Wine Business Solutions

The Wine Paper 47

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Direct Impact

The results of our 2017 Direct to Customer Benchmarking exercise are in.

We've also just completed our Wine On-Premise USA 2017 research. This is now the 2nd year that we've looked at the world's largest On-Premise market enabling us to see clearly, the trends that are operating.

As we've found from 9 years of analysing the On-Trade in the UK (the true litmus for wine globally) as well as the Australian On-Premise, change in share of listings is a very reliable lead indicator, not just of On-Premise sales but also of what happens ultimately in the Off-Premise.

But what is the effect of Direct to Customer sales (DtC) on other distribution channels? Is there a link? Well of course we know that there is. This has been the lifetime's work of Dr Johan Bruwer who has shown beyond all doubt that there is not only correlation but causal proof (or as close as research can get).

What we are seeing in the US now, is what we have been predicting all along. US wineries have increased their share of On-Premise listings in their home market by 15% year on year, according to our research, which is just a tick under the rate at which DtC shipments are increasing.

Now correlation is never proof but I am certain that if Johan were to run his rigorous process in the US, that it would confirm common sense. If so many people have been able to try, buy and become loyalty club members of American brands, why would they take a risk on an unknown brand when out to dinner?

Producers from imported countries must therefore respond with their own direct to customer strategy or risk being driven out of the market. Whilst there will always be some place in the US for highly differentiated product such as Champagne, most European wines and, maybe even, Marlborough Sauvignon Blanc, it's difficult to see how much of the rest of the New World offer will hold its place.

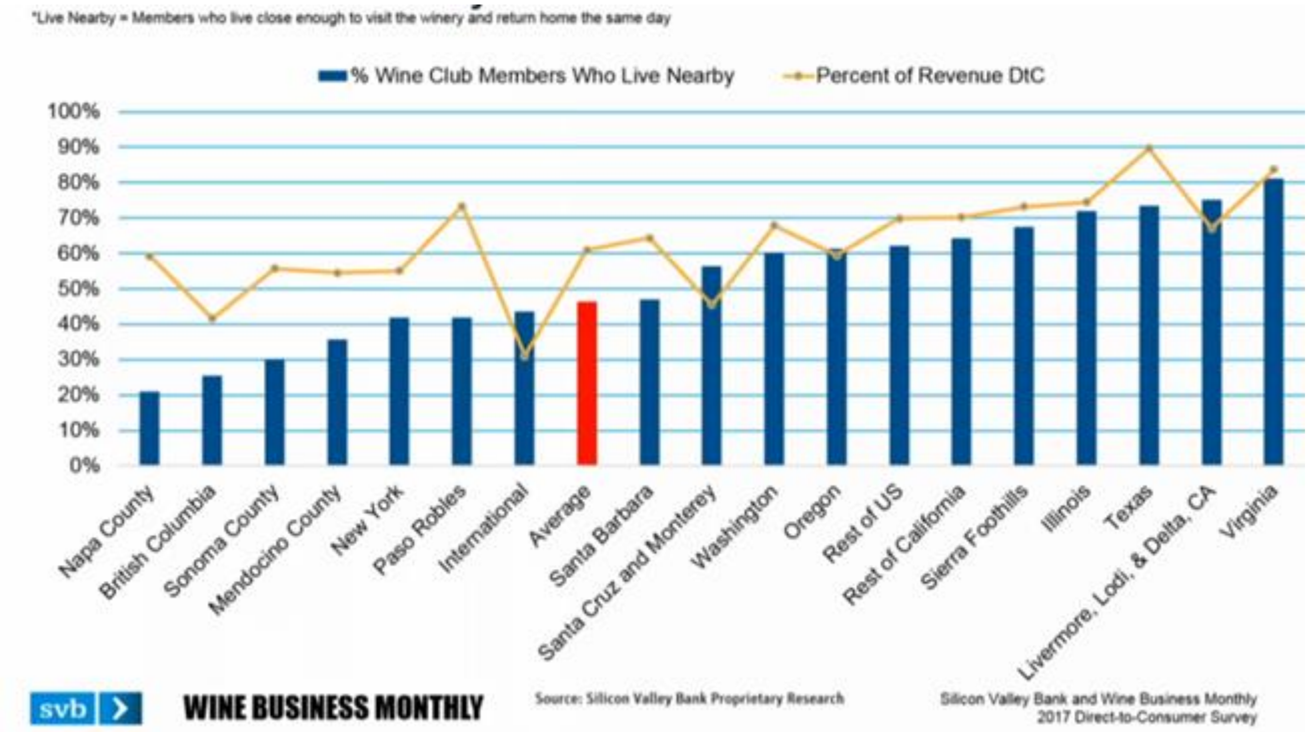
This is where Australia, New Zealand and South Africa are both challenged and advantaged. We speak the same language and share (some) of the same humour with our American friends. But unless producers from these countries can match or better US wineries' DtC efforts, the prognosis is not good.

When the Australian Government made their $50 Million Export and Regional Wine Support Package substantially contingent upon developing international direct to consumer business, this was perhaps a better move than what most believed it to be (whether or not the government intended to be that clever).

From early discussions had with key Australian producers and other industry leaders, most felt that this exercise would be a 'tick box' thing to keep the government happy, rather than the real way forward. This is understandable as direct sales in the Australian context are currently almost entirely about selling to those best placed to drive to the winery (no matter how miserable those individuals may happen to be.)

This has meant that all the $millions spent advertising Australian wine regions has been primarily about creating 'travel porn' and thereafter about interstate and international visitors visiting, well, restaurants... But isn't it the same in the US? Well no, actually. The more highly developed a region is in terms of DtC and the stronger its brand is consequently, the less likely it is that direct sales will be to locals.

Figure One – Members who Live Nearby* vs Total Revenue from DtC Sales



Many of our South African clients absolutely get how important international visitors are to their future and are well set up to do home market fulfilment of DtC sales made to foreign tourists at the winery, as well as those that result from hosting in-market consumer events in export destinations.

This hasn't been the case for the overwhelming majority of Australian producers but there are now strong incentives to change. The partner options range from people simply operating an online retail store through to full DIY direct sales out of California as the Molly Dooker and others do.

China is a bigger challenge but we have connections who can do door to door fulfilment to that market as well. They will be launching their Cloud Based, WeChat enabled Mandarin POS platform later this month. Anyone that would like to know more about that, please just be in touch.

You may have seen the publicity already. Now, for the first time ever, more wineries in Australia, New Zealand and South Africa charge for tasting than do not, according to our [2017 DtC benchmarking].

The University of Central Florida's Robin Back (Cousin of Charles Back of Fairview fame) can take a lot of the credit here, I feel. He was the first to carry out research that confirmed that people actually buy more wine when they pay for tastings. Logically, if you are given something for free, you value it less.

We've therefore pushed this hard to the 200 plus wine business owners and senior managers who have attended our workshops over the last 12 months across the three countries. It's very pleasing to see that wineries have now completed the revolution.

A lot of the resistance has been down to a fear of upsetting people who for too long have been using the wine industry as free entertainment. That is all changing. Those wineries that are charging are getting that, in order to command a fee, the 'entertainment product' must be better. Tasting fees also mean more money to pay for better staff and the training thereof.

Whilst visitor numbers across Australia, New Zealand and South Africa are up 12% overall, only South Africa managed to keep pace with the US' DtC growth of 18%. Australia only grew DtC sales at 8% and New Zealand, barely at all.

This is largely to do with the difference in the type of experience offered and sales training. These are relatively easy fixes that we can help with.

As we have been stressing all along, the seated, structured, paid tasting experience is around 6 times as effect as the belly to the bar, bottles on the bench, walk up sampling demo.

That all starts with first knowing who is visiting your cellar door. You can't measure conversion if you don't count visitors. The number of wine businesses that are doing so has actually declined to barely half (54%).

Our 2017 research shows, however, that the difference in DtC revenue attained by businesses that count their customers and those who don't equates to $A120,000. Those that counted visitors typically increased sales by 8% in the last 12 months. Those that did not declined, on average, by 4%. ($A1Million being the average DtC revenue for all survey participants). Kind of makes its own case for hiring that DtC specialist and doing some decent staff training?

There is another profound change happening in the US On-Premise. Not only is there a big swing to local product, there is an even bigger swing back to the major wine styles and away from so called 'alternative' varietals. We've seen the same thing in the UK and Australia On-Premise but nothing like to the extent as is currently happening in the US.

Figure Two – Share of US Wine Listings by Wine Style.

Style	2017	2016	CHG
Chardonnay	28%	19%	48%
Sauv Blanc	20%	15%	31%
Pinot Gris/Grigio	15%	14%	10%
Riesling	11%	13%	-12%
White Blend	4%	3%	17%
Moscato	3%	4%	-37%
Albarino	3%	3%	-14%
Chenin Blanc	2%	4%	-41%
Gruner Veltliner	2%	2%	-25%
Viognier	2%	3%	-54%
Gewurztraminer	1%	3%	-55%
Vermentino	1%	1%	-11%
Pinot Blanc	1%	2%	-37%
Verdelho	1%	1%	-32%
Arneis	1%	1%	-43%
Rhone Blend	1%	1%	10%
Soave	1%	1%	-30%
Bordeaux Blend	1%	1%	-37%
Muscadet	1%	1%	-43%
Others	5%	9%	-49%

Style	2017	2016	CHG
Cab Sauv	20%	13%	56%
Pinot Noir	20%	13%	53%
Merlot	10%	10%	-2%
Malbec	8%	8%	-8%
Zinfandel	7%	7%	-4%
Syrah/Shiraz	5%	7%	-25%
Red Blend	5%	2%	108%
Sangiovese	4%	5%	-5%
Tempranillo & Blends	3%	4%	-19%
Nebbiolo	3%	2%	13%
Rhone Blend	2%	2%	-6%
Bordeaux Blend	2%	3%	-39%
Grenache & Blends	1%	3%	-51%
Barbera	1%	2%	-20%
Gamay	1%	1%	-10%
Montepulciano	1%	1%	-28%
Cab Franc	1%	2%	-64%
Amarone	1%	1%	-50%
Nero D Avola	1%	1%	-20%
Cab Blend	1%	4%	-86%
Valpolicella	0%	0%	4%
Dolcetto	0%	1%	-41%
Carmenere	0%	1%	-67%
Mouvedre	0%	1%	-63%
Others	2%	5%	-57%

We use just under 40,000 listings for our sample so there is next to no possibility that this change and the magnitude of it isn't real. The thing is, it was never that these most listed and liked varietals weren't the best to make wine with. It was down to them being grown in the wrong places and made in the wrong way resulting in boring wine at best. This has changed massively during the last 5-8 years and no more so than in Australia.

What does this mean in terms of how each country needs to adapt its strategy? Let's look at it on a country by country basis.

Positives

New Zealand is the fastest growing major country category in the US On-Premise, increasing its share of listings by 49% in the last year to over 3% of total, according to our research.

New Zealand has arguably the strongest brand set of any supplier country. The Top 20 most listed is a real roll call of New Zealand's best producers. The gimmick brands, distributor owned and retailer labels that have infected the category in Australia and the UK simple haven't cut it in the US. This is one of the great benefits of selling in this market. US consumers and the three-tier system that supplies them loves brands.

Negatives

Marlborough has the lowest listed price of any Region in the Top 30. Even the Veneto and the Languedoc average higher.

This is because the New Zealand category has been set up at $10 per bottle lower in the On-Premise than both the international benchmark for New Zealand wine and the standard pricing for their quality level in the US. Quoting one NZ client – "After having had all the value knocked out of our price over 20 years by British supermarkets, we then went straight in at the bottom in US". New Zealand has at least been able to increase its average listed price by 5% this year and is no longer on the bottom. That honour now belongs to Chile after having had some ambitiously priced ultra-premium wines delisted.

Sauvignon Blanc now makes up 88% of New Zealand's total listings. Pinot Noir, the great hope for the future, is not even 4%.

Opportunities

The biggest single opportunity is Pinot Noir. That segment is under huge pressure in the US right now as the owners of major brands such as Meiomi scramble, driving prices of land and fruit through the roof. There is also a lot of Pinot being made in the wrong climate zones. When a wine idea doesn't work, it's usually because you priced too low or too high, you were too early or too late, you made the wrong style or whatever. I've talked to many of the major producers but maybe you don't talk to each other – Guys, you were just plain unlucky. The importer brought out his own brand, left your wine in a shed, got distracted, etc. I really cannot see why you can't be successful if you refocus and get with the right partners.

Positives

Probably the single best thing the Australian category has going for it, bizarrely, is the investment of a US company. The Jackson Family show the world how it should be done. Buy the highest quality vineyards you can. Restore them. Make it about region. Make it about your place within it. Make the best wine you can. Don't intervene too much but be highly innovative and progressive. Price appropriately. Find the best paths to market - Yangarra is the 3rd most listed Australian brand in the US after Penfolds and Jacobs Creek.

'Hipster' brands like Jamshed and Lucy Margaux are gaining traction through Vine Street Imports but is this really what we want to say about Australian wine? These wine styles can and are being made everywhere.

Negatives

Australia's listings fell by over 20% last year. The drop in Shiraz listings was one of the main drivers. Australia is, also, losing share within the Shiraz category. (30% vs 37% last year). The US (59% vs 42% last year) are soaking up Shiraz listings from everywhere. What their winemakers chose to do with the style going forward will, therefore and somewhat perversely, have a big impact on Australia.

5 of the Top 20 brands (Jacobs Creek, Cup Cake, Lindemans, 19 Crimes and Wolf Blass) have a cheaper average listed price than the cheapest US Top 20 brand. Why? You wouldn't buy someone you didn't like a bottle of Jacobs Creek or Lindemans in a restaurant in the UK or Australia (you can't find these wines on wine lists in those countries in any case) so why ram these products into your most import image building channel globally? Won't someone who has real clout please talk to these people? Meanwhile these brands are all the fastest growing whilst most of Australia's best regionally driven brands are the fastest declining.

Opportunities

The single biggest opportunity that Australia has is that the majority of the Top 30 importers don't even carry an Australian brand. One of the best of them told a client that "they would have to have rocks in their head to carry an Australian brand". A larger one told another client that "of the 39 growth opportunities we recently reviewed, Australia ranked 37th". These are the most powerful and influential people in the US. It is they that need to be flown here to see the true splendour of the modern Australian wine industry. What will we sell them? Margaret River Cabernet and Chardonnay performs even worse than Central Otago Pinot, currently. That can only improve. Cool climate Shiraz, Riesling and Red Blends?

Positives

After years of struggle, South Africa is at least now a major country category that must be taken seriously.

Australia can only wish it had a friend in the US like Vineyard Brands (Ranked 12th) is to South Africa. None of the Australia friendly importers rank anywhere near the Top 30 list. Vine Street and Distinguished Vineyards rank 63rd and 64th, respectively.

Individual brands like Graham Beck, have been able to make a success of it doing it all themselves.

Negatives

After having been 'flavour of the year' last year, in this notoriously trend driven market, that baton has clearly passed to Greece as it has in many other markets that we measure. South Africa's share of listings dropped by 27% in the last year, the most of any major supplier country.

South Africa's share of Chenin Blanc listings remained steady. The issue is that the whole category fell by over 40%. And it wasn't even South Africa's fault. American restaurateurs have simply become so much more enamoured with producers further up the Loire who grow Sauvignon Blanc rather than Chenin.

The biggest issue for South Africa is lack of category clarity (i.e. what should South Africa mean to an American?) Running through the most listed brands in order – Graham Beck is mostly about sparkling wine, Adi Badenhorst is about, well, 'Hipster' wine, Man Vintners is about packaging, Ken Forrester is trying to make the world's best Chenin and Babylonstoren is mainly about wine tourism. So, what is one to think?

Opportunities

Clearly a coherent message around the country, its regions and their offer is the biggest challenge and opportunity. Eben Sade, part of the 'Swartland Revolution' along with Adi Badenhorst (both damn good winemakers), tried to lead the country down the path of focusing on blends. I firmly believe, and the US numbers confirm, that he was always on the right track with that. Old / Bush Vines Chenin will have its day.

It's South Africa's ability to show the world something it can't see from anywhere else, that is where the greatest opportunity lies.

The primary purpose of our US On-Premise research is to uncover the essential nature of the market. We examine independently owned On-Premise outlets, as opposed to chains, to see whether that part of the market is fundamentally different to the overall wine market.

The clear answer is "no". The three-tier system means that this is the best set up market on earth for building brands. By stark contrast, our UK On-Premise research shows very little evidence of hard brands in the table wine space. In Australia, many believe that that the supermarket duopoly means that if you are listed there, you can't build brands in the On-Premise. The reality is that the best do well in all channels.

In the US, they love a winner. Big Importers, big brands and big wine ideas all improved their positions markedly in the US On-Premise in the last 12 months, according to our research. If and until there is a major dismantling of the system, this trend is only likely to strengthen.

Figure Three – Countries Share of Brands and Total Listings

Country	Number of Brands	Share of Brands	Total 2017	Total 2016	CHG
USA	113	60%	48%	42%	15%
Italy	30	16%	17%	18%	-3%
France	19	10%	15%	18%	-16%
New Zealand	8	4%	3%	2%	49%
Argentina	7	4%	4%	4%	4%
Australia	3	2%	2%	2%	-21%
Chile	3	2%	1%	1%	-12%
Spain	3	2%	5%	6%	-21%
Germany	2	1%	2%	2%	-6%
South Africa	0	0%	1%	1%	-27%

So, who is winning and when is a wine label a 'brand'? It's an arbitrary decision. We've designated a brand as having more than 30 listings in our survey for the purpose of this exercise. The chart above looks at how many 'brands' each country has and their share of total brands. We then compare that with total listings.

You can see that those countries such as the US and New Zealand that have a disproportionate number of brands relative to their share of total listings are growing fastest. You can also see that those countries that have the biggest negative differential between their share of listings and number brands (France and Spain) are amongst the fastest dropping. If you need help with brand development, we've worked with some of the world's best. As always, we're here to help you build a better wine business.

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

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.

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