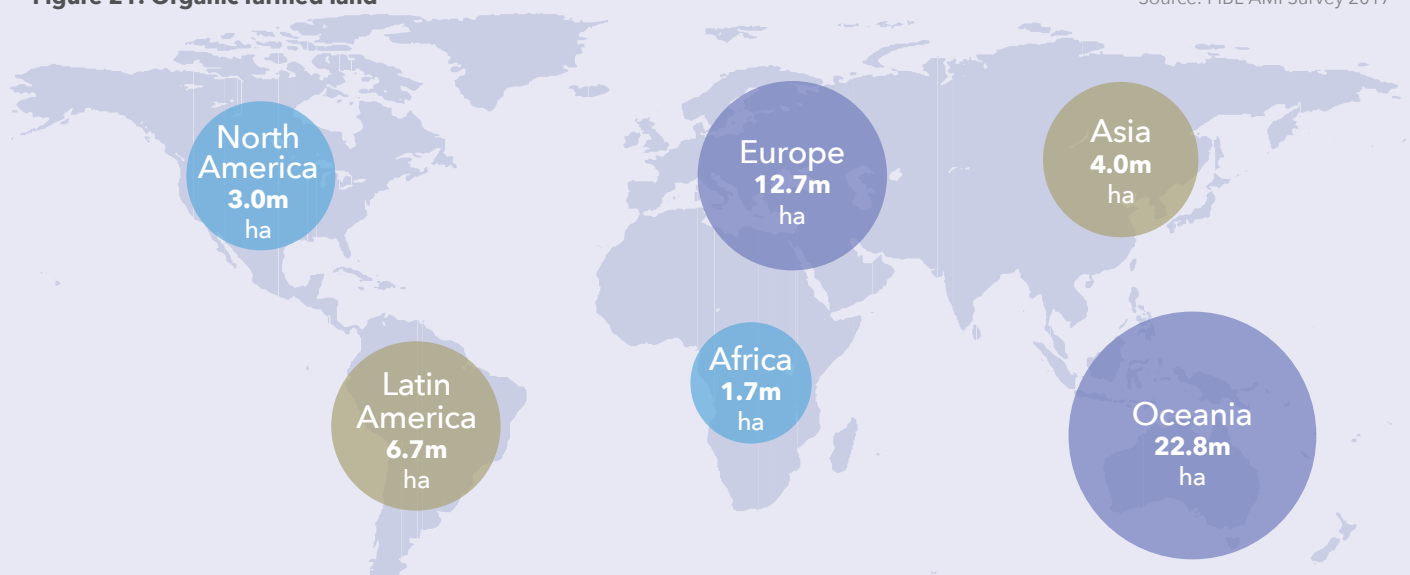
The supply distribution does not always match market demand; in certain regions demand growth is outpacing supply, for example the US (half the world's organic demand but less than 10% land supply).

The key challenge for growth markets moving forward will be sourcing sufficient local supply to satisfy demand. This will take time, and in the meantime it opens up significant export opportunities for countries which have available supplies. For example, the US imports 65% of its overall organic food and drink sales.

- An estimated 51 million hectares of land worldwide is farmed organically.
- This represents around 1% of agricultural land globally.
- Organic farmed land has grown by 15% since 2014.
- 179 countries are now farming organically.
- Leading regions of the world are Oceania (45%) followed by Europe (25%) and Latin America (13%).

Figure 21: Organic farmed land

Source: FIBL-AMI Survey 2017



AUSTRALIA



22.7m hectares (44%) of world supply

- Land is overwhelmingly dedicated to very extensive grazing land for beef cattle production, with little impact for dairy or produce.
- +4.4m hectares since 2015.
- Equates to 1.25% of total agricultural production.
- Mostly exported with particular focus on Asian markets.

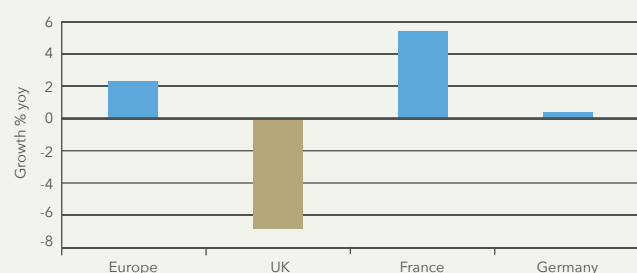
EUROPE



12.7m hectares (about 25%) of world supply

- Organic production accounts for 2.5% of agricultural production.
- Europe grew by 2.3% in 2015 with France leading the way.
- Spain ranks number 1 in terms of organic land availability in Europe.

Figure 22: Growth in European organic land



Source: FIBL-AMI survey 2017



UK



521k hectares

- Growth in UK organic land area off the pace.
- Down 6.7% year on year, whilst organic food sales grew by 7.1%.
- Conversions up slightly (5%) but from a low base (only 3.9% of total organic land).

LATIN AMERICA - ARGENTINA



3.1m hectares

- Around half of Latin America supply.
- Mostly exported.

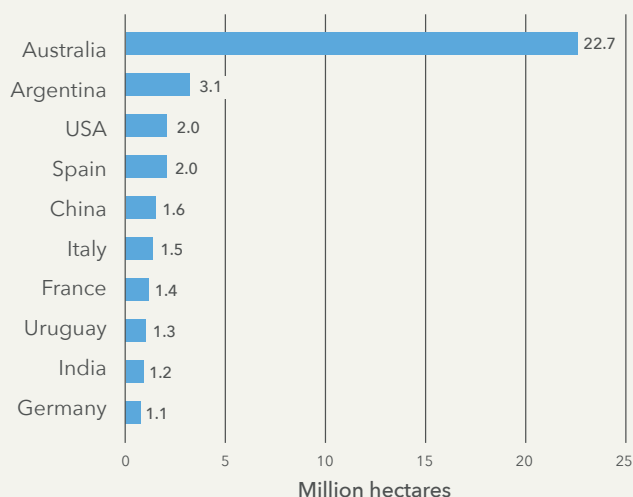
USA



2m hectares

- One of the most notable markets where demand growth is outstripping supply; organic is 5% of food sales but just 1% of farm land.

Figure 23: The ten countries with the largest areas of organic agricultural land 2015



Source: FIBL-AMI survey 2017

Organic Dairy Production

- Global organic dairy production is increasing and is essentially focused in the key markets where sales are high; namely North America and Europe.
- Certain regions are ahead of others in supply growth and this is related to how long the domestic market has been growing and to what degree.
- Overall, supply growth in key markets is forecast to be in line with demand growth (taking into account domestic growth and export opportunities) therefore maintaining a balanced supply / demand picture.
- UK dairy conversions are minimal, especially in comparison to key European markets such as Germany and France, and have entered the system later. In addition, the volume is destined mainly for export markets rather than to meet domestic growth which can be covered by existing suppliers.
- There is risk of short-term over-supply in some markets due to the phasing of conversions, i.e. in Europe.
- A global threat to continued supply growth for many countries, is the availability of and access to global organic feed supplies.

USA



- The USA produces 6bn litres and this has grown +10% yoy.
- California and Wisconsin are the heaviest organic dairy producers, in line with market sales concentration.
- Supply growth has not always kept a pace of demand: Just 3% of dairy cows were certified organic in 2011 but interest in conversions increased significantly in 2016 in particular, when conventional dairy prices fell.
- Conversion takes 3 years and currently supply is ahead of demand, but this situation is cyclical.

CANADA



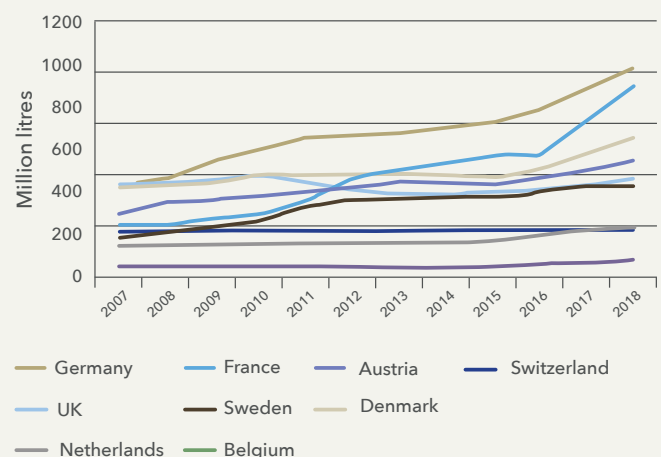
- Canadian organic milk production has doubled over the last 8 years and in 2014/15 was equal to just over 1bn litres, representing a 6% increase year on year.
- Quebec produces 40% of the country's organic milk.

EUROPE



- Europe produces approx. 3.0bn litres and this has increased by 2% year on year.
- 5 countries account for circa 75% of total production (Germany, France, Denmark, Austria and the UK).
- Over the last 10 years production has doubled in France, Austria, Germany and Sweden.
- Growth in Denmark has been comparatively slow and in the UK production has been stagnant.

Figure 24: European organic milk production forecasts



Source: European Organic Dairy Producers

Organic milk supply is forecast to increase significantly in Germany, France and to a lesser extent Denmark over the next few years, adding approx. 1bn litres to European supplies in the next 3 years. This is due to:

1. Significant domestic market demand growth.
2. Export opportunities, often inter-community, E.g. 30% of the organic milk used in processing in Germany is imported and Denmark sells the most organic milk to other countries in the EU.

Whilst a large number, it represents around 25% of the current market which will do little other than to cover 3 years of existing consumer growth, so overall there is little change expected in the supply/demand balance in the EU over time. However, the phasing of the new milk arrivals during 2017-2019 could have a short term impact on the market.

Figure 25: UK organic milk production

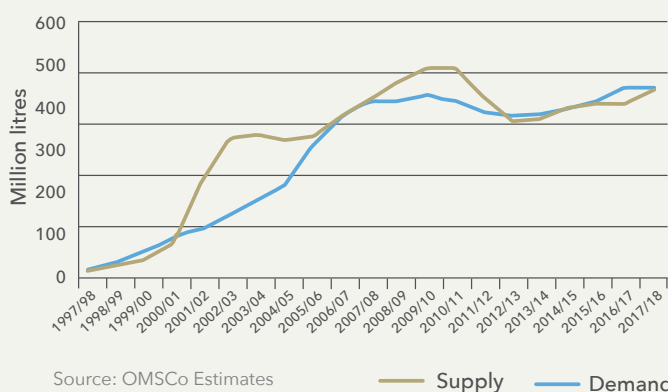
Supply	11/12	12/13	13/14	14/15	15/16	16/17	17/18
Base UK supply	501	431	370	377	400	400	400
Planned expansion	-1%	-6%	2%	6%	3%	3%	6%
Supply from existing producers	496	405	377	400	412	412	424
New entrants	0.0	0.0	0.0	0.0	0.0	0.0	20
Exits	-65.0	-35.0	0.0	0.0	0.0	0.0	0.0
Gross supply available	431	370	377	400	412	412	440
Utilisation	98%	99%	99%	99%	99%	99%	99%
Total utilisable UK supply	422	366	373	396	408	408	440
Imports	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total available supply	422	366	373	396	408	408	440

Source: OMSCo Estimates



- Produces around 13% of the EU's organic raw milk supply.
- Dairy supply is concentrated in the South and West of the UK but there is a national supply, with over 400 producers from Land's End to Inverness.
- Over the last few years supply in the UK has matched demand, however recently increased demand from export markets in particular on top of moderate growth in the UK, has meant that export expansion has had to be dramatically scaled back in order to cover the domestic market.
- As a result circa 60m litres have been recruited to meet export demand over the next few years, but currently no additional expansion in supply is forecast.
- Innovative partnerships are increasingly a feature of managing global supply. For example, Organic Valley (the leading organic dairy co-operative in the US) and OMSCo (UK) have become members of each other's co-operative, holding one share, and trade dairy products back and forth to balance supply and demand fluctuations in domestic markets.

Figure 26: Organic milk supply vs. demand (litres)



Conclusion

Globally organic food and drink is in strong growth and organic dairy is a key sector within this, valued at \$9.5bn. The consumer drivers behind this growth are well documented and are only likely to become even more relevant over coming years.

In many countries, organic dairy supply has not kept pace with demand growth and in addition to this supply tends to be cyclical in nature, therefore opening up opportunities for exports.

Organic dairy is the biggest sector of the organic food and drink market, valued at £344m, and is in growth. However this growth has been trailing that of other key countries. Within the organic dairy sector, liquid milk has been responsible for most of the growth, and sales last year grew by 3.3% to £150m. This is despite historically high retail price premiums versus the non-organic equivalent, as supermarket price wars drove conventional prices down whilst margin recovery drove organic prices up.

Private label organic milk is purchased by 1 in 4 households and last year nearly one million more households purchased it for the first time. This is all the more impressive, given the context of a sector that has low advertising spend, little to no innovation and promotion, and is dominated by private label. Underlying like for like sales have picked up over the last year, signalling a gradual shift in consumer attitudes and beliefs; the timing of this change does coincide with the press launch of a research report from Newcastle University on the benefits of organic milk. This cause-effect is reflective of a mainstream consumer perception that organic milk is 'better in some way', but like anything, unless we are reminded about something, and hear about it regularly other messages prevail. Advertising spend in the milk category is already low given its size, and organic accounts for less than 1% of this spend.

A category that manages to still convert consumers despite the lack of traditional levers is no mean feat.

Retail support for organic continues to increase with total distribution points increasing by a modest 3% and for certain retailers it has been used as a tool to entice higher income consumers through their doors. The real step change for organic will be when retailers and government assign it a more strategic role. There are a few examples in the UK but nothing like the picture in countries like France, where the Government supports organic through its public procurement policies and organic-only grocery chains like Carrefour Bio and Bio Coop have developed a substantial retail presence. As a result, France's organic dairy demand has increased from just half of that of the UK in 2005 to being 50% larger.

UK organic milk supply has seen more significant expansion than it has in recent years but still at a very modest level compared to other countries. But then this is not surprising as there has not been the same need to expand to cover domestic growth. Europe's organic milk supply will increase by 25% in the coming 3 years (about 900m litres), of which the UK will have new supplies of milk from conversions of just 60m litres. These have



been recruited against known export demand and given the growth in the UK market, will now enable exports to expand as over the last few years they have been constrained in order to maintain supplies to the domestic market.

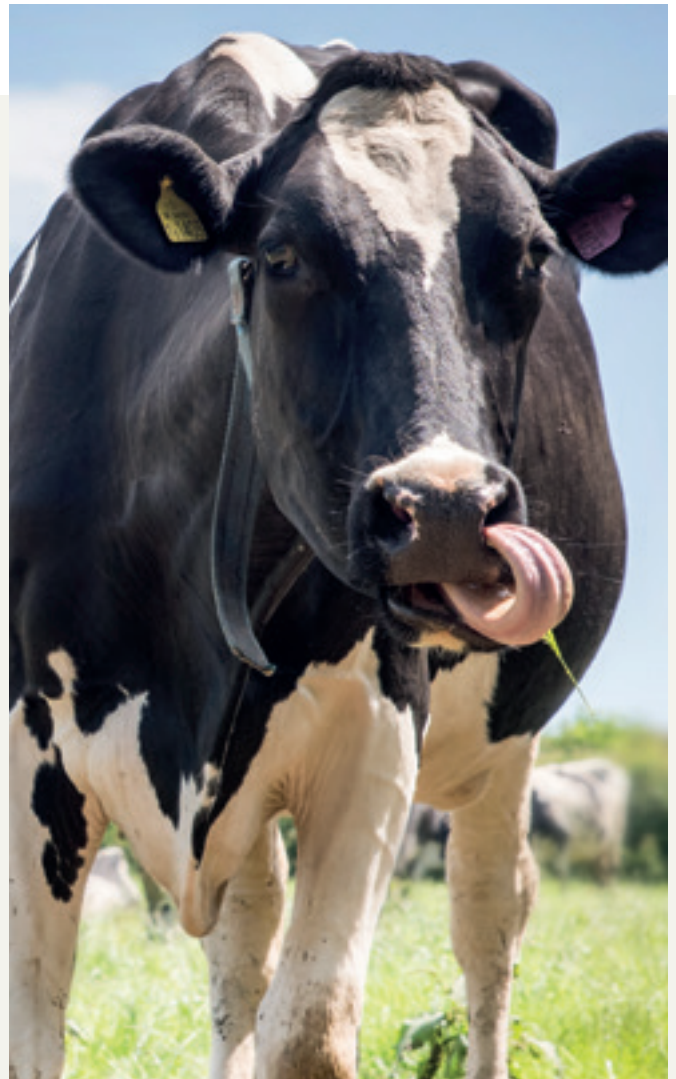
Looking forward there is the unknown of Brexit and an element of risk as new milk hits the European market, but equally there is opportunity and the confidence that from an end market and consumer perspective, organic hits the spot in terms of emerging consumer needs, and so can only play a bigger role than it does today.

Periods of over-supply on the continent are unavoidable but will be short-lived as the new milk is needed to meet the current rate of demand growth. Brexit is more of a critical and near-term challenge for organic dairy exporters due to the EU-US Organic Equivalency agreement which enables EU producers to sell their products as USDA certified organic in the US. If this agreement is not extended to cover the UK once the UK leaves the EU, then Europe's primary organic dairy exporter to the US will hand over this entire market to the remaining members of the EU.

In the domestic market, increasing the pace of the switch to organic milk requires the combined efforts of brand owners, retailers and producers to improve presence on shelf, enhance the on-pack communication of organic benefits, increase the promotional weighting in the category and leverage the on-trend benefits organic provides.

At the same time, with rising conventional milk prices the retail premium for organic milk is likely to fall in the coming 12 months, which will promote further trial and switch onto organic dairy products.

British organic dairy is the 'raw material' that provides the customer with a platform for on trend, persuasive propositions and communications. The question is not about growth. The question is about how much and how fast, and whether this growth is domestic or export-led.



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JAA media

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