Wine Business Solutions

The Wine Paper 57

December 2019

The Biggest Mistakes

Page 3 – The Top Ten Wine Business Mistakes

Page 12 – The Top Ten Tips for Building a Better Wine Business

Making mistakes and learning from them is an essential part of both business growth and personal development. As Vasse Felix's Paul Holmes à Court neatly summed up to me over lunch, however, - "You've, perhaps, got to make eight or nine good decisions to make up for one bad one in this business".

Most wineries work with a 30-40 year horizon and don't have access to slush buckets full of venture capital so making the right choices is important. So is taking risks. But let's now focus on good decision making.

There are some grave mistakes that we see people routinely making that we would far rather they didn't. I prefer not to see people suffering unnecessarily even if there is more work for us in cleaning up afterwards.

This is particularly the case when new money / new people enter the industry. In every industry, there are things that are particular, peculiar, counter intuitive – things that you couldn't anticipate no matter how much broad-based business / life experience you have.

In order, here are our 'Top Ten Biggest Wine Business Mistakes' just in time for Christmas contemplation.

1. <u>Not engaging experts early enough</u>. (You may be thinking that I would say that, but I say so sincerely).

   A quick onceover costs very little. Fixing some of these basic mistakes sometimes costs millions. This is particularly the case when it comes to new brands, design projects and cellar doors / tasting rooms. This is often thought of as the 'fun bit' and project 'owners' are often reluctant to share. This is understandable as this is where everyone wants to have an opinion and a piece of the credit.

   One thing we are seeing a lot of currently, for example, is people travelling internationally, picking up ideas from tasting rooms in other countries (something we strongly encourage) but picking out aspects that may look impressive but aren't what they should have been focusing on.

   Tasting rooms are there to sell wine. Before and after the visit. That is all. We often see staff trying to turn the tasting room into a merchandise shop, a 'brand home' celebrating the wineries heritage, a wine bar, a wine food or travel 'experience' or any one of a number of other guises that avoid the 'dirty job' of actually forming a relationship with a customer, selling them wine and collecting their details so as to continue that relationship and, of course, sell them more wine. As this is all highly measurable, certain personality types will do almost anything to avoid it. You can't be tolerating that. For most wine businesses today, this is where most of your profit is locked up.

The way that you set up your 'theatre' has a profound affect on whether or not sales are made. You can change people's behaviour entirely, based simply upon how you arrange the space that you sell wine in. Well trained staff are critical but the setup of the selling space, marketing collateral, stemware, signage, cash register placement and supporting technology etc. is equally as important.

This is the easiest consulting work that we do. To see what people don't see when they see it every day. We've worked with some of the world's best operators in this space. I've seen literally thousands of tasting rooms in dozens of wine producing countries. We benchmark sales so as to objectively quantify and qualify success. We therefore have some idea of what works.

2. <u>Not getting your brand name right</u>

A brand name that is easy to see, say and remember is a wine business's greatest asset. I've written about this in detail before as have many others. This is not, of course, unique to the wine business. What is unique to the wine business is that, if you name your brand after your place or your family and it isn't unpleasant to the ear, then you're probably OK.

That might sound boring, but it works.

Still we see people failing with brand names all the time because their brand name is;
- unpronounceable (I should talk, with my last name)
- indigenous (and therefore very few people are confident saying it),
- abstract (requiring further explanation. It has to be intuitive. This also applies to branding / design)
- irrelevant or confusing (in terms of the name's literal meaning).
- jingoistic or colloquial (if you don't take your wine seriously, how can you expect anyone else to).

Solid names like Craggy Range or Shaw & Smith inspire trust. Difficult names are, well, just forgettable and unforgivable. Some like Freixenet and d'Arenberg get around it with clever packaging. You don't want to have to work that hard.

There is a lot more possibility to go again with a new brand name, if it was wrong the first time, than people generally believe <u>if</u> you are small brand. Exercises like Montana changing to Brancott or Taylors also trading as Wakefield are more challenging.

What is for certain is that of all the things that you have to fight to win, your brand name shouldn't be one of them. Sometimes it is better to simply let go and start afresh.

3. Underestimating the importance of Brand Architecture.

I was at a party a while back. It was in the days when I was still teaching in the MBA program at UTS. A young man approached me and said – "I'd like to do a program just on branding. Nothing else". My (difficult) task was to gently explain to him that 'branding', as he thought of it, is what you get to do after you know very well how to do everything else.

It is the same principal that world famous winemaking / viticulture consultant Alberto Antonini refers to when he speaks of doing 'little with wine'. Paraphrasing, he says that you only get to do little with wine successfully after you understand how to do everything extremely well.

Just like the millennial trying to make handmade cheese and salami down at your local Hipster bar, without the years of hard work put into understanding the intricacies of the craft, a lot can go wrong. A lot of learning is required before making something extremely complex look simple.

Deciding;

1. what the rules of your brand's architecture are (what you will and won't tolerate),
2. what your total offer looks like when pieced together,
3. how many tiers you will have (and how many SKUs within them),
4. how many brands you will have,
5. how you price everything,
6. what channels of distribution you operate in (understanding what that will do to price achievable) and
7. what your growth / contraction aspiration is,

are the most important decisions any wine business makes. Get any one of those wrong and it, really, will be millions of dollars down the drain and years to clean up. You want the best quality of input into those decisions that you can get.

Generally, the simpler, the cleaner, the less levels and the least number of brands (one is almost always the correct answer) then the greater your chance of cutting through in a massively crowded sector.

We still see people designing their offer like they are the only business that will ever make wine. Sales people never want to disappoint a customer by not giving them what they want. Better always to focus on what is good for your business rather than what is good for your reseller's business.

4. Not working hard enough on pricing

Pricing is everything when it comes to business profit and sustainability. If you don't build in margin / profit in at the beginning, you'll never get to it by cost cutting at the end. Not sustainably, at least.

Pricing correctly and successfully resisting resellers attempts to bash you down below where you need to be is the key. (We discuss this in detail in our [Winning by a Margin] best practice guide to reseller management).

It almost makes me ill when I hear people talking ex cellars or wholesale pricing who then can't tell me retail pricing. Avoid those people. All pricing should start with shelf / restaurant list / tasting room price and work backwards. All involved should know those prices and discount tolerances.

Price supports your image. It reflects your self-belief. It tells people where you sit in the market. You simply can't get it wrong.

Through our On-Premise research , Direct to Customer Benchmarking, analysis of On-Line retail, desk research library and other sources, we put a huge amount of effort into understanding pricing of wine now and where it's heading to in the future.

5. Not setting the right growth targets

I was once asked – "Is there a greater evil in the wine world than counting cases?" I think not. In a wine world that is getting smaller and becoming rapidly more premium, a plan that involves growing case sales volume needs to be compelling.

It's not that it doesn't happen. We can think of Duckhorn Vineyards or the Indelicato family's businesses in the US that were able to grow massively on the back of being able to produce good quality wines at the right price point post GFC (I'm talking $22 per bottle of Duckhorn Decoy, for example).

Surviving what Donny Sebastiani once described to me as the 'hell zone' (between 200-600,000 cases) is more than many great Australian names were able to manage in the 2000s.

Generally, most businesses that have survived and thrived that we deal with have reduced production, increased prices and sold more direct, in line with the market.

6. Not responding to change quickly enough

If we look at Direct Shipments of wine in the US, 25% of value or $1USBillion is at over $US100 per bottle. As more sales occur in the tasting room than the value of wine shipped, we can therefore project that the direct sales market for wine priced at over $US100 is $2USBillion plus in the US.

If we look at the price of wine in the On-Premise in Australia, for example, the average bottle of wine on a wine list has risen from $57 to $76 in just 5 years - a 33% increase.

This is all happening at the same time as the volume and value of wine in most markets is struggling to keep up with population growth and inflation. It's those big numbers that always hog the headlines.

And yet I still hear businesses, regions and even entire countries (including their government and representative bodies) talking about 'getting on the shelf' when that ought to be the primary goal for a handful of companies only. It should be the last objective for more than 90% of wine businesses.

Too many businesses are still using the wrong 'anchor' to determine what their price structure is.

Chain retailers work to drive prices down to what your wine costs. So even if that chain retailer leaves you with an acceptable margin when you sell to them directly, if they then dictate the price that you can sell for in other channels, then your brand will forever be compromised.

The On-Premise are driven by paying their rent and their staff through maximising spend. The Direct Channel is driven by what the consumer will pay when told your story. Each one of these channels produces an extremely different outcome in terms of both pricing and what your offer can be.

If you want to effect the change needed and get your business correctly orientated so it is selling the right product mix, at the right prices, to the right customers, through the right channels, then it is about reassuring your team that it is OK to get better. That we all need to get better. I see significant businesses, regions and entire countries at real risk of failing because their leadership are intent upon making people feel comfortable.

Statements about 'being true to who we are' are trumping ambition. The answer to the question I so often get asked – "can't we just sell wine to people like us?", meaning can't we just sell wine to people we feel comfortable with, is usually "No – those people don't have the money you need.". And no, it's not "wine made our way", it is wine made the best that it can be made. And you'll pay.

7. Not understanding the leverage of premium pricing.

There is a lot of idiotic stuff being written currently, in my view, that is being given credence by the world's leading wine business publications, written by people who don't understand the basic pricing dynamics of wine who are attacking the shift to premium. This is dangerous stuff.

Yes, there are examples of businesses and regions that are overreaching. It is difficult to make sense of Napa Valley Cabernet and associated tasting fees when outside of the US, for example, but these are rare. Even in Bordeaux, once you move outside of those famous names that are collectable, there is still a lot of good value to be had. In a market that is very much subject to global competition, things tend to get sorted out very quickly. Wine is, generally, worth what people will pay for it.

When you price at a premium, it's not a matter of a percentage increase in price equals a percentage increase in profit. There is a leverage effect. I have been in a longstanding battle trying to persuade South African producers to get their prices up. From the time that I started with this argument until this moment, things have actually gotten worse and Chenin Blanc is now the lowest priced white wine style in the UK On-Premise market, for example, at £22 per bottle, average listed price. Austrian Gruner Veltliner is the most expensive at £39. If South Africa simply sold Chenin at the same price as Gruner, they would not make double the profit. They would make 13 times the profit. Or they would only need to sell one container to make the same money as selling 13. Even very small increases in price (or your channel and price mix) have a profound effect to profit.

Number of cases needed to make R1,000,000		**14,815**	**13**	**1,153**
EBITDA	15%	R 67.50	69%	R 867.50
Op EX	30%	R135.00	11%	R 135.00
COGS	55%	R247.50	20%	R 247.50
Ex cellar price - Rand		R450.00		R 1,250.00
Exchange rate	0.052	£23.40	0.052	£65.00
Freight	£1.80	£25.20	£1.80	£66.80
Warehousing	£2.40	£27.60	£2.40	£69.20
Freight out	£3.00	£30.60	£3.00	£72.20
Duty	£26.76	£57.36	£26.76	£98.96
Agent Margin @ 20%	20%	£72.00	20%	£124.00
Wholesaler Margin @ 20%	20%	£90.00	20%	£155.00
Price per bottle		£7.50		£12.92
Restaurant Margin	60%	£18.66	60%	£32.70
Value added tax @ 20%	20%	£3.73	20%	£6.54
List price		£22.39		£39.24

8. Not getting what your region stands for sorted

This is a big one and hard. The average wine consumer is now sophisticated enough that they know what regions are, generally, good for what wine styles. Or at least trade gatekeepers are. All our research confirms that if you are the dominant player, where an important wine idea is concerned (e.g. Provence – Rose, Napa – Cabernet, Germany – Riesling, Argentina - Malbec etc), then over time, you will just get stronger. It's only when something better / more premium exists and a region fails to respond that those regions are threatened (e.g. Marlborough Sauvignon Blanc by Sancerre.)

That means that regions like Stellenbosch, Mudgee, The Great Southern, Hawkes Bay, McLaren Vale etc are greatly underperforming their possibility. You see, these regions face a double jeopardy in that the leading regions for each wine style normally carry the highest price enabling them to reinvest in building that brand. So, those leaders win through both message clarity and out-investment.

McLaren Vale provides an interesting case study. Always playing second fiddle to the Barossa where Australian Shiraz is concerned, at the same time, as a region, they haven't put their stamp on what it is that they do better than anyone else.

The sight of the banners (of what is today the 87 cellar doors and more competing wine businesses) waving at you as you used to drive through the main street of McLaren Vale has clearly played on the minds of producers to the point where today, you see possibly the most diverse set of producers in a confined space that you will see anywhere in the world vis a vis Alpha Box and Dice vs Angoves.

This kind of 'small world' approach where the region behaves as if it is the whole wine world means that there is no cohesive message about what the region is good at. Coupled with that, a determination not to have a system where any sub-region, type of vineyard or wine style gets elevated above any other, means the trade and consumers have no way to rate wines other than by producer (of which there are some world class ones but too much variance to form a clear view).

The key to winning with regional strategy is to take as big a view as possible of your global opportunity, focus on the one thing that you do better than anyone else and then to centre strategy as tightly around you and your fellow producers as a wine region as you can, aligning food, hospitality and accommodation around wine, rather than the other way around. By allowing the South Australian government to run away with strategy, positioning wine within a bigger SA tourism offer and having your local tourism information office promoting attractions outside the region, there is the risk of attracting ever increasing numbers of the wrong customer and sending them elsewhere.

9. Not working hard enough on presentation

Castel Mimi - Moldova

I've just returned from Moldova where I've been helping them with their national competitive strategy. Here is a nation of people who really get the importance of presentation. Even the old State-owned brands have had every aspect of their packaging fussed over. Bottles, paper stocks, embossing, engraving, proprietary bottles – if there is a way to look better, they're all giving it their best. (The wines are good too, just quietly.)

If they can apply themselves as diligently to getting their strategic focus right – promoting interesting blends contain indigenous varietals made with care, quality and innovation, then watch out.

10. Trying to do too much

Keeping it simple is perhaps the easiest advice to give but so often the hardest to follow. I admit that I sometimes struggle with it myself. When you look at the world's most successful wine brands, simplicity is so often at the heart of their success.

I've also recently started working with clients in Bordeaux. The Sichel family (Owners of Chateau Palmer and Chateau d'Angludet) work with just one or two wines per brand. Chateaux Palmer is more of a business project. Chateau d'Angludet is the heart, soul and where the family live. The things you can think about when you have just one or two wines to make…

So, there it is. Hope you enjoyed reading and that it provided a basis for further thought and discussion. It's been our busiest and, for me, most rewarding year yet. The World's Best Vineyards looks like going from strength to strength as a concept, we've got new products coming on stream including a German On-Premise report and we are already getting enquiries about next year's workshop. Hope you have a wonderful Christmas and I look forward to seeing you somewhere in the wonderful world of wine in 2020.

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.

Wine Business Solutions

Phone +612 9744 8332

info@winebusinesssolutions.com.au

http://winebusinesssolutions.com.au