Sustainability – Challenges in Sourcing Agricultural Materials

Hans Jöhr
Corporate Head of Agriculture
The Nestlé Company

• The leading food company
  – 98'458 mio CHF in 2006

• Swiss based, active world-wide
  – 481 factories in 87 countries
  – about 250'000 employees

• Global sourcing strategy
  – local adaptation
  – source about 2/3 of our agricultural materials in emerging markets

• Total purchasing value of agr. materials: approx. 17bio CHF
Main Agricultural Materials

- **Milk**: 11.9 mio t
- **Coffee**: 741'000 t
- **Cocoa**: 370'000 t

... fruit, vegetables, cereals, potatoes ... partly sourced directly from farmers

... sugar, oil, meat, spices and other ingredients sourced through trade

Value: 17.5% of our turnover
Sourcing Objectives & Challenges

• Sourcing must contribute to:
  – sustainable & profitable business
  – competitive pricing
  – lowest system costs (zero defect, no-waste)
  – shared values throughout supply chain

• Sourcing must be the base for safety and quality
Quality is our priority

The 3 Dimensions of Food Quality
Emerging economies are set to boost the GLOBAL DEMAND and SUPPLY for consumer goods

Emerging economies have been growing faster than developed ones and catch up **thirsts** of their ever-growing population

Fast growing economies represent:

- 1/2 of the world **energy consumption**
- 70% of world's Foreign exchange **reserves**

Source: The Economist and OECD
Drivers for change

Opportunity: serving more consumers

Growth concentrated in developing countries and overwhelmingly urban

In 2005 the world became over 50% urban

Source: OECD
Drivers for change & challenges

- Changing business environment
  - trade & manufacturing
  - regulatory requirements
- Consumer expectations
  - new quality thinking
  - manufacturer liability
- Consumers concerns
  - food safety issues
  - production methods
- Geographical decoupling of supply and consumption
  - logistic / infrastructure / legislation
- Future food / feed / fibre / energy needs

The big challenge today is breaking the link between economic growth and negative environmental impact.
There are clear limits to the earth's natural resources capacity.
Consumer expectations and concerns

Social Responsibility & Personal Values
- ethics, fair trade
- labor issues, rural life, politics ...

Functional quality
- environment, technologies (GMOs), animal health & welfare...

Emotional quality
- emotional quality

Access / Affordability
- convenient
- safety
- conscience
- function
Challenges in upstream supply chain

- Transparency, traceability from farm to table to address consumers preferences:

  - SAIN / SAI
  - NEMS ...

  - quality & safety
  - efficiency & productivity
  - consumer perception
  - company image

- ethics, fair trade
- labor issues, rural life, politics ...
- environment, technologies (GMOs), animal health & welfare, ...

Input Providers → Farmer → Trade Processor → Food Industry → Trade Retail → Consumer
Collaborate on industry level

Food Industry Initiative
support of sustainable agriculture in general

mainstream agriculture pre-competitive

• Key raw materials
• Direct sourcing
• Preferred suppliers

60+ Countries
Agricultural raw materials supply chain
Examples of Nestlé direct sourcing

- **Milk**
  - Argentina, Australia, Brazil, Chile, China, France, India, Spain, Turkey, Pakistan ...
    - ensure sustainable supply

- **Coffee**
  - China, Indonesia, Malaysia, Mexico, Philippines, Thailand ...
    - assist in coffee cultivation

- **Cassava (starch)**
  - Ivory Coast
    - Public Private Partnership with
      - ensure long term supply
Nestlé Example

• Milk. e.g. Pakistan
  – Farmer training in
    • Animal husbandry, feeding, health
    • Farm management, profitability
    • Milk quality, safety
    • Collection, cooling in 3200 villages!
    • Sustainable production...
  • train about 140'000 farmers
Nestlé Example

- **Coffee** e.g. Thailand
  
  - *Arabica Experiment & Demonstration Farm* - part of the Royal Development Project
    
    - scientists trained in somatic embryogenesis
    
    - train "trainers" & farmers
      
      (up to 16'000 / year)
    
    - fertilization, irrigation, harvesting
      
      ...
    
    - bought 34'400 tons in 2006
Our overall strategy

The Concept of Shared Value Creation

Value Chain Innovations for Nestlé and Society

New innovative sourcing & purchasing practices

Adapted environmental, labor and safety practices

New/Renovated Products for Nutrition, Health and Wellness

Agriculture & Sourcing

Manufacturing & Operations

Consumers

Agricultural & local supplier development

Food safety standards & workforce development

Nutrition knowledge & awareness

Building the Context for Growth

Our overall strategy
All inclusive value chain approach linked to consumers

Input Providers → Farmer → Trade Processor → Retail → Consumer

Extension services on technical assistance & farm management advise

Name of chairman

October 2007
Corporate Social Responsibility built into Nestlé's strategy

CREATE SHARED VALUE
Reduce poverty,
Improve health
Empower people

SUSTAINABILITY
Protect the future

COMPLIANCE
Laws, Business Principles, codes of conduct
Creating shared value in practice

Aimed at creating improved business conditions for the company:
- reliable, high quality sourcing
- improved government functioning - regulatory
- skilled, loyal workforce
- superior products which successfully compete

For society, results in:
- improved earnings of suppliers
- increase skills, job stability
- higher quality of life
- greater stability, economic and social development

2/3 of all 250,000 employees receive formal training every year

Linking farmers to markets to generate regular cash flow
• Interactions with more than **500,000 farmers** directly supported by more than 650 sourcing agronomists and 4,500 technical staff working at farm level and in supply chain

• Running more than **150 Sustainable Agriculture projects** worldwide with many different stakeholders
Final remarks

• **Sustainable supply of safe & compliant agricultural materials absolutely required**
  – safety & compliance are the "license" to sell
  – consumers simply expect that their food is safe and produced out of sustainable production systems (triple bottom approach)

• **Huge efforts of the whole chain are required**
  – enforce good agricultural practices
  – apply active and not re-active sustainable sourcing programs

• **Sharing knowledge and value with stakeholders**
  – based on trust and efficiency
  – mutually agreed "sustainability" standards / schemes / approaches...
  – clear common objectives (focus on measurable targets)

• **Nestlé supports**
  – joint industry efforts on sustainable agriculture
    (http://www.saiplatform.org/)
  – runs own programs on direct sourcing from farmers
"Sustainable Agriculture is productive, competitive and efficient while at the same time protecting and improving the natural environment and conditions of the local community"

*(definition mutually agreed by SAI founding members; Group Danone, Nestlé and Unilever)*
Sustainable sourcing practices are widely accepted by leading Business Research Institutions as being the way forward to successful business.
Business case for sustainability

**Value Drivers**
- Sales
- Cost
- Tax Rate
- Investments
- Financing Structure
- Risk Premia

**Outcomes**
- Resource Efficiency
- Lower Environ. Risks
- Innovative Products
- Price Adv.
- Quality Adv.
- Brand Value
- Differentiation
- Customer Satisfaction
- Employee Satisfaction
- Total Tax Contribution
- Reputation

**Processes**
- Risk-, Rep.- & Stakeholder Mgt.
- Regulatory & Compliance
- Production & Resource Mgt.
- R&D, Innovation
- CRM
- HR
- Tax
- Finance
- IT
- IR
- Communication
- Reporting (Sustainability)
- Sponsoring
- Community Affairs

**Shareholder value**

FCFF = Free Cash Flow to the Firm. WACC = Weighted Average Cost of Capital

*Source PricewaterhouseCoopers*