

Natural Products NZ Survey 2014

Analysis of Results and Key Findings

4th November 2014

Audit | Tax | Advisory

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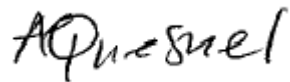
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1 Introduction from Natural Products (NZ) Incorporated

1.1 Natural Products Survey 2014

- Natural Products Survey 2014 is the most comprehensive industry survey to have been undertaken since 2008. The natural products sector has experienced considerable growth since then and the survey has been invaluable for quantifying its contribution to New Zealand's economy. It has also provided significant insights into the industry's current and emerging capabilities, and its challenges and opportunities for growth.



Alison Quesnel

Executive Director

Natural Products (NZ) Incorporated

2 Approach and Methodology

2.1 Our Approach

- Crowe Horwath was engaged by NPNZ to survey members of NPNZ, collate the responses and prepare this report for distribution to the industry. An email was sent to all member organisations of NPNZ with a link to the online survey. Questions were developed by NPNZ in conjunction with New Zealand Trade and Enterprise and the Ministry of Business Innovation and Employment.

2.2 The Methodology

- 186 members of the Natural Products Association were asked to complete the survey
- 88 responses were received. These are broken down as follows:
- Large firms: 50 employees and above: 14
- Medium firms: 10 to 49 employees: 24
- Small firms: 0 to 9 employees: 42
- Not indicated: 8
- For the charts on turnover, employment and wages/salaries, estimates were made for the non-respondents using a variety of sources and added to totals. Values for these indicators should be treated as an indication only.
- Charts have been annotated with the words “Treat as indicative only” or similar in all cases where the sample is small (high number of no-responses) or the respondents were asked to tick a range (e.g. 5 to 9 employees) rather than give an exact figure.
- MBIE has also supplied additional information that relates to their findings on Innovative Foods and Opportunities in Asia.

3 Key Findings

3.1 What keeps the industry awake at night

- A significant concern for firms of all sizes within the industry is related to customer issues.
- International government regulations are seen as a major barrier to growth for firms of all sizes.
- Availability of capital is the number one barrier to growth for small firms.

3.2 Sourcing materials for New Zealand production

- The majority of respondents use less than 50% New Zealand ingredients. Some of this is a result of these ingredients only being produced or manufactured overseas.
- Where there is a choice of New Zealand or overseas supply, consistent supply and quality are crucial to ensuring that the industry 'sources locally'.

3.3 How the industry innovates

- Cost, skills and time are problems for developing or introducing a new indigenous New Zealand product. Accessing overseas licensed innovations appears to be viewed as a realistic alternative.
- Large and medium firms undertake strategic planning and are focused on operating excellence. Smaller firms are focussed on getting their products out to customers and making sales.

3.4 How the industry markets itself to the world

- New Zealand is perceived as 'clean and green' but firms market their products around reliability and integrity.
- 'Clean and green' features low in how firms present their products to the world.
- Small firms might market on 'clean and green' until they develop brand awareness and the focus becomes reliability and integrity.
- There is perceived value in products making a substantiated health claim. However, although not a fact from the research findings, firms may be unlikely to do this due to the cost and competitiveness.

3.5 Confidence and Prospects

- 2014 has been more difficult than the previous three years.
- The industry is optimistic about the next three years. Firms expect to make more sales mainly from New Zealand, Australia and the Asian region and employ more staff.
- Smaller firms are looking more to traditional markets in the US, UK and Europe, while larger firms are more focussed on Australasia and Asia.

4 Survey Results

4.1 Part 1: Business Operations

4.1.1 Turnover

Turnover of the industry is estimated at circa \$1.4 billion:

Category	Estimate
Respondents	\$805m
Non-respondents	\$576m
Total estimated turnover	\$1.4b

Note:

- These numbers are estimates only.
- Sample of respondents is 77 out of 88 i.e. 11 no responses.
- Turnover estimated at the mid-point of the bracket.
- A number of firms were given more precise turnover figures using Kompass estimates.
- Non-respondents' turnover estimated using membership data.

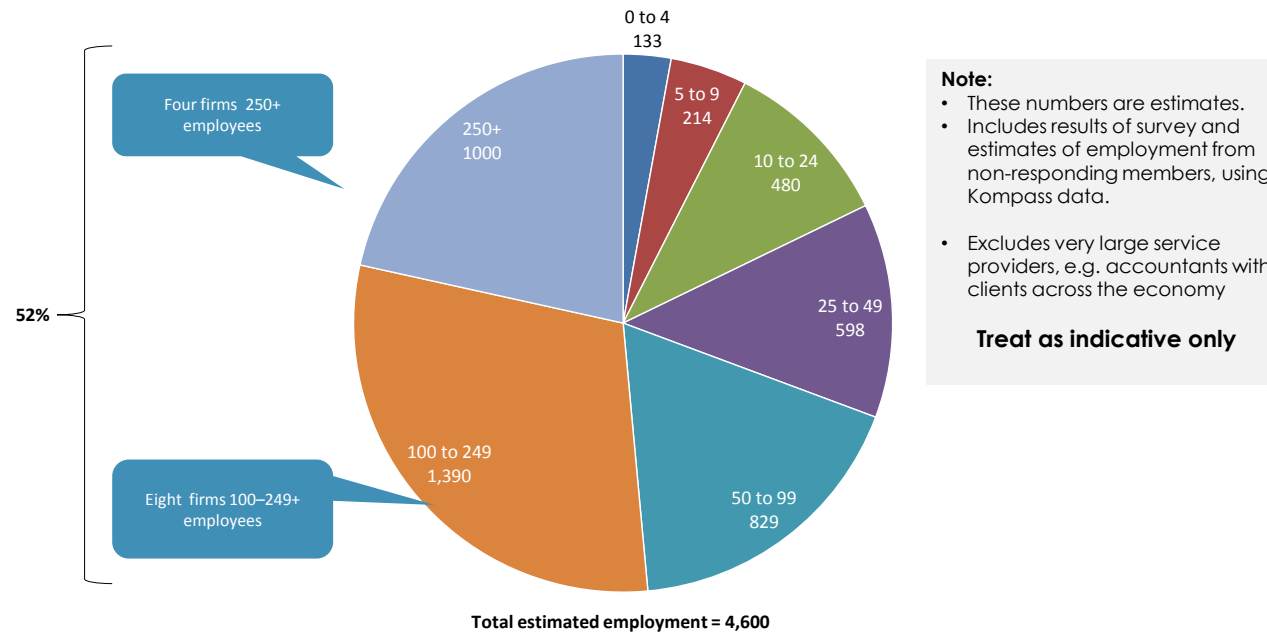
Treat as indicative only

4.1.2 Employment

The industry is estimated to employ 4,600 people; large firms (100 or more employees) account for 52% of employment:

Number of employees by firm size

Employees



4.1.3 Employment growth

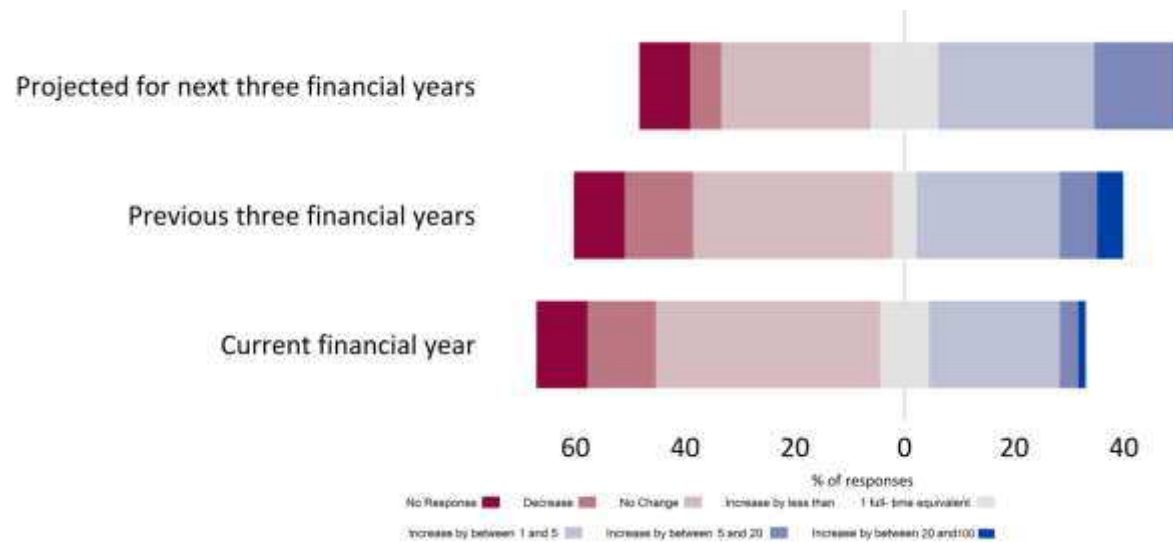
Respondents are expecting stronger employment growth in the next three years than has occurred in the last three years:

Employment growth

Respondents are expecting stronger employment growth in the next three years than has occurred in the last three years

Historical employment growth and future expectations

% of responses

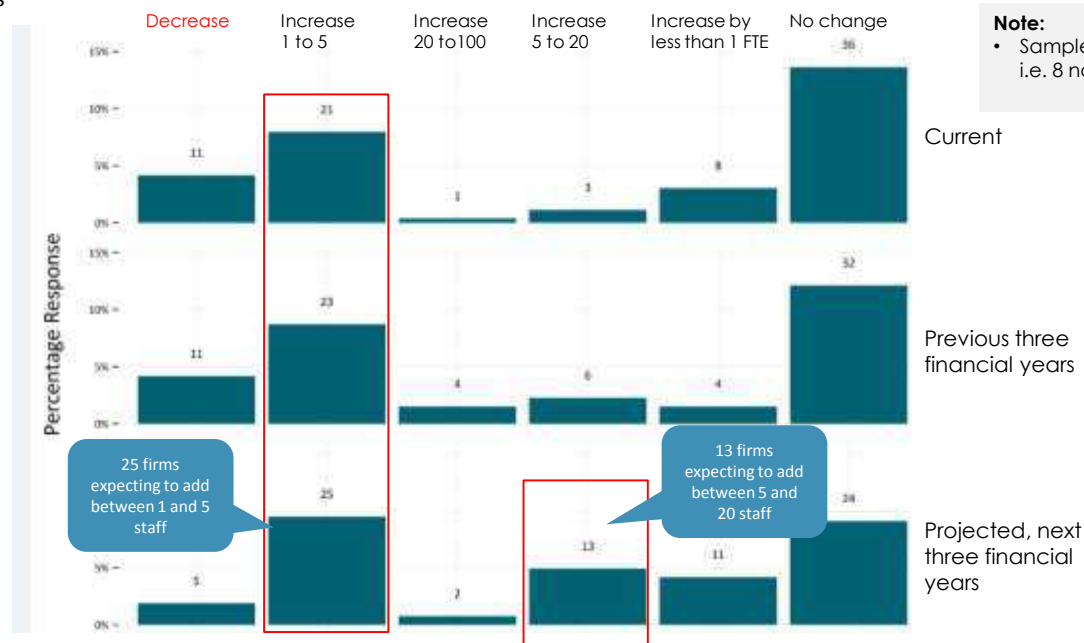


4.1.4 Employment growth

The majority of respondents are expecting to add jobs over the next three years; those growing employment are typically adding between one and five workers:

Historical employment growth and future expectations

% of responses

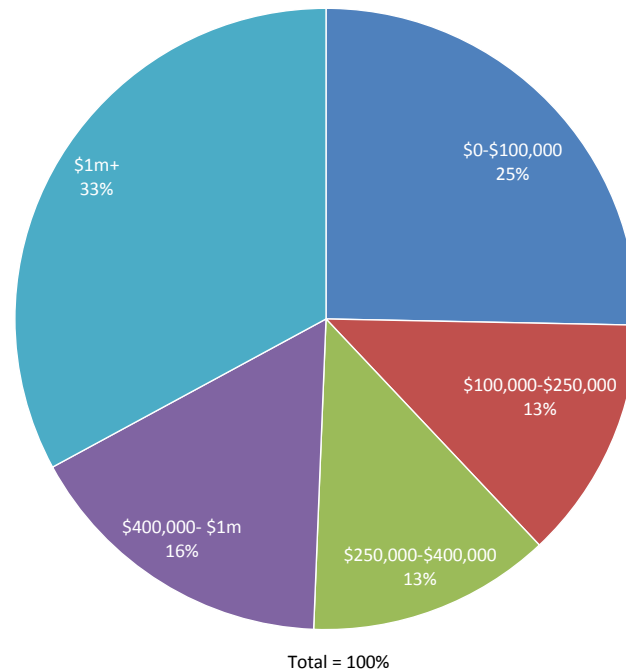


4.1.5 Salaries/wages

Thirty-three per cent of respondents pay more than \$1 million in salaries:

Expenditure on salaries/wages in last financial year

% respondents; 2014



Note:

- Sample is 80 out of 88 i.e. 8 'no responses'.
- Excludes members who did not complete the survey.

4.1.6 Estimated value of salaries and wages paid, last financial year

The industry is estimated to have paid in the region of \$258 million in salaries and wages in the last financial year:

Category	Estimate
Survey respondents	\$168m
Non-respondents	\$90m
Total estimated salaries/wages	\$258m

Note:

- The sector includes firms involved in a wide range of activities, from service providers such as accountants and lawyers who are highly paid, to shop assistants who will be on or above the minimum wage.
- This estimate is calculated by multiplying the estimated number of people employed (4,600) by the average wage for a full time employee in New Zealand (\$56,000).

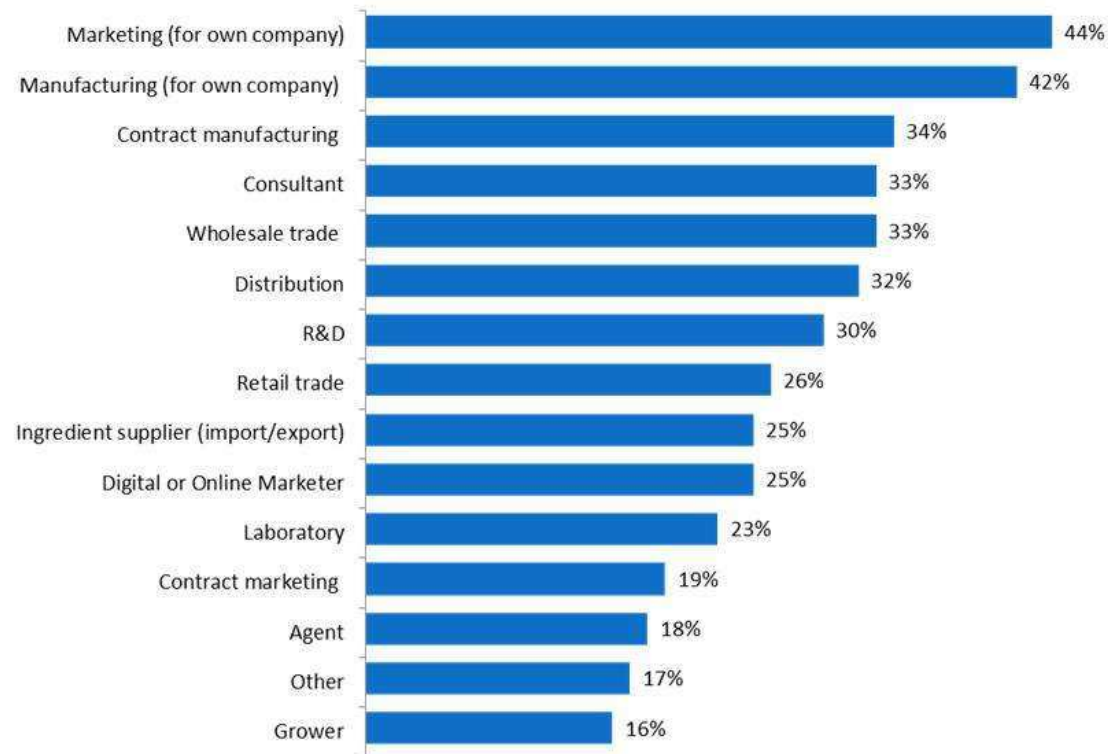
Treat as indicative only

4.1.7 Business activities

Respondents are involved in a wide range of activities:

Business activities

% of respondents involved in activity



Note:

- Respondents were asked to tick all that apply to their business. Many involved in multiple activities.

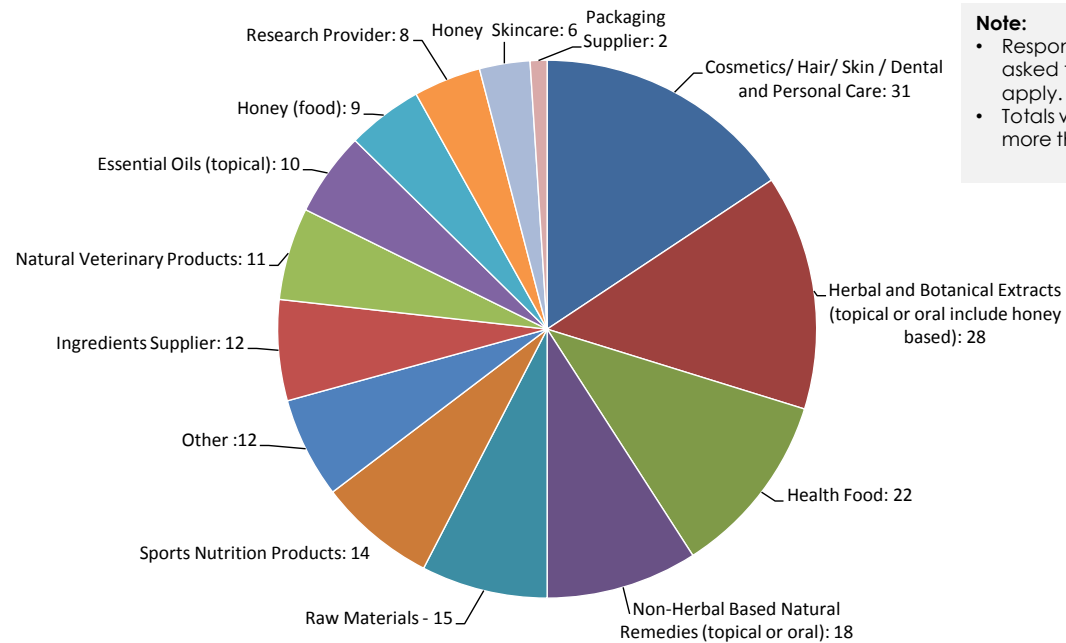
Treat as indicative only

4.1.8 Products and services

Respondents provide a wide range of products and services; with health foods, personal care and health and botanical extracts bring more prevalent:

Respondents providing a product or service

Number respondents



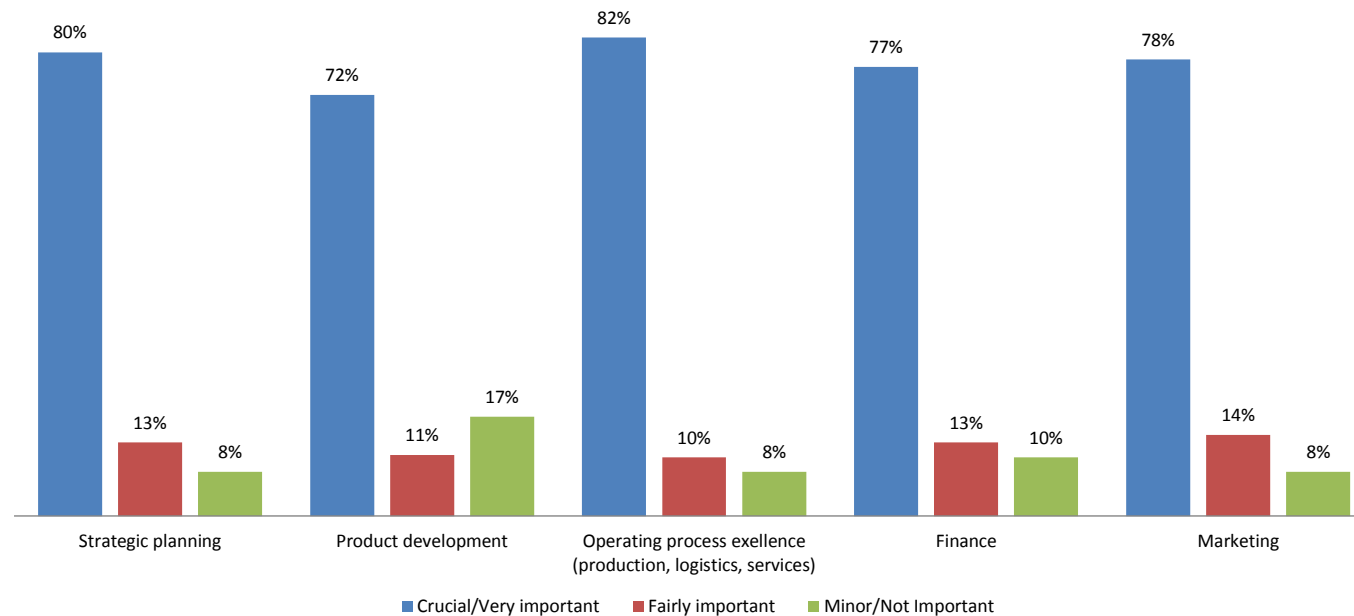
Note:

- Respondents were asked to tick all that apply.
- Totals will add up to more than 88.

4.1.9 Importance of business functions or practice to the company's operations & future plans

Strategic planning, product development, operating process excellence, and finance and marketing all scored as being highly important to operations and plans of respondents:

Percentage of respondents reporting the following factors as important to their operations and future plans
% respondents

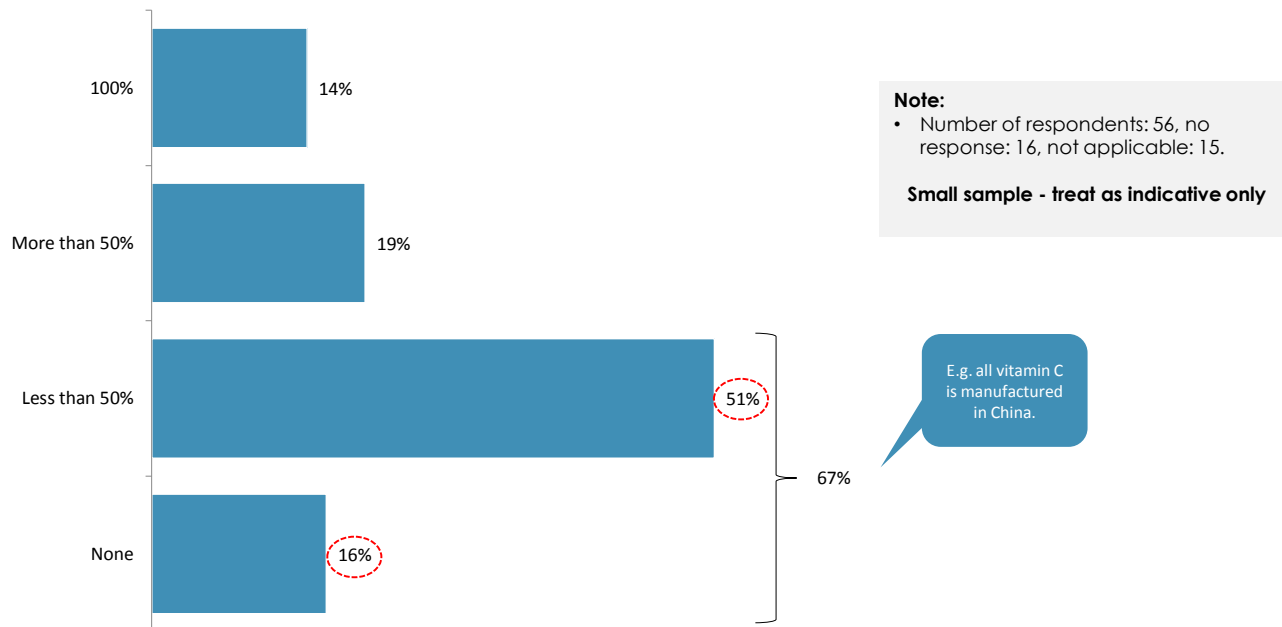


4.1.10 Use of New Zealand sourced ingredients or materials

51% of respondents use less than 50% New Zealand ingredients; 16% use none:

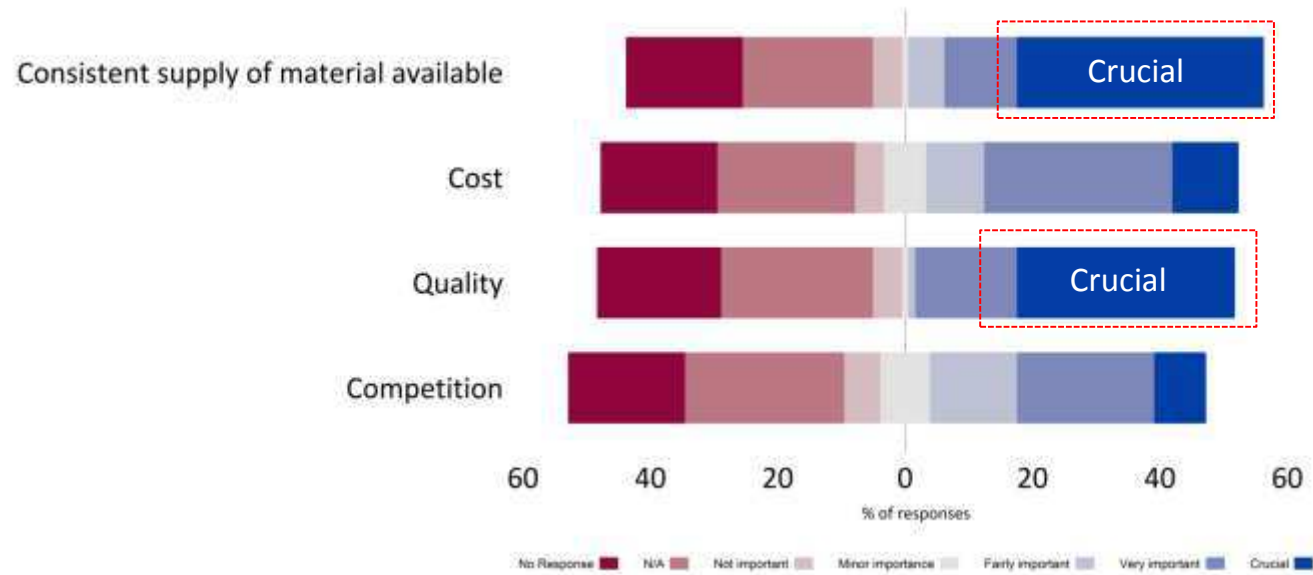
New Zealand sourced materials used in production

% respondents



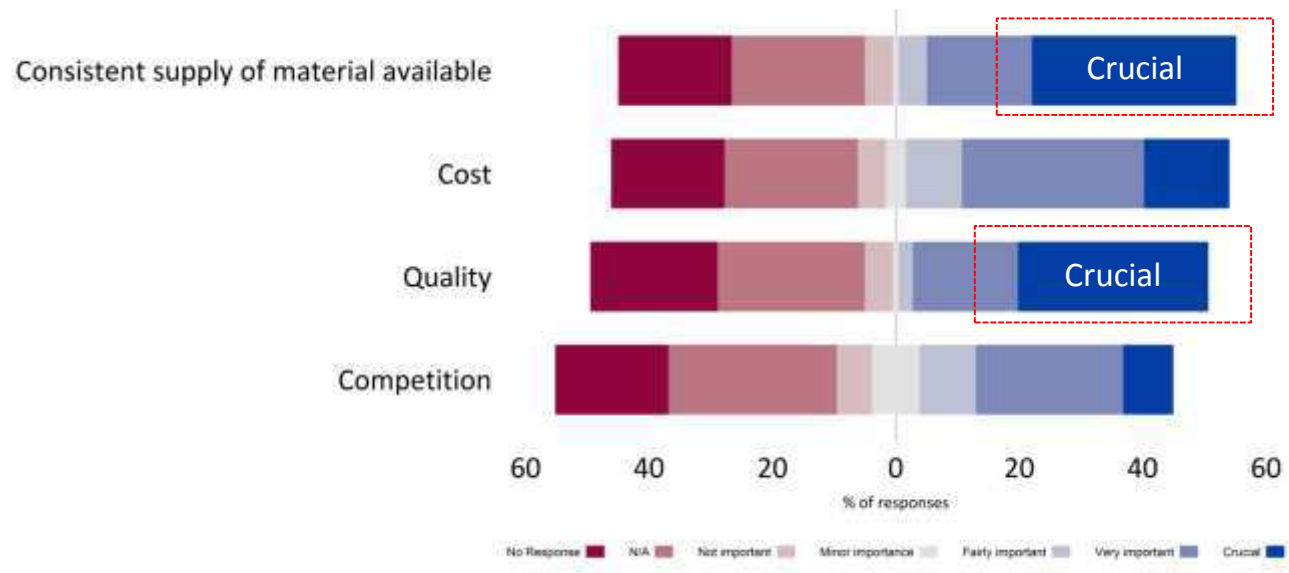
4.1.11 Importance of factors in choosing New Zealand ingredients

Consistent supply and quality are seen as crucial in choosing New Zealand ingredients:



4.1.12 Importance of factors in choosing new imported ingredients

Similar to the choice to use New Zealand ingredients, supply and quality are also crucial in choosing imported ingredients:



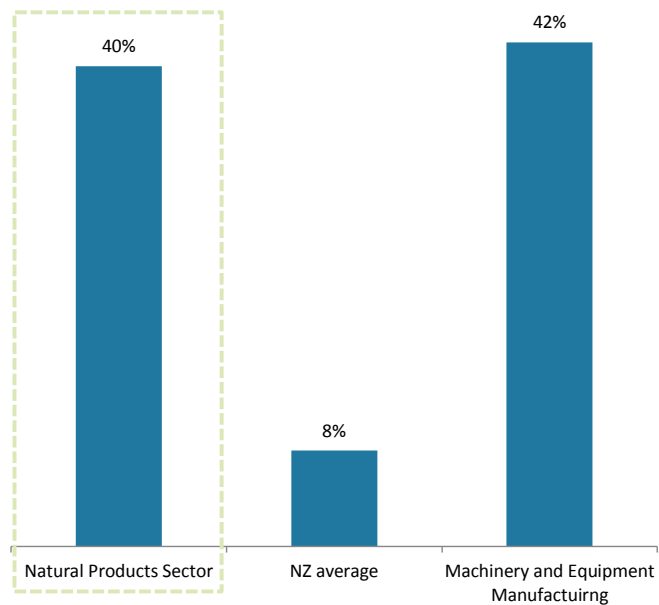
4.2 Part 2: R&D and Innovation

4.2.1 R&D rate

The natural products sector has one of the highest rates of R&D in the economy, second only to machinery and equipment manufacturing (mainly high-tech manufacturing):

Investment in R&D

% of respondents, 2014; (comparators), 2013



Note:

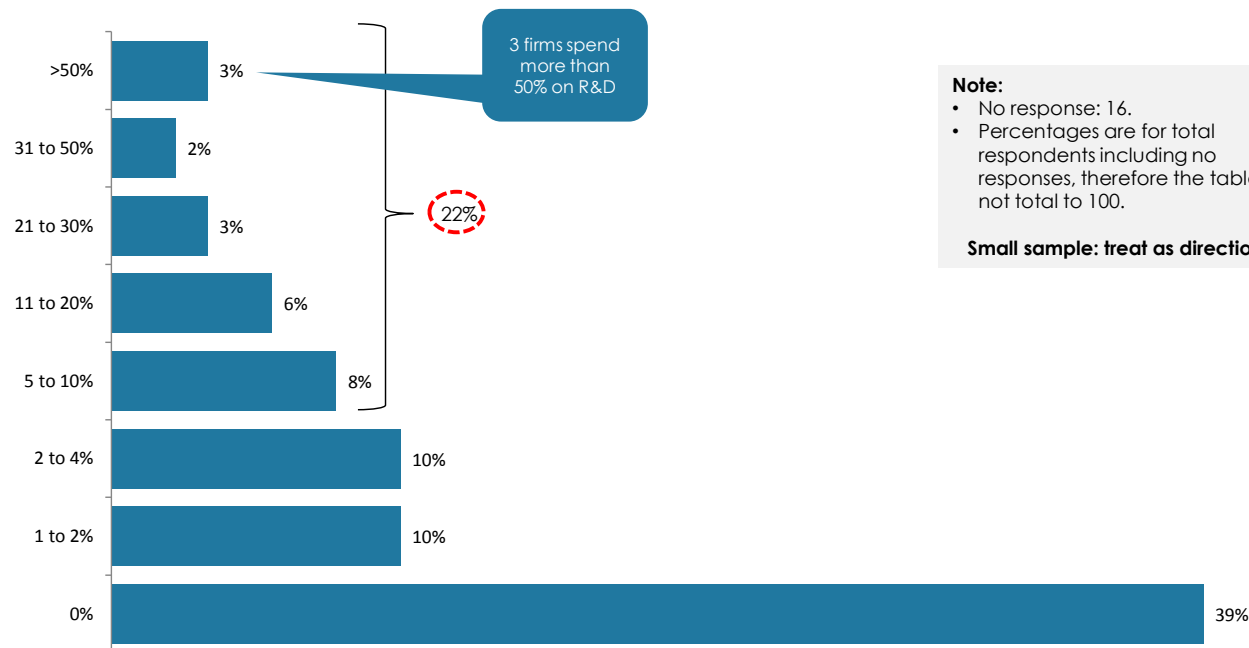
- The R&D rate is the percentage of firms in a sector that have undertaken R&D activity in the last two years.
- R&D covers any activity characterised by originality. It should have investigation as its primary objective, and has an outcome of gaining new knowledge and/or new or improved materials, products, services or processes. Buying technical knowledge or information from abroad is included.

Small sample: treat as directional

4.2.2 Percentage of turnover spent on R&D

22% of firms spend 5% or more of turnover on R&D:

R&D spend
% turnover



Note:

- No response: 16.
- Percentages are for total respondents including no responses, therefore the table will not total to 100.

Small sample: treat as directional

4.2.3 Factors limiting ability to conduct R&D

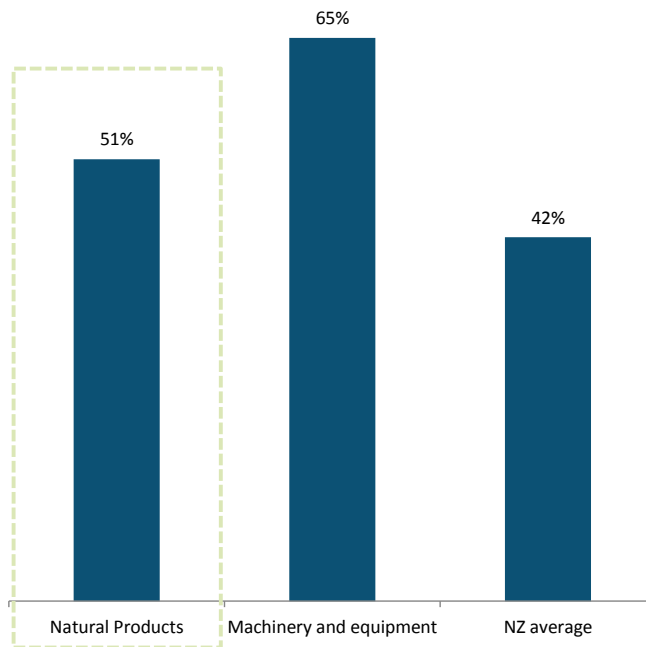
Cost or lack of capital are key barriers for small and medium firms; however, access to technical expertise or research facilities is common across all firms:

Top three barriers	
Large firms	
1	Regulatory issues
2	Lack of technical expertise
3	Lack of research facilities
Medium firms	
1	Cost/Lack of capital
2	Lack of time
3	Lack of technical expertise/Lack of research facilities
Small firms	
1	Cost/Lack of capital/Lack of time
2	Regulatory issues
3	Lack of technical expertise/Lack of research facilities

4.2.4 Innovation: Introduction of new goods and services

The rate of introduction of new goods and services by respondents is above the New Zealand average:

New goods or services introduced in last year
 % of respondents, 2014; (comparators), 2013

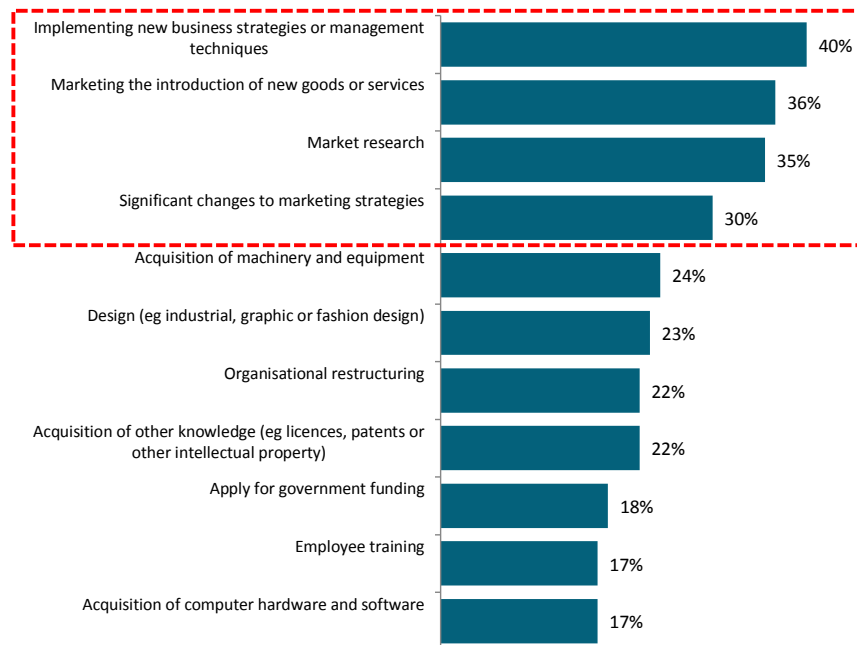


Note:

- Natural products percentage is a percentage of total number of respondents, i.e. 88

4.2.5 Activities to support innovation

Business strategy and marketing stand out as activities most often undertaken to support innovation:



4.2.6 Factors limiting ability to conduct innovation

For small and medium firms, the cost to develop is a barrier to innovation; however, Government regulations and lack of appropriate personnel are innovation barriers for large firms:

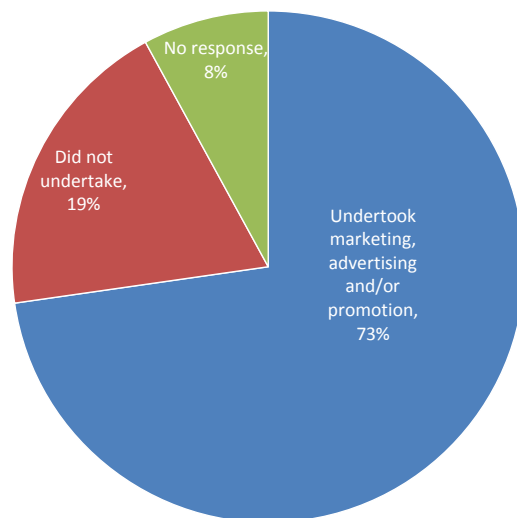
Top three barriers	
Large firms	
1	Government regulations
2	Lack of appropriate personnel
3	Lack of information and marketing experience
Medium firms	
1	Cost to develop or introduce
2	Lack of management resources
3	Lack of appropriate personnel
Small firms	
1	Cost to develop or introduce
2	Lack of management resources
3	Lack of cooperation with other businesses and Government regulations

4.3 Part 3: Marketing. Growth and Overseas Income

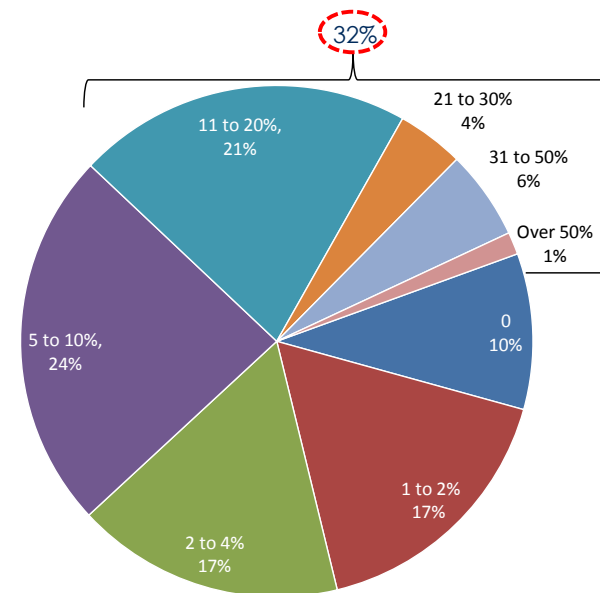
4.3.1 Expenditure on marketing, advertising and promotion

32% of respondents spend 11% of turnover or more on marketing, advertising and/or promotion:

Respondents that undertook marketing
% respondents



Percentage of annual turnover spent on marketing
% respondents



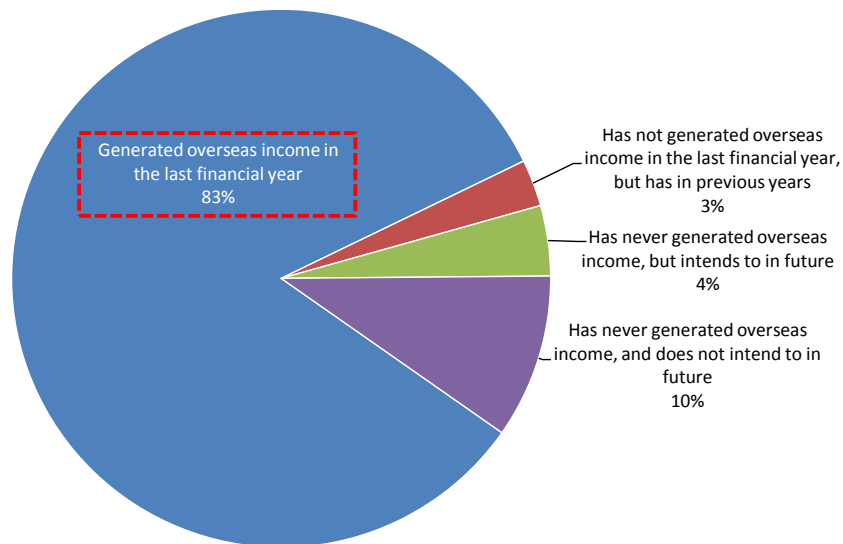
Note:

- Sample is 71 respondents.
- Chart does not include 17 no responses.

4.3.2 Overseas Income

The natural products industry appears to be highly export-sensitive; with 85% of respondents reporting total export earnings to be \$285 million:

Description of respondents business in terms of overseas income
 % respondents



Note:

- Sample is 71 respondents.
- Chart does not include 17 no responses.

Estimated turnover of respondents:

- \$805 million

Total export earnings indicated from respondents:

- \$285 million

Exports as a percentage of turnover:

- 35%

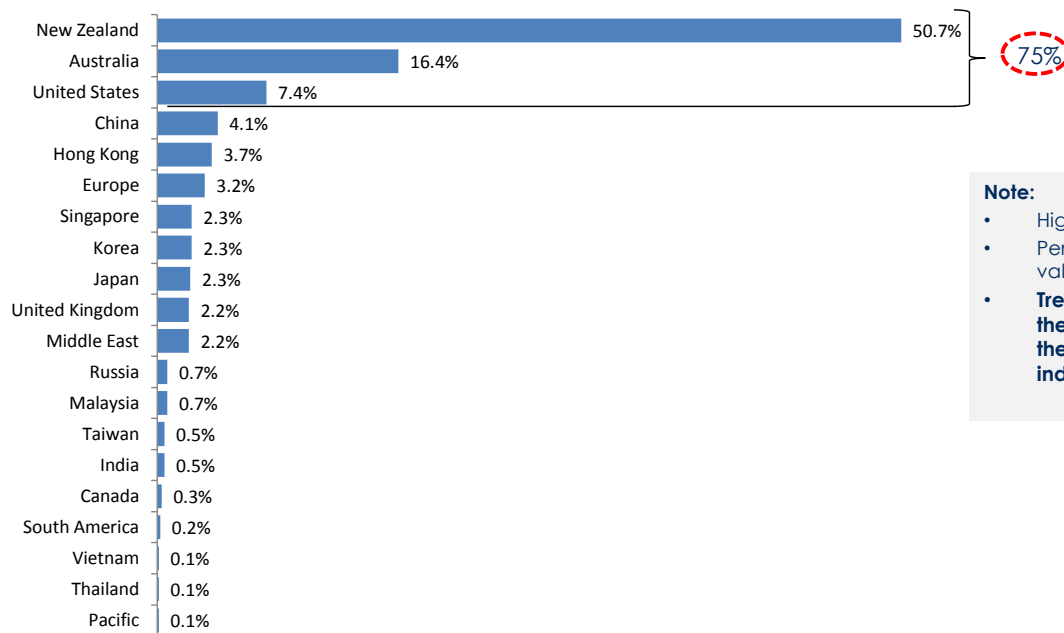
Contains significant estimates: treat as indicative

4.3.3 Relative importance of selected markets to respondents

New Zealand is 50% of the market followed by Australia and the United States; Asian markets are small individually but important in aggregate:

Relative importance of selected markets to respondents

% markets



Note:

- High number of no responses
- Percentages do not indicate value
- **Treat as indicative only of the relative importance of these markets to the industry**

4.3.4 Growth outlook : Level of confidence regarding growth in key markets

New Zealand, Australia, China and Hong Kong are key markets for all firms; however smaller firms are still expecting growth in more traditional markets, such as US, UK and Europe:

Confident regarding growth in the following markets					
Large firms		Medium firms		Small firms	
1	New Zealand	1	New Zealand	1	New Zealand
2	China	2	Australia	2	China
3	Australia	3	China	3	Australia
4	Singapore	4	Hong Kong	4	Hong Kong
5	Hong Kong	5	Singapore, Malaysia, Korea, Taiwan	5	US, UK, Europe, Taiwan, Middle East

4.3.5 Preparedness: Confident that firm will be prepared to enter key markets in the next five years

Firms believe they are prepared to enter Australasian and Asian markets (in particular China and Hong Kong) in the next five years:

Confident firm will be prepared to enter the following markets					
Large firms		Medium firms		Small firms	
1	New Zealand	1	New Zealand	1	New Zealand
2	Australia	2	Australia	2	China
3	China	3	Hong Kong	3	Singapore
4	Korea	4	China	4	Taiwan
5	Hong Kong	5	US, Europe	5	Australia

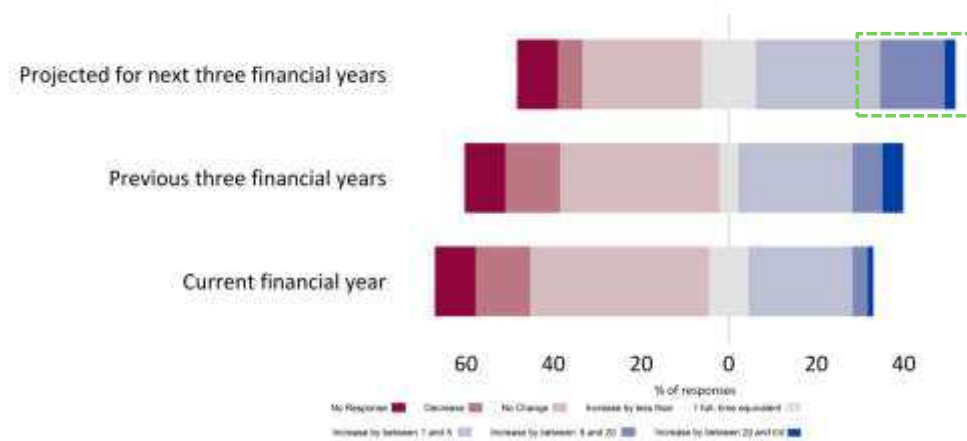
4.3.6 Revenue growth: Historical and projected

Respondents are positive about revenue growth in the next three years:

Revenue growth: historical and projected

Respondents are positive about revenue growth in the next three years

Revenue growth
% growth



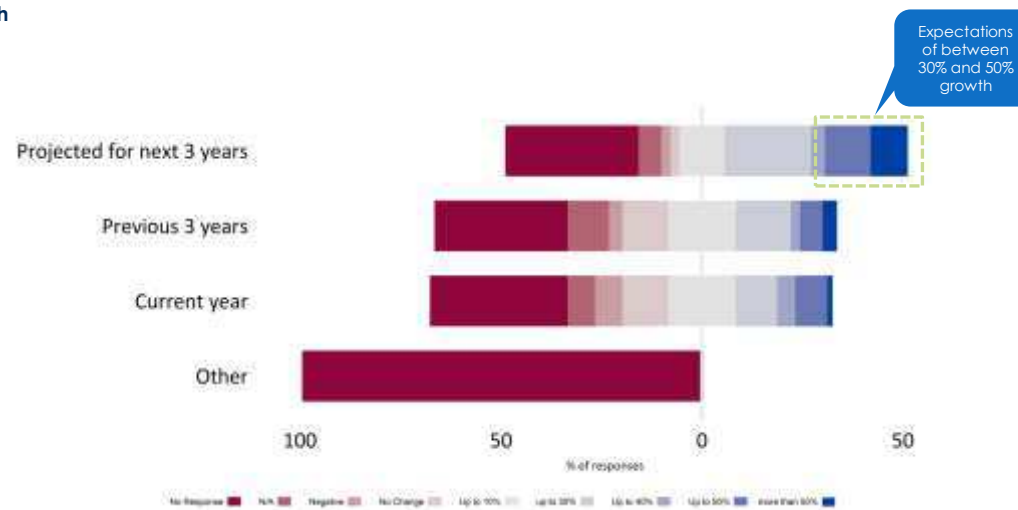
4.3.7 Export growth: Historical and projected

Respondents are projecting strong export growth in the next three years:

Export growth: historical and projected

Respondents are projecting strong export growth in the next three years

Export growth
% growth



4.3.8 Factors influencing success in key export markets

Respondents made the following comments:

Summary of comments	
<ul style="list-style-type: none"> • The New Zealand Story – for access to Asia <ul style="list-style-type: none"> – New Zealand grown and produced – High nutritional properties – Traceable – Quality (control) – ‘Made in New Zealand’ • China Free Trade Agreement • Government funding • Certification <ul style="list-style-type: none"> – Organic – TGA for Australia – Quality, process and/or natural certification • Economic stability of the market • Regulatory requirements <ul style="list-style-type: none"> – Understand requirements and able to meet these – Low regulation for importing 	<ul style="list-style-type: none"> • Strong networks and relationships with distributors and retailers • Innovation <ul style="list-style-type: none"> – R&D – new product formats – Unique niche product offering – Use of science innovation • Quality market intelligence • Individual firm strengths <ul style="list-style-type: none"> – Strong brand – First to market – Value for money products – Quality products – Online sales capacity – Product availability – Staff that speak Asian languages – Marketing experience – Regulatory expertise

4.3.9 Barriers to growth

International government regulations and access to raw materials are key barriers to growth for medium and large firms; availability of capital and operating costs are key barriers for small firms:

Identified barriers to growth					
Large firms		Medium firms		Small firms	
1	International government regulations	1	International government regulations	1	Availability of capital to fund growth
2	Increased competition	2	Increased competition	2	International government regulations
3	Access to New Zealand raw material	3	Access to imported raw material	3	Increased competition
4	Access to imported raw material	4	Access to New Zealand raw material	4	Cost of getting product to market
5	Local supply issues	5	Availability of capital to fund growth	5	Increased operating costs and New Zealand government issues

Increased competition is an issue across firm sizes

4.3.10 Regulatory and compliance issues in destination markets that hamper exporting

Respondents identified the following regulatory and compliance issues in destination markets as hampering exporting:

Summary of comments

- Increasing demands of compliance and regulators (and associated costs)
 - Malaysia – costs of DCA requirements
 - China – ‘blue hat’ regulatory requirements
 - Australia – Therapeutic Goods Authority
 - South East Asia – Halal certification
 - Korea – FDA
 - Developed countries – GMP (note that US moving to full GMP – impacts on need for firms to update their technical support, product stability studies)
 - RMP limitations for dairy, Europe dairy tariffs
- Lack of knowledge of regulatory requirements in target destination e.g. ingredients allowed, nutrition label claims, packaging – each market has different requirements, some firms feel this is getting harder
- Organic standards in US, China, Korea
- Bias in favour of the home country
- Lack of consistent entry rules in each city in China (linked to corrupt Government officials)

4.3.11 Regulatory and compliance issues in New Zealand that hamper exporting

Respondents identified the following New Zealand regulatory and compliance issues in destination markets as hampering exporting:

Summary of comments

- Lack of clear regulations
 - Mixed messages from regulators
 - Lack of progress with Natural Products legislation
 - Lack of credible New Zealand regulatory agency for natural and supplementary health products
 - Duplication of requirements from different regulatory agencies
 - Manuka honey guidelines and border testing, inconsistencies between New Zealand regulations and global trends
- Prohibition on making therapeutic claims for natural health products
- Compliance to GMP
- Lack of Government export certificates
- Ministry of Primary Industries
 - Lack of advice, support and understanding of market access requirements e.g. Chinese regulations
 - Dietary supplements containing animal and dairy ingredients are required to comply with MPI Overseas Market Access Requirements (OSAR) – feel does not always reflect importing custom requirements (burden on local exporters)
 - E Certification system
 - RMP changing audit requirements
 - Biosecurity interface
- Lack of organic trade agreements with US, China and Korea and cost of organic certification
- Lack of harmony with Australia, TGA regulatory research

4.3.12 Ideas for help in addressing regulatory issues and barriers that hamper exporting

Respondents suggested the following ideas for addressing regulatory and compliance issues that hamper exporting:

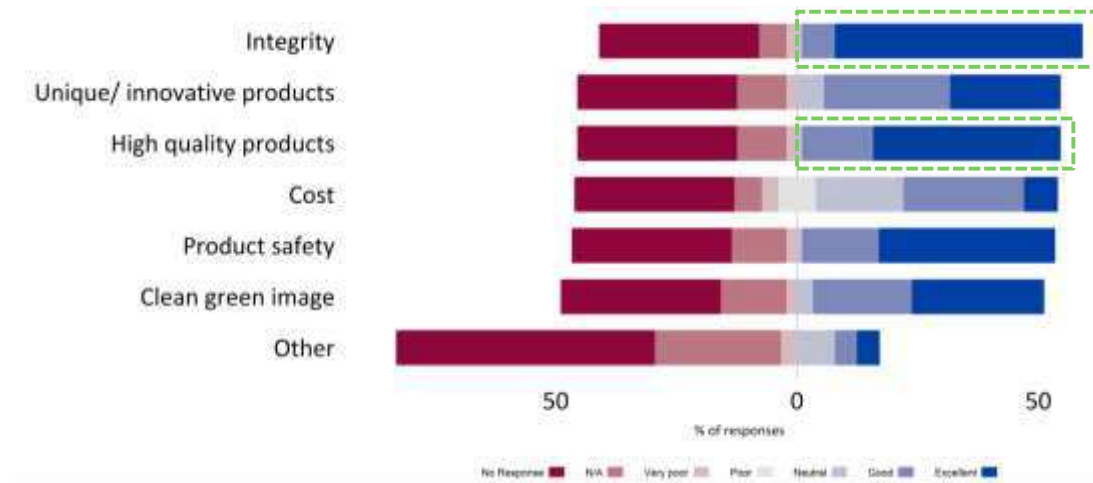
Summary of comments

- | | |
|---|--|
| <ul style="list-style-type: none"> • Investor capital • Assistance for small companies e.g. MPI small business specialist • Regulation: <ul style="list-style-type: none"> • New and stronger regulations • Low cost regulation scheme • Quality compliance • Align regulations with offshore Free Trade Agreements • Ensure input from traditional practitioners when deciding on permitted herbs listed in regulatory sites • Help from New Zealand representatives: <ul style="list-style-type: none"> • Specialist consultants • NZTE – navigating local markets • CECC • Productivity Commission • Industry Cooperation Assistance from government | <ul style="list-style-type: none"> • Regulatory authority/advisory service • Free Trade Agreements e.g. ASEAN countries • Consistent rules • Information <ul style="list-style-type: none"> • What is required for each market e.g. pesticide limits; infant formula brands' access to China • Portal linking exporters to overseas regulators • Directory of approved overseas regulatory consultants • Consistency and understanding of rules <ul style="list-style-type: none"> ○ Rules for entry into China for Manuka honey • Government assistance with: <ul style="list-style-type: none"> • Re getting products listed/registration in overseas markets e.g. South East Asia • Funding • Cost of compliance with legislation (some feel assistance from Callaghan is hard to secure) • Compiling safety dossiers • Clinical trials or stability test which may allow access to a particular market • Market regulatory advice |
|---|--|

4.3.13 Perception of company attributes by international customers

Respondents report that customers have strongly positive perceptions of them across all attributes, with integrity and high quality products scoring highly:

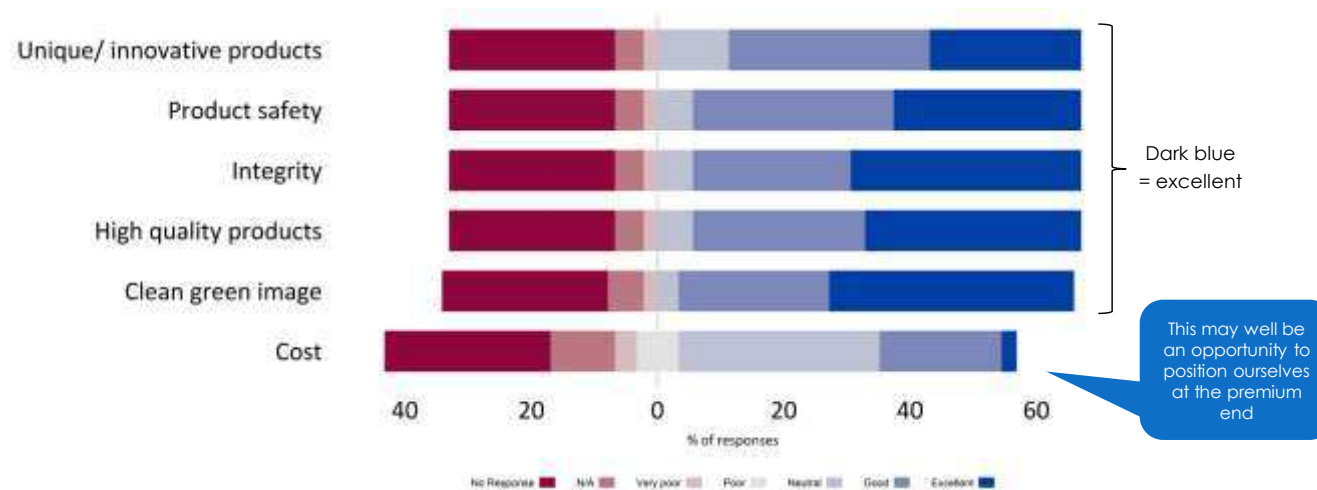
Degree of perception
% scale



4.3.14 Perception of New Zealand Natural product industry by international markets

Respondents report that the New Zealand industry has a positive image in international markets across all attributes, although cost scores somewhat less strongly:

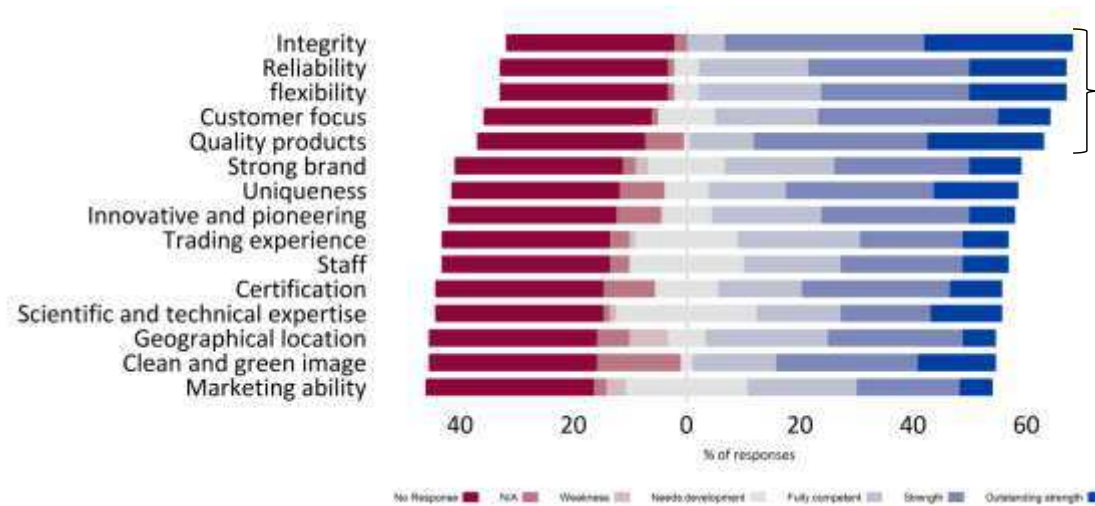
Degree of perception
% scale



4.3.15 Respondents' perception of the strengths and weaknesses of their firms

Respondents scored fairly evenly across attributes, although integrity, reliability, flexibility, customer focus and quality products scoring marginally higher:

Strengths and weaknesses
% perception

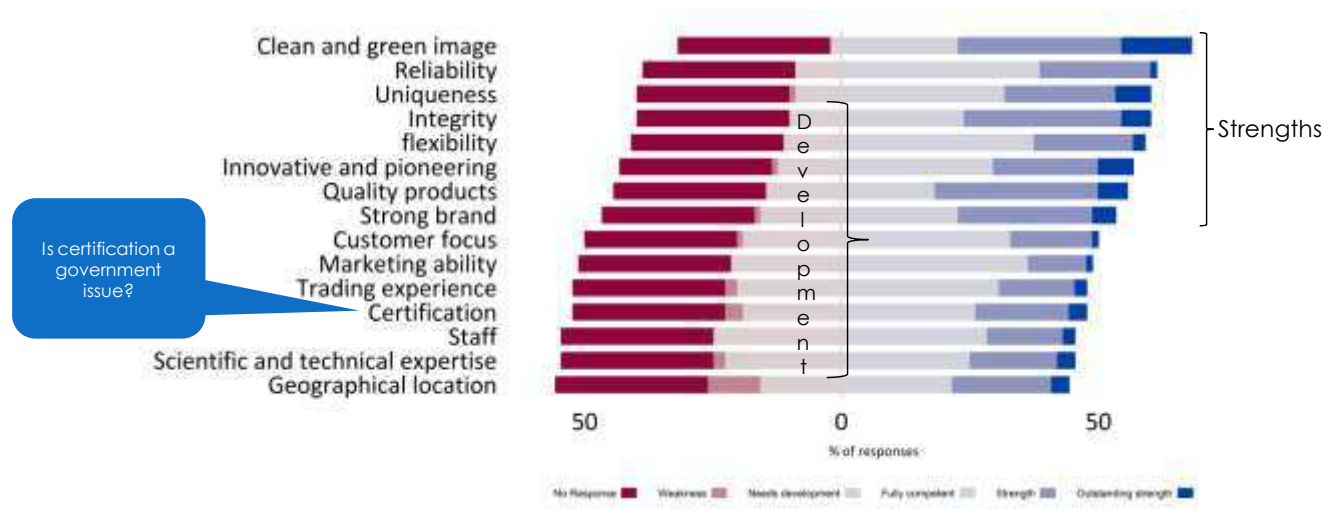


4.3.16 Strengths and weaknesses of the Natural Products Industry

The 'clean green' image, reliability, uniqueness and integrity are seen as key strengths; branding, marketing, experience and staff are seen as needing development:

Strengths and weaknesses

% perception



4.3.17 What are the significant issues that keep the firm's managers and owners awake at night?

Customers are a significant concern across all firms. Small and medium firms are concerned about economic and environmental factors; small firms are concerned about the cost of running a business:

Significant concern					
Large firms		Medium firms		Small firms	
1	Customers	1	Competitors	1	Money
2	Compliance	2	Customers	2	Cost management
3	Staff	3	Economic & environment	3	Compliance
		4	Operational issues	4	Customers
				5	Economic & environment

4.3.18 What are the issues that have minor significance to the firm's managers and owners, which don't keep them awake at night?

Tax is of minor significance to all firms; but compared to small firms, money is less of a concern for medium and large firms:

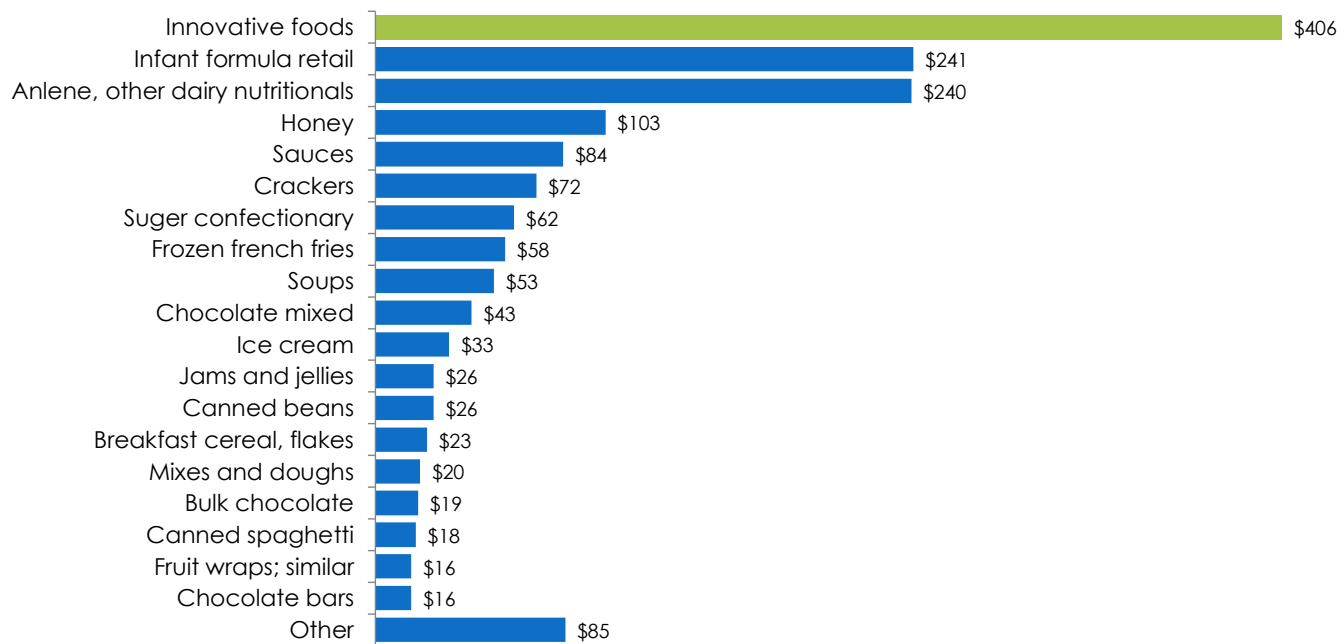
Issues of minor significance					
Large firms		Medium firms		Small firms	
1	Tax	1	Tax	1	Tax
2	Competitors	2	Compliance		
3	Operational issues	3	Money		
4	Money				

4.3.19 'Innovative Foods' (aka HS210690: Other Food preparations, N.E.S)

Innovative foods is the largest processed foods export category and has shown strong growth:

Export value of top 20 processed foods products (HS6 level)

\$USm, 2012



4.3.20 'Innovative Foods'

Many products exported under HS210690 can be classified as part of the natural products industry:

Definition	
The trade code HS210690: other food preparations, n.e.s. is a catch-all "category of categories" for products that did not exist when the trade codes were developed. Past research clearly shows this category is almost exclusively a wide range of new, innovative food products ranging from self-saucing puddings to Nutraceuticals.	
Example products exported under HS210690	
Yoghurt base	Colostrum (powder, tablets)
Flavourings	Dietary supplements
Freeze dried meals	Food supplements
Natural health preparations	Enzogenol (a nutraceutical)
Powdered deserts	Fruit bars
Health supplements	

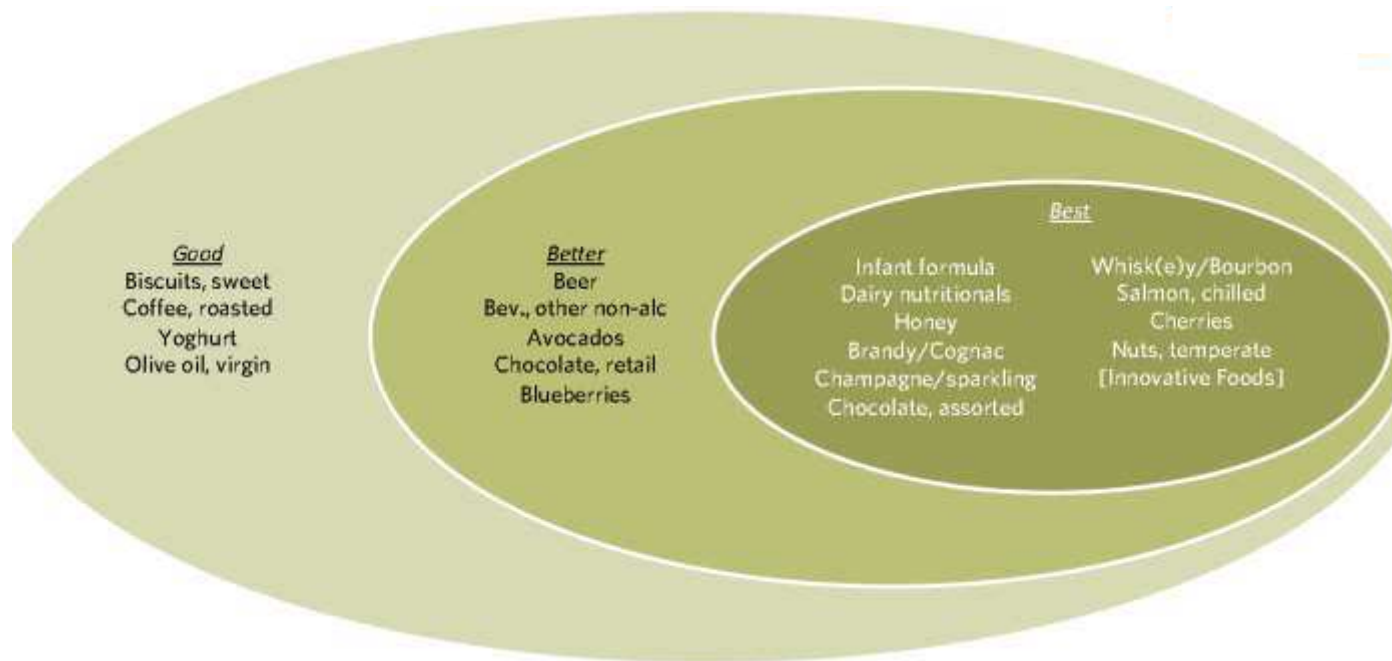
4.3.21 Opportunities in Asia: 'Innovative Foods'

Work commissioned by MBIE as part of the Food and Beverage Information Project shows that New Zealand is a strong #3 in the East and South East Asian market:

EXPORTS to E/SE ASIA BY PEER GROUP						
Country	Peer export share	Export value; FOB sender			\$/kg	
		US\$m; 12	5y CAGR	5y ABS	US\$; 12	5y CAGR
USA	46%	\$1,261	9%	\$448	\$8.74	4%
Netherlands	16%	\$431	15%	\$220	\$11.35	15%
New Zealand	7%	\$185	8%	\$57	\$4.84	10%
Germany	6%	\$160	19%	\$93	\$8.13	9%
Australia	4%	\$108	7%	\$32	\$3.75	9%
France	3%	\$79	4%	\$13	\$7.36	4%
Canada	3%	\$76	12%	\$32	\$6.35	17%
Switzerland	2%	\$65	10%	\$24	\$13.23	0%
Belgium	2%	\$61	-6%	-\$20	\$5.06	2%
Other	11%	\$52	13%	\$131	\$5.87	-8%
TOTAL from peers	100%	\$2,712	10%	\$1,031	\$7.59	6%
Inter-regional/other		\$2,556				
TOTAL		\$5,268				

4.3.22 Opportunities in Asia

...and identifies 'innovative foods' as one of 11 'best' opportunities for New Zealand in East and South East Asian markets:



5 Summary and Conclusions

- Despite relative difficult trading in 2014 compared to the previous three years, the industry is reasonably confident about prospects for growth for the immediate future. The survey indicated a change of focus and emphasis, dependent on the size of the business, which would not necessarily be industry specific. Small and medium sized firms are experiencing typical growth issues associated with lack of capital and cost management, that can be addressed via the strategic planning process.
- Interestingly, new entrants to the export market tend to trade on the New Zealand 'clean and green' image which gives us a competitive advantage at entry level. However, once the brands are established, then integrity, high quality and product safety are the attributes that international customers most value.
- The investment in research and development ('R&D') in the industry is second only to machinery and equipment manufacturing (mostly high-tech manufacturing) with 3% of respondents spending over 50% on R&D. Despite this positive result, not all firms are investing in R&D. Innovation is increasingly important for long term success and many in the industry have taken advantage of funding available from Callaghan Innovation, in the form of growth, project and student grants.
- Certainty of supply, either from New Zealand or overseas, is recognised as a critical success factor within the industry, particularly access to raw materials. This, along with international government regulations, was also identified as a key barrier to growth, particularly by our larger firms. A number of regulatory and compliance issues continue to cause frustration to the industry, and it is implied that significant increases in both domestic and export sales can be achieved when these are addressed.
- Additional information supplied by Ministry of Business, Innovation and Employment ('MBIE') that relates to innovative foods makes interesting reading. The products classified in this sector include those shown on page 41 of the report. Our relative performance as a country compared to other exporters to South East Asia is impressive (3rd) with MBIE indicating this as an area where they see a strong growth opportunity.
- The shift in emphasis of importance of export markets is evidenced by the survey responses when comparing UK and Europe with Asian markets including China and Hong Kong. Only smaller firms expect growth in the UK and the US while larger firms are more confident here in New Zealand, across the ditch in Australia and into Asia.



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