

The Economics of Organics¹

John Ikerd²

Most people probably would think of the economics of organics in reference to the rapid growth in markets for organically grown foods. As I mentioned in my earlier presentation at this conference, sales of organic food and beverages have grown from an estimated \$1 billion in 1990 to \$29.2 billion in 2011.ⁱ Organic cosmetics, health care products, and clothing add another \$2.2 billion to sales of “certified organic” products. Organic sales grew at average rates of more than 20% per year during the 1990s and have held in the 10% range since the “great recession” of 2009. The growing preference for things organic extends well beyond *certified* organic products, as attested by the existence of the Organic Horticultural Benefits Alliance, which is “dedicated to the education of *organic and sustainable lawn and garden practices* in the Houston metro area.” Organic home gardening and lawn care are generally not *certified* organic.

Non-certified products and services are frequently marketed as “organic” because of the growing consumer demand for products that are safe to eat, safe to use, or safe to be around. A growing number of consumers want products that also are produced without degrading the land, exploiting other people, or polluting the natural environment. The growth in *Fair Trade* is probably the most visible indicator of this trend.ⁱⁱ Organic is commonly used as a simple and convenient term to use to communicate a range of characteristics that consumers increasingly prefer when purchasing goods and services. This shift toward organics in consumer preferences obviously represents an opportunity for businesses to increase profits by producing both certified organic and “organic-like” goods and services. However, the shift in consumer preferences in favor of things organic is far more than another consumer fad or marketing craze that will be out of fashion as soon as “the new wears off.”

Those businesses that treat the growing public demand for organics as just another profit opportunity may well find themselves out of business when their customers discover their lack of ecological, social, and economic integrity. Market surveys generally indicate that most people who are willing to pay premium prices for organic products and services are concerned primarily about safety or purity. However, many are also concerned about the ecological and social impacts of their purchase decisions. They are concerned about how employees, and farm animals, are treated by those who produce the products or provide the services they buy. They are concerned about the long term impacts of their choices on earth -- air, water, soil, energy, and the overall natural environment. They are not only concerned about protecting themselves and their families but they are concerned about the health and well-being of future generations. They want to meet their own needs without diminishing opportunities for others to meet their needs as

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² John Ikerd is Professor Emeritus, University of Missouri, Columbia, MO – USA; Author of, *The Essentials of Economic Sustainability and Sustainable Capitalism*, <http://www.kpbooks.com>, *A Return to Common Sense*, <http://Amazon.com>, *Small Farms are Real Farms*, Acres USA, <http://www.acresusa.com/other/contact.htm>, *Crisis and Opportunity: Sustainability in American Agriculture*, University of Nebraska Press <http://nebraskapress.unl.edu>; and *A Revolution of the Middle and the Pursuit of Happiness*, <http://sites.google.com/site/revolutionofthemiddle/>; Email: JEIkerd@gmail.com; Website: <http://faculty.missouri.edu/ikerdj/> or <http://www.johnikerd.com>.

well, including others of future generations. They are concerned about sustainability. The growing preferences for things organic are inseparable from growing concerns for ecological, social, and economic sustainability.

A general perception persists in the sustainable/organic community that the economics of organics is no different from contemporary, neoclassical free-market economics. If individuals and businesses were better informed about the long run economic consequence of their decisions, they claim, maximizing profits or individual self-interests would ensure sustainability. Virtually every major corporation in the U.S. has a “socially responsible” or sustainability program that is based on this premise. They suggest to investors that being a socially responsible or sustainable company need not compromise their economic bottom line. This misperception is prevalent and persistent even among many prominent advocates of organics and sustainability. They believe the economic incentives are adequate to ensure sustainability, or at least would be adequate if people were better informed and our market economy worked more *efficiently*.

Ecological economists believe we also need to “get the prices right” by *internalizing* the social and ecological *externalities* of our economic activities. They admit to so-called market failures or situations where market prices fail to reflect the impacts of individual and business decisions on the economic value of natural and human resources – meaning nature and society. They propose various government tax incentives and regulations that would force businesses to consider the “full economic costs” of their decisions. While more efficient markets and internalizing externalities both are *necessary* to ensure economic sustainability, they are not *sufficient*. The inherent danger in focusing on market-based strategies is that we risk allowing the necessary to become an obstacle to the sufficient. In other words, we may simply slow the rate at which our economy and society continue moving in the wrong direction – until it's too late to change course.

First, the strategies of efficiency and internalizing externalities are based on an understanding that it would be more economical in the “long run” to protect, renew, and regenerate the natural and human resources that ultimately must sustain the economy. As a general statement, this is true. All economic value is derived from nature by way of society. There is no place to get anything other than from nature – earth, water, air, and energy. Once we move beyond self-sufficiency, we become dependent also on society, to help us transform the things of nature into things that have economic value. As long as we barter with people we know *personally*, we can maintain a *social* economy. However, as our economic relationships become more complex and *impersonal*, we need a monetary or currency-based economy to facilitate our trades or transactions. Today's economy is an impersonal, money-based economy.

The fundamental problem is that impersonal economies place an economic premium on the present over the future. The promise of receiving a smaller economic return next week or next month may be far more valuable than the promise of receiving a larger return deferred until next year or next decade. This is why many consumers willingly pay interest when they borrow money and others expect interest when they loan them money. This is why investors give priority to investments that promise quicker returns over those for which returns will be deferred further into the future. At an interest rate of 7%, a given amount of money ten-years in the future is

worth only half as much as the same amount of money today... because money invested at a compounded interest rate of 7% will double in value in ten-years.

With respect to the economics of investing for “long run” economic sustainability, a given monetary benefit or cost expected 100-years in the future has less than 1/1000th as much economic value as the same amount of money received today. Obviously, investments made for the benefit of future generations cannot compete successfully with investments promising positive economic returns next week, next year, or even next decade. At a typical corporate rate of return of 15%, values of investments double every five years, which discounts expected future costs and returns even more severely. This is why many corporate planning horizons only extend five-to-seven years into the future. Anything beyond that is of little economic consequence.

Products and services have economic value only if they are scarce, meaning there is not enough available for everyone to have all they want without giving up something else, usually by spending money. Admittedly, as the resources of nature – minerals, water, air, energy – become depleted or degraded, they become *scarcer* and thus more economically valuable. More *efficient* markets would be capable of reflecting these increasing economic values more effectively, thus providing increasing economic incentives to conserve, ration, and find renewable substitutes for nonrenewable resources. But, things of nature often become ecologically and socially scarce long before they become economically scarce. The best current example perhaps is global climate change. By the time protecting the global climate becomes economically valuable to investors it may well be too late to reverse the process. Likewise, if we wait for the degradation of civil society though economic inequity to become economically valuable, society at that time may lack the collective civil capacity to restore itself.

Consequently, to ensure long-run economic sustainability we must be willing to make investments that are purely social or ethical in nature and thus have no economic value. There is simply no economic value in doing anything for the sole benefit of someone else or for society as a whole, certainly not for the benefit of those of future generations. This is not a market failure or lack of efficiency; markets can only reflect economic values. Internalizing externalities can only assign dollar-and-cent costs and benefits to those things that have *economic* value. If we are to create a sustainable economy we must make social and ethical investments that have no economic value. Sustainability is about intergenerational equity: Meeting the needs of both present and future generations. The needs of future generations can never be given anything approaching equal consideration when decisions are based solely, or even primarily, on economic value.

In general, those who are concerned about sustainability need to understand that economic relationships are fundamentally different from social and ethical relationships. *Economic* relationships are individual, impersonal, and instrumental. Economic value is *individual* in that it accrues to individuals and not to families, communities, or societies as wholes. An economy is nothing more or less than a collection of individual economic enterprises and organizations. An economic relationship is *instrumental* because it is a means to a further end, specifically, to gaining something of greater economic value. This is the reason it makes no economic sense to invest in anything if the payoff is deferred until after you are dead and why the economy gives

priority to the present over the future. Finally, an economic relationship is *impersonal* because if we can't buy, sell, or trade something to another person, it has no economic value.

Social relationships also are *instrumental* in that they depend on reciprocity or expectations of receiving something in return. Unlike economic relationships, the expectations from a social relationship may not be specific with respect to what, when, or where. Regardless, if we expect to have a friend we must be a friend. The value of social relationships is not economic, because social relationships are inherently *personal* in nature. A social relationship with one person is fundamentally different from a social relationship with another person, even if both are friends, family members, or neighbors. Social relationships cannot be exchanged or traded to another person. Social value is *interpersonal* in that it depends on relationships among specific persons.

Perhaps most important with respect to sustainability, social values naturally evolve into ethical values. Ethical values are a particular culture's interpretation of morality or the basic principles or laws of nature that govern all relationships. A societal or community ethic is a code of conduct that applies to all people in all situations within that community or society. A cultural ethic evolves over time from a society's collective experiences from personal social relationships. As social relationships become less personal, people begin to understand the personal values they receive as individuals arise not just from their personal connections but from all of the interconnectedness within their families, communities, societies, and humanity as a whole. This is the process by which *personal* social values evolve to *impersonal* ethical values.

Ethical relationships are *communal*, *non-instrumental*, and *impersonal*. Actions that are purely ethical in nature are *not an instrument* or means of acquiring some further ends. The ethical act is its own reward; the benefits are immediate. Ethical relationships produce nothing of economic value to be exchanged or traded to anyone else; ethical relationships are clearly non-economic. Unlike social relationships, purely ethical relationships show no preference for specific individuals or persons – they are *not personally* discriminatory. Ethical relationships are *communal* in that what is ethically right or wrong in a relationship with one person is right or wrong in relationships other people, including all other people of both present and future generations.

The social and ethical values that sustain positive personal relationships within families, communities, and societies evolve into impersonal ethical commitments of responsibility, equity, and justice for those of future generations. Ethical values can also evolve out of personal relationships with nature. Thus ethical values evolve to guide relationships with non-persons – to earth, air, water, forests, lakes, streams, rocks, or other species. Stewardship of nature is an ethic that has evolved out of past human relationships with nature. Social values of trust, kindness, and courage also evolve into commitments to treat nature in ways that are honest, fair, responsible, respectful, and compassionate toward those of future generations. Concerns for the whole of society and the future of humanity are neither economic nor purely social in nature; they are fundamentally ethical concerns.

There may well be economic value associated with doing things for the common good of society or for humanity. It's easier and often less costly to do business with people we know and trust. In economic jargon, the “social capital” embodied in trust reduces economic “transactions

costs.” Businesses can also “do well” financially by “doing good.” Some people will pay premium prices for ethically or socially-responsibly produced products, as in the cases of organics and Fair Trade. However, as philosophers and ordinary people throughout human history have known, the economic value of social and ethical relationships are almost insignificant in comparison to the social and ethical values that give quality, purpose, and meaning to human life.

If all investment decisions are preconditioned on receiving something of economic value in return, the investments necessary to protect, renew, and regenerate the natural and human resources essential for economic sustainability will not be made. More efficient markets would more accurately value scarce economic resources but will not ensure economic sustainability. Internalizing externalities would ensure that all economic values are reflected in market prices but cannot ensure the social or ethical investments necessary for sustainability. The ecological health and productivity of nature and society can be sustained only by people expressing their social and ethical values through their individual and collective choices and actions. This is economic reality; the economics of authentic organics, meaning sustainable organics.

Marketing experts may respond to this reality by pointing out that many organic consumers don't rank environmental and social concerns high on their list of reasons for buying organic, suggesting consumers are not really all that concerned about sustainability. I worked for a large corporation in merchandizing and advertising for a few years and taught agricultural marketing for several years at a major university. So, I understand where the skepticism regarding whether consumers are concerned about anything other than their own, individual well-being. We have created a culture in America that considers any motive other than individual, self-interest to be illogical or irrational. Rational behavior is defined as seeking self-interests.

If we are asked to explain why we are willing to pay higher prices for organics, the logical and rational responses are that we think things organic are safer to eat or be around, are more nutritious or healthful, or will actually save us money on health care or allow us to be more economically productive. It is quite logical and rational to be concerned about our individual health and economic well-being. Such answers will not evoke any embarrassing or time consuming follow-up questions for the interviewer. American consumers are often in a hurry and are not generally willing to share their personal thought or feelings with strangers, meaning with interviewers. So, they quite logically would give answers that seem logical and rational.

However, most of us actually do not make purely rational or logical economic decisions, at least not always. We care what our friends, family members, and neighbors think about us, including what we buy at the supermarket, how we garden, and how we care for our lawns. We consider the purely social/personal value of our purchase decisions, as well as the economic value. We also care what we think about ourselves; whether our economic decisions are consistent with our basic moral and ethical values. We don't want to feel guilty or ashamed about how the things we buy affect people that we don't know personally, including those of future generations. Many of us also consider the other living and non-living things of earth in our decisions, because we know we are a part of the nature and our well-being is inseparable from the well-being of the earth. In other words, we are social and ethical beings, as well as economic beings. Most of us just don't feel like discussing such things with an interviewer we meet in the

supermarket or on a phone call. So, I am a bit skeptical of market surveys regarding the real motives of people who pay premium prices for things organic.

Marketing experts also tend to point out that most consumers in fact are *not* willing to pay premium prices for organic products or services. I agree that a majority of American consumers are still basically skeptical of the general concepts of organic and sustainable. Many simply do not believe anything is wrong with the industrial products we consumers or the industrial economy we have created. They point to the wide variety of products at affordable prices for most Americans as an obvious success story that shouldn't be questioned. Those who question whether our capitalist system is actually producing safe and healthful products or whether industrial pollution threatens public health today and the future of humanity are labeled as un-American. Those who suggest we ought to address growing environment and social problems collectively, through government, are labeled as socialist or communist.

I agree that a majority of Americans are not ready to switch from conventional industrial products and services to organic food products, home gardens, or lawn care services. However, I believe the potential market for organic/sustainable products and services is already far larger than is being served by today's businesses. The following quote from a statement of The Hartman Group, perhaps the most respected market research firm that focuses on sustainability, suggests the size of the potential market for things authentically organic: "In 2010, we found that, despite a struggling economy, three out of four U.S. consumers said they made purchase decisions based on sustainability concerns *at least occasionally*, but that only one out of four consumers said they regularly purchased sustainably."ⁱⁱⁱ

Market experts may look at the 25% who regularly purchase sustainable products as a small minority of the total market. However, 25% is huge in relation to the percentage of the current market that is supplied with organic/sustainable products and services. The Hartman Group report highlighted organic foods as an area in which actual food purchases most nearly mirrored consumers' willingness to pay premium prices for sustainable products. However, the nearly-\$30 billion in organic food purchases represents just a bit over 4% of the total food and beverage market. Even when natural foods, local foods, and other "non-industrial" foods are included, the total of non-industrial foods is probably less than 7% of the total food and beverage sales. This means the potential market for organic/sustainable foods is probably three to four times as great as is currently being served by organic/sustainable producers. I suspect the potential is just as great for those who sell products and provide services related to gardens and lawn care.

I tell those on small farms who are produce organic and sustainable foods for local customers to not worry about changing the minds of Walmart shoppers or competing for their dollars. There are already far more people who want to buy sustainable/organic foods than producers, processors, or marketers willing and able to make sustainable/organic foods accessible to them. The challenge is to convince farmers that organic/sustainable farming is a real opportunity, not a passing fad but the future of farming. Equally important, is the challenge of finding ways to link organic/sustainable farmers with organic/sustainable consumers through reasonably efficient local markets that make organic/sustainable foods affordable to consumers. Organic products and products don't have to be *convenient* and *cheap*, but they must be *accessible* and *affordable*.

Unfortunately, much of what passes as organic or sustainable today is actually “greenwashing.” Greenwashing is defined by Wikipedia as “a form of spin in which green PR or green marketing is deceptively used to promote the perception that an organization's aims and policies are environmentally friendly. Whether it is to increase profits or gain political support, greenwashing may be used to manipulate popular opinion to support otherwise questionable aims.” The authentic organic consumer is not easily deceived. Many have been deceived before by promises of authenticity that turned out to be inaccurate if not fraudulent. For example, the current popularity of “local foods” is a direct reflection of loss of confidence in “industrial organic” foods. Once deceived, the organic/sustainable customer does not soon forget. Many are very tech-savvy and are not reluctant to share their experiences with like-minded “friends” near and far through the internet. Whereas, greenwashing may seem to make economic sense in the short run, the greenwashing business needs to have a quick exit strategy.

Greenwashing is quite common among large corporations. As I indicated previously, most people don't make purely economic decisions – but corporations do. Corporations with few investors, such as family corporations, are little different from partnerships or individual proprietorships. However, the large, publicly traded corporations that increasingly control the global economy are not real people, regardless of what the U.S. Supreme Court has ruled. Their investors are real people, with social and ethical values, but investors in these corporations have no means of expressing their social or ethical values in the decisions of the corporation.

The basic problem is that a corporation is obligated to serve the “common interests” of its investors. These investors often are scattered all around the world, have different nationalities, ethnicities, cultures, and religions and thus countless different social and ethical values. Many individuals invest through pension funds and mutual funds and don't even know how much of what companies they own at any given time. High-speed electronic trading has made a mockery of social responsibility, as many large corporate investors may own shares in a given company for only a fraction of a second. The only common value of corporate investors is a purely economic value: The desire to increase the economic value of their investment. This is the reason publicly-traded corporations participate in greenwashing. This is also the reason corporations are willing to invest in organics and sustainability only if such investments promise a competitive economic return on their investment. While such investments are necessary, they are not sufficient to ensure economic sustainability.

Some advocates of authentic organics believe that if organic consumers are willing to pay the full economic, social, and ecological costs of organic production, that organic producers or service providers will be able to maximize profits while supporting social and ecological sustainability. They can simply rely on the “economically irrational” decisions of consumers to ensure social and ecological integrity. Admittedly, “consumer irrationality,” meaning social and ethical decisions, is a step in the right direction, but still will not ensure sustainable organics. The profit maximizing corporation will always have an incentive to squeeze more profits out of the system by depressing prices to their organic suppliers or raising prices to their organic customers. It is cheaper economically to extract and exploit than to renew and regenerate. Sooner or later, competitive pressures will force the profit maximizing corporation to betray the public trust in ways that deplete and degrade the natural and human resources upon which its

sustainability ultimately depends. Sustainable business organizations must share in the social and ethical investments with their suppliers and customers to ensure sustainable organics.

Some may question whether it is idealistic or naïve to expect sustainable/organic businesses and their customers to make social and ethical investments in the future of humanity, whether it squares with economic reality. A few quotes from arguably the most widely respected economist of the 20th century, John Maynard Keynes, provide some valuable insights into such questions. Back in the early 1920s, Keynes wrote, “the *economic problem* may be solved, or at least within sight of solution, within a hundred years. This means that the economic problem is not... *the permanent problem of the human race*.”^{iv} Man's permanent problem will be “how to use his freedom from pressing economic cares ... to live wisely and agreeably and well.”

As it turned out, Keynes was right. The “economic problem” has already been solved for the vast majority of Americans, as well as most of those in the rest of the so-called *developed* world. In fact, most Americans probably had as much material wealth as we actually needed as far back as the 1950s. A 2004 review of more than 150 scholarly studies indicate that as developing national economies grow, beyond some very modest level of material well-being – around \$10,000 to \$15,000 per capita – there is little if any correlation between increasing wealth and the overall happiness or well-being of people in a nation.^v A 2003 British cabinet office report confirmed that “Despite huge increases in affluence compared with 1950, people throughout the developed world reported no greater feelings of happiness.”^{vi}

The research is simply confirming our common sense. Once our basic material needs are met – food, clothing, shelter, health care, – we know that the quality of our life depends far more on the quality of our relationships – friends, family, community, society – than on the quantity of income or wealth. Our happiness also depends on our having a sense of purpose and meaning in life. Without purpose and meaning, there is no sense of rightness or goodness in what we do. Once our basic economic needs are met, the pursuit of happiness, well-being, or quality of life is about developing the social and ethical dimensions of life, rather than striving for more income or wealth. For the vast majority of Americans, our economic problem has been solved.

It's time to look beyond organics or sustainability as limits or constraints to our ability to pursue a desirable quality of life and focus instead on the unlimited opportunities for creating a new and better world of the future. It's time to seek balance and harmony among ethical, social, and economic values. It's time to awaken to a new economic reality: It is not a sacrifice to share with other people or to care for the earth. These things make our lives better. The social and ethical values of sharing and caring far outweigh any short run economic sacrifice. The real economics of organics is not about greater profits or wealth; it's about learning to live wisely, agreeably, and well.

End Notes

ⁱ *Organic Trade Association 2012 Press Release*, “Consumer-driven U.S. organic market surpasses \$31 billion in 2011,” http://www.organicnewsroom.com/2012/04/us_consumerdriven_organic_mark.html

ⁱⁱ Joe Satrin, “Fair Trade Products, Led By Ice Cream, See 75 Percent Sales Growth, Huffington Post,” 3/14/2012, http://www.huffingtonpost.com/2012/03/14/fair-trade_n_1339288.html .

ⁱⁱⁱ The Hartman Group, “Sustainability 2013,” <http://www.hartman-group.com/hartbeat/sustainability-2013>

^{iv} John Maynard Keynes, *Essays in Persuasion*, (Miami, FL: BN Publishing – no copyright date) pp. 366-368.

^v Diener and Seligman, “Beyond Money,” *Psychological Science in the Public Interest*, 5 (1), 2004, 1–31.

^{vi} Oliver James, “Children before cash; better childcare will do more for our wellbeing than greater affluence,” *The Guardian*, May 17, 2003. <http://www.guardian.co.uk/society/2003/may/17/children.healthandwellbeing> .