Wine Business Solutions

The Wine Paper 22

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The Quick and the Dead

When a turnaround happens in agribusiness, it generally surprises people. It's hard to image "sunshine" after six or more years of "rain". Those that have seen cycles will be aware of what's to come. Those that are ready to run will benefit significantly.

Most of you will have seen this "Wine Industry Wheel of Fortune". The GFC helped delay timelines by eighteen months or so in California, two years in Marlborough and more in Australia where major structural problems have never actually been dealt with but otherwise, it has proven to be accurate.

Figure 1 – Wine Industry Wheel of Fortune

What's not necessarily clear from this diagram is the speed at which things change. In Marlborough this week, for example, Warburn Estate (effectively Woolworths who are the biggest importer on NZ Sauvignon Blanc into Australia) has just increased grower payments by 35% for next season. This reflects acute competition for fruit in the face of shortage and will result in the price of own label increasing to the point where brands will have an advantage.

Best poised to "make hay" will be brands like Villa Maria that never fully capitalised on the "Sauvignon Blanc Boom" but have built up a lot of consumer trust over time and will now constitute a significantly better customer value proposition than over-priced own label . Now is the time for those sorts of brands to be investing heavily in consumer brand building using funds that were previously used to support price.

So what other opportunities are out there? Definitely now is the time for mergers and acquisitions. Foley has bought the NZ Wine Company and Yealands has bought Ager Sectus. The entire mid-tier of NZ is consolidating. There's more to come.

In Australia, after selling a medium sized WA wine business at a premium following a long but thorough campaign through the bottom of the market, we now have clients actively looking to buy wine industry assets. In South Africa we have worked on the merger of Co-Ops. Weakening currency has taken a little of the pressure to consolidate off but the lowest cost / largest scale operators will ultimately win out. Now is definitely the time to move. WBS associate Adam Parkinson is currently working on a project in South Australia to optimise the throughput of a 20,000 tonne facility. I'm helping to do the same for a 12,000 tonne NSW operation.

Most importantly, we have assisted clients through the formation of strategic alliances leveraging our network. As conventional wholesalers struggle to make a margin on selling 60 or more brands, companies that have invested in a sales force and who have targeted a limited number of growth opportunities through partnering with specialist producers are experiencing significant gains.

In terms of wine style opportunities at premium price points in Australia it's still all about cool climate.

Figure 2 – Sales of $20 plus wine in Nielsen audited retail to June 2012

$20 Plus	$(000'S)	Val % Growth YA	Val % Share	LITRES(000'S)	Vol % Growth YA	Vol % Share	Price Per Unit ($)	Number of SKU's	$(000'S) per SKU
Chardonnay	24,254.2	9.5	9.9	684.7	9.3	3.6	26.51	606	$ 40
Shiraz	78,625.2	8.3	27.5	1,980.8	7.6	12.1	29.81	1,228	$ 64
Cabernet	42,230.2	2.3	25.3	1,057.7	1.2	10.7	29.96	592	$ 71
Cab Merlot	8,177.0	-5.2	7.7	241.8	-8.2	2.9	25.37	154	$ 53
Merlot	1,799.8	10.5	2.4	54.6	5.2	0.9	24.72	149	$ 12
Moscato	128.8	5.3	0.2	4.4	4.0	0.1	21.63	20	$ 6
Pinot Noir	27,388.4	14.5	41.6	771.8	13.9	27.0	26.61	731	$ 37
Pinot Gris	7,425.6	43.8	14.0	247.2	40.1	8.0	22.53	232	$ 32
Sparkling	73,176.1	11.6	24.6	2,215.2	13.2	11.8	24.77	243	$ 301
Sem Sauv	8,722.8	14.6	4.4	276.6	12.5	1.9	23.61	86	$ 101
Sauv Blanc	27,162.5	17.8	5.7	825.2	16.3	2.7	25.61	263	$ 103

These bottom five "cool customers" highlighted in yellow grew their share of volume and value by an amazing 15% on average in the last year. Overall, the $20 plus category was up 10% by volume and value. As we will see, this reflects growth trends in other markets at premium price points.

Pinot Gris is still growing at breakneck speed and is the easy answer now for people who have quality fruit. People like Andrew Hendry at Coopers Creek who have specialised in Albariño and Nick Nobilo with Gewürztraminer have a very bright future in my view. The biggest opportunity for New Zealand, Tasmania and cooler regions of mainland Australia is with Chardonnay. Although growing at a more modest 9.5%, "Ultra-Premium Chardonnay" should be a more profitable and sustainable idea going forward as the concept becomes popularised. Smarter marketing and more group initiatives are needed. Chardonnay and cooler climate Shiraz must form the central planks of Australia's go forward strategy.

Where does that leave Cabernet? There is a major opportunity emerging for Margaret River, Coonawarra, Hawkes Bay and Stellenbosch in North America at high price points. Napa is running short and price expectations of wineries at the high end are increasing markedly.

Figure 3 – Supply / Demand Analysis of Main US Varietals – Source, Silicon Valley Bank

It gets more interesting still when you look at the US by price point. Basically the higher the selling price, the stronger the recovery in the last 12 months. Just like the stock market, there has been a lot written about trading down in the recession, not so much about recovery.

Figure 4 – Net Change in Price by Price Category YTD June 2012 – Source, Silicon Valley Bank

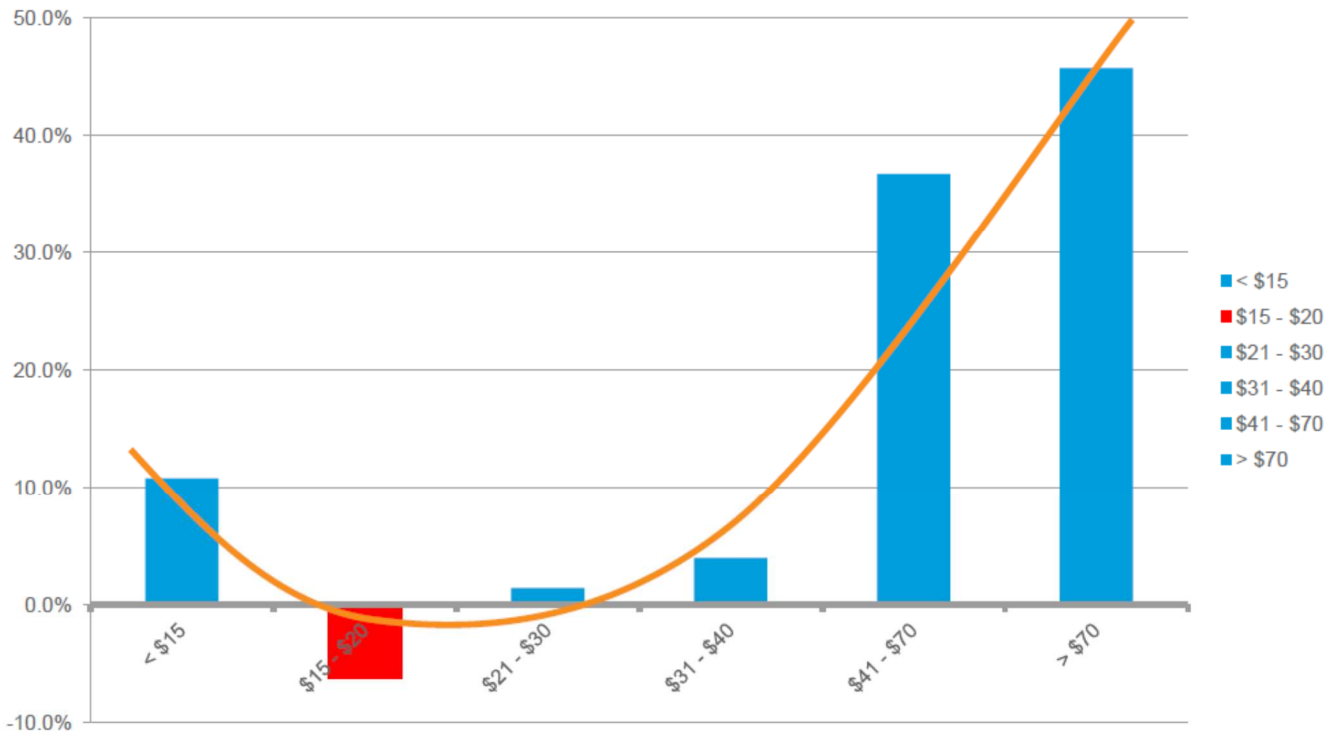
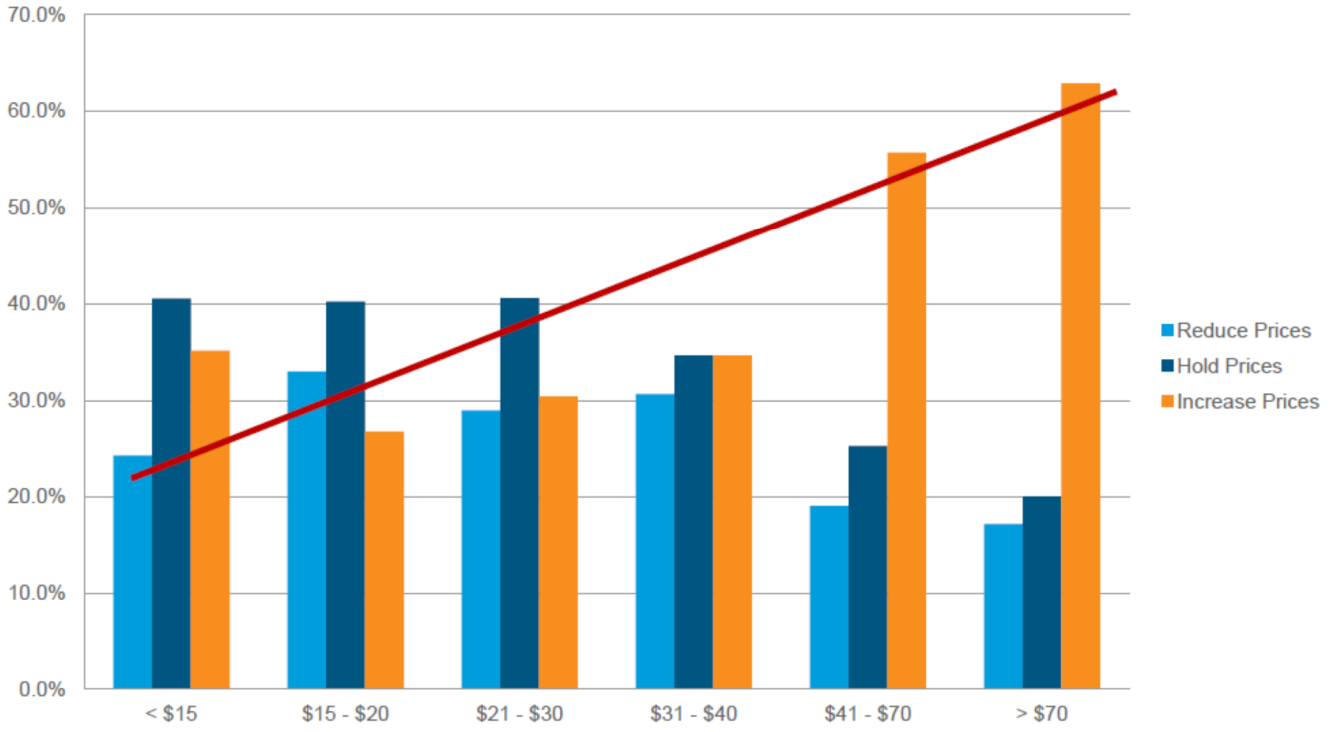


Figure 5 – Expectations of US wineries for pricing during next 12 months – Source, Silicon Valley Bank



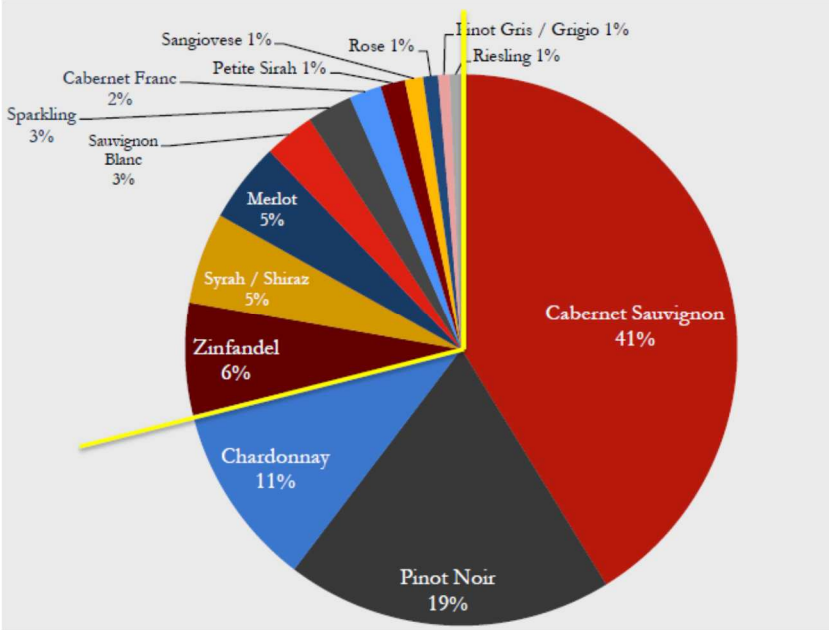
This constitutes a golden opportunity for Australia in particular to "do it right" (i.e. to make the story about the people involved, selecting the right sites, choosing the right clones, growing with the right row spacings and pruning methods, managing the soil and water properly, making the best possible wine and doing it sustainably) rather than trying to take shortcuts with Parker Points.

It's also about developing smarter go to market models. The competition for premium imported wines in the US is strongest from good on the ground direct marketers. The opportunity is not to beat them but to join them through setting up your own direct to customer and direct to trade operations. WBS is helping a number of clients with this.

Through these channels the opportunity for ultra-premium Cabernet, Pinot Noir and Chardonnay becomes more pronounced still. These 3 varietals make up 71% of Direct to Customer spend.

Figure 6 – Average Bottle Price of Wine Shipped Direct to Consumer in the US – Source Shipcompliant

Figure 7 – Proportion of Direct to Consumer spend by varietal in the US – Source Shipcompliant



The bounce back is stronger still in the UK with Nielsen reporting a 32% increase YTD April for wine sales over £10 in the off trade. Our Wine On-Premise UK 2012 report is due for release shortly. You can reserve your copy and find out where the opportunities are by following this link.

When originally contemplating Direct to Customer as a topic for our 2012 workshop series, I had considerable reservations. Prime amongst them was that this may be a fad. We've all seen how internet companies exploited people's expectations that having a web site would deliver advantage. Then everyone had one. Then it was a shopping cart, then social media and so on giving rise the question – "What happens when everyone starts selling direct?"

After six sold-out workshops in McLaren Vale, the Barossa, Western Australia, Stellenbosch, Sydney and Melbourne, we now have significantly more insight into just what makes wineries' Direct to Customer (DtC) strategies work. *(Note – Workshops in Tasmania, Marlborough and Hawkes Bay are coming soon)*

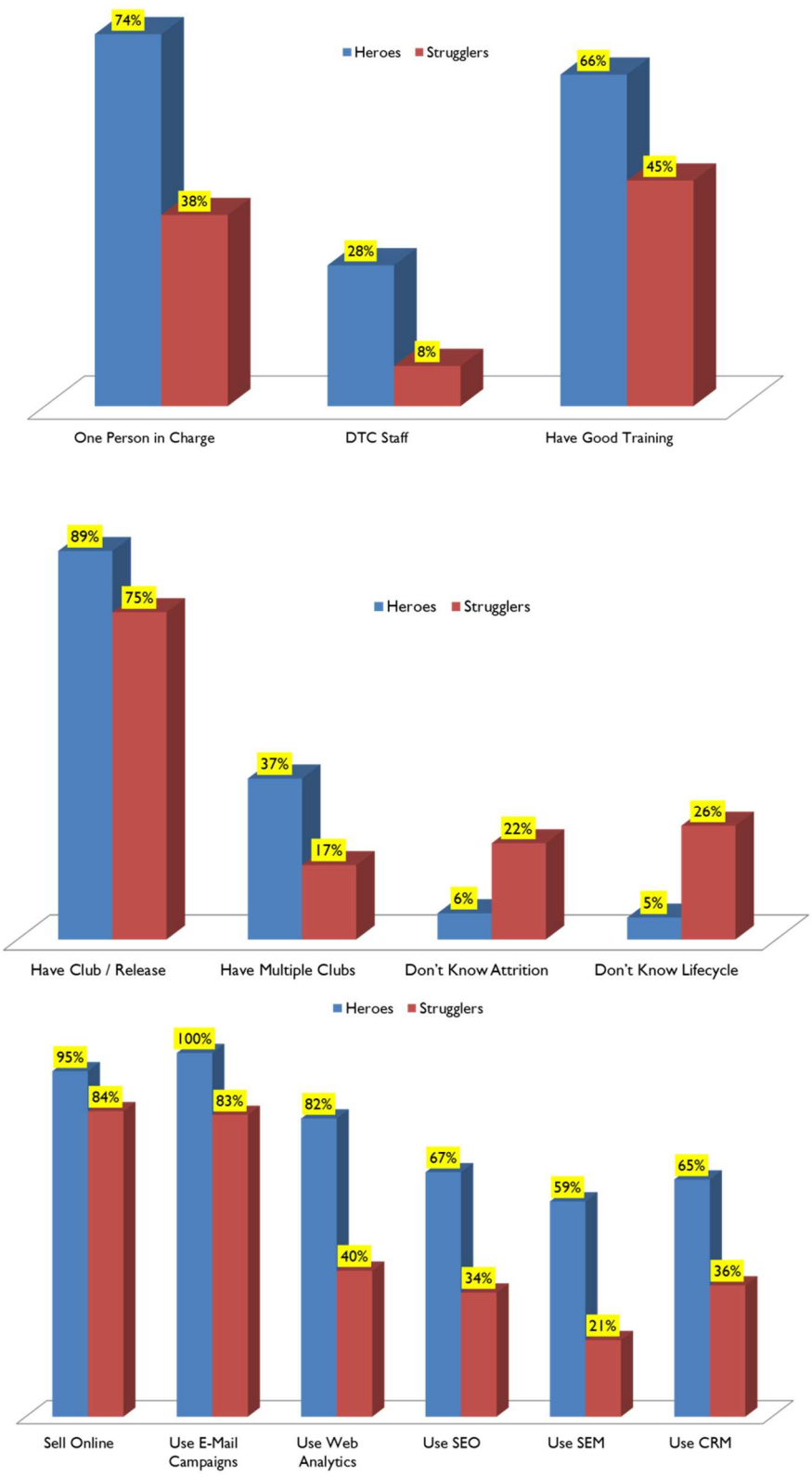
After seeing our customers operate who are successful in this area, I am now utterly convinced that well executed DtC strategy is a source of sustainable competitive advantage. Why? Because it is difficult, it is complex and it requires focus. These are genuine barriers to entry. It might sound counterintuitive but these are the only circumstances under which any of us should consider doing anything in business. Otherwise you risk being copied and competed out.

And the differences in performance are startling. Watching people who have worked out how to build DtC business is like watching dragsters burning down the runway whilst their neighbours sit on tractors with flat batteries. It's that clear cut.

So what is making the difference? What's a wine business need to do to join these star performers?

1. **One person responsible.** Wise Academy of California researched its database of wineries and sorted those that they called "heroes" (the top 15% of performers) from the rest – "strugglers". One thing that is clear immediately is that those companies that allocate dedicated resource are over represented in the "hero" group.

Figure 8 – Performance of "Heroes" vs "Strugglers" as defined by Wise Academy LLC



2. Events

It all starts with making people happy and having them remember you. It's that simple. Some, like Grant Burge, have been doing this for decades before technology was developed to support the DtC effort. Getting events exactly right and optimising outcomes in terms of member sign up and sales depends on a lot of semantics. The two day workshops have been a great opportunity to work through exactly what these are.

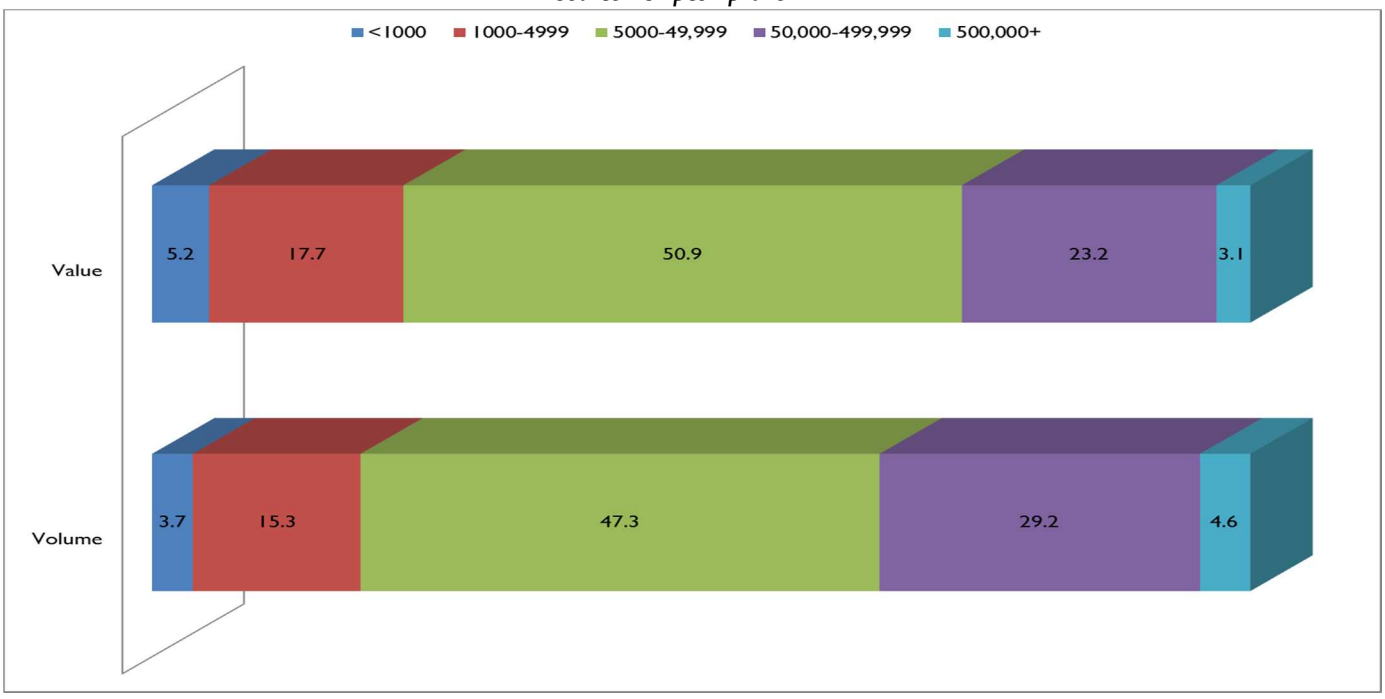
3. A determination to build a quality database

Everyone in our network and that of our families, employees, suppliers, growers, shareholders and even trade customers can and should be part of our loyalty program. We spent a lot of time workshopping the best ways to do this.

4. Smart use of technology.

The software and systems available are now highly sophisticated, easily integrated, cloud based and cheap to access for small business. At the same time, small wine companies have, by and large, not fully grasped the opportunity that DtC marketing presents. As earlier mentioned this takes time, focus and dedicated human resources, not things small business owners typically have in abundance. I have not included "money" at this point because many of the most useful tools and technologies have little or no cost associated with them. Small companies can therefore be excellent at this discipline.

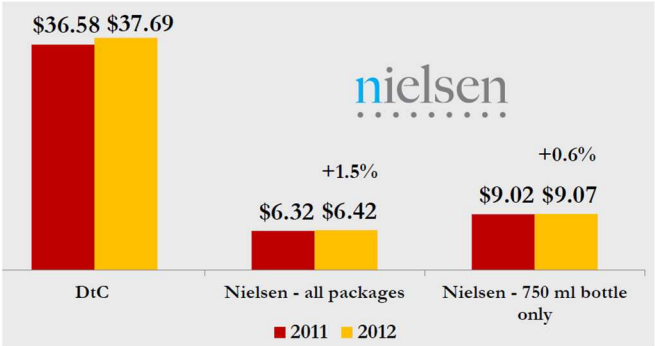
Figure 9 – Proportion of Direct to Customer sales by wineries of varying 9 litre case production levels
Source - Shipcompliant



Large wine companies, conversely, often miss the potential because they are looking at the wrong set of numbers, just as they do where On-Premise opportunity is concerned. In the US, according to Shipcompliant, DtC shipments make up just 1% of production. (I can hear listed company people snoring right about now…)

In value terms, however, DtC shipments are equal to 11% of the entire market that Nielsen measure in the US and 21% of the Nielsen audited grocer channel according to Shipcompliant. When you further consider that DtC sales normally yield 8-10 times the profit of sales through 3 tiers of distribution, the case for DtC really starts to become compelling. This is because the average value of a bottle sold DtC is around 4 times higher. Our successful Australian customers further confirm this.

Figure 10 – Average per unit retail sales point by channel and pack size – Source Nielsen and Shipcompliant



The real winners currently are medium sized companies that can move quickly and allocate dedicated resources. WBS has many clients who are adding literally $millions to revenue through a single person engaging a database often of no more than 5000 consumer customers in a well thought out program of activity.

5. CRM

This year's workshop program gave us the chance to properly research what's out there, to talk to participants about implementation and to develop strategies for overcoming issues and shortfalls. Finally the holy grail of low costs integrated systems is at hand. Your web site back end and POS software should be able to be integrated with your accounting and inventory management system so that: -

- if a customer interaction occurs, you can capture it
- if a sale takes place, you can account for it
- if a status changes, it changes everywhere

- if a record is needed, it can be easily located
- you can measure campaigns, sales, prospecting
- spotting trends in customer activity is easy.

If not, we can help. As always we take and give commission to no one. We simply promote those providers that, in our customers view, do the best job.

6. It's all about people

One of our South African clients who has been singularly successful in turning his business around through marketing direct to customer using low cost technology. His business has grown by more than 40% for each of the last three years. When I asked him what the real secret was, he said that the most important factor was getting key family members more engaged.

CRM has always been about managing customer relationships. We just have better, lower cost tools to help us do this more efficiently and effectively now. Making DtC a central plank of business strategy, as some firms should and many must, often requires a shift in business culture.

Recognising this, WBS welcomes Luanne Hill as an Associate. Luanne has vast experience in leading change initiatives and developing leadership within some of the world's best known service businesses. She specialises in making change stick. She also runs her own wine business with her partner so has much hands-on experience.

At a time when many of you will be thinking about gearing up, handing over to the next generation or cashing in on your hard work, we've put together a team to help you find the best possible solutions.

The "Top Ten Tips" for Building Better Wine Businesses.

(From a Wine Business Solutions article published in Wine Business Magazine)

One - Start by understanding your customer value proposition. Only part of this stems from your company's unique heritage and / or personality. To be successful, this needs to be strongly linked to what your customers ultimately want from the experience of your brands. There is some excellent research on this that is publicly available. Getting it right is therefore not out of the reach of small companies.

Two - Once you understand what customers value most, you can then remove what they don't want (thereby reducing costs and freeing up cash), focus your communication on what they do want (often at no additional cost), differentiate your company on the basis of fulfilling customer needs more accurately than any competitor (again often at no extra cost) and raise prices (because your offering is more highly valued)

Three - Always be asking the question – "If I could start with a blank canvas today – what would our wine business look like?" It's all too easy to let existing assets, existing product lines and existing ways of doing things blind us to what it is that our consumers value most. Often it's simplicity. Complexity usually adds to costs and often only serves to confuse customers. Retaining unnecessary or irrelevant product lines, assets or business processes is the worst contributor.

Four - Make everyone in the company accountable for securing customer preference. This is not just the job of marketing but of everyone in the company, the owner most particularly. Make this the focus of the way every employee innovates their job processes on a daily basis.

Five - Invest in relationships. This is particularly so with major distribution partners. Make sure sufficient time and money is invested before demanding results. Be prepared to invest up front in bringing them to your home base and entertaining them in order to build enduring friendships.

Six - Make all employees champions for profit. Develop a culture of honesty around net revenue. Make sure everyone knows the actual price achieved net of all discounts, rebates, bonus stock and anything else that might otherwise cloud the true profit picture. Keep them focused on reducing costs but let them know that a percentage increase in wine company revenue is, on average, twice as effective as the same percentage decrease in the cost of goods sold and 3-4 times as effective as the same percentage saving in operating expenses.

Seven - Optimise your pricing mix. Focus first on selling more, higher margin product in high value markets to high value customers. Beware of people in love with "big volume". Big numbers make for big stories but often mean a lot of running around for no additional profit.

Eight - Build better business intelligence gathering systems – most companies are good at monitoring their own press. Very few have effective systems in place to monitor competitors, track changes in consumer preferences and turn customer feedback into customer value added.

Nine - Build 5-10 year Strategic Plans, forecast rolling 12 month budgets, link them to the most relevant KPIs and tie remuneration to these wherever possible. Everybody knows they should do this. Few do. The difference in the performance of companies that do is enormous.

Ten - Watch your cashflow – building a cashflow forecast is a relatively easy exercise with the right software and some quality assistance. Some people survive years of losses but you can only run out of cash once. In a cash hungry business like wine – Cashflow is not just King but Oxygen.