Wine Business Solutions

The Wine Paper 79

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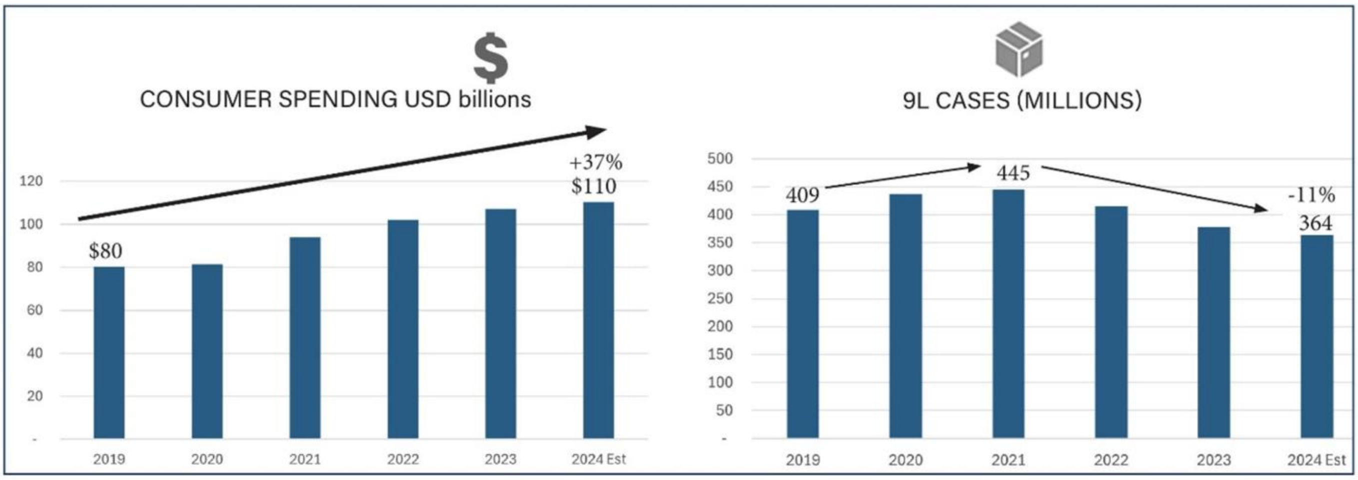
Surfing the Next Wave

Figure 1 – Annual Volume and Value Changes in US Wine Sales - Source, Wine Business Magazine

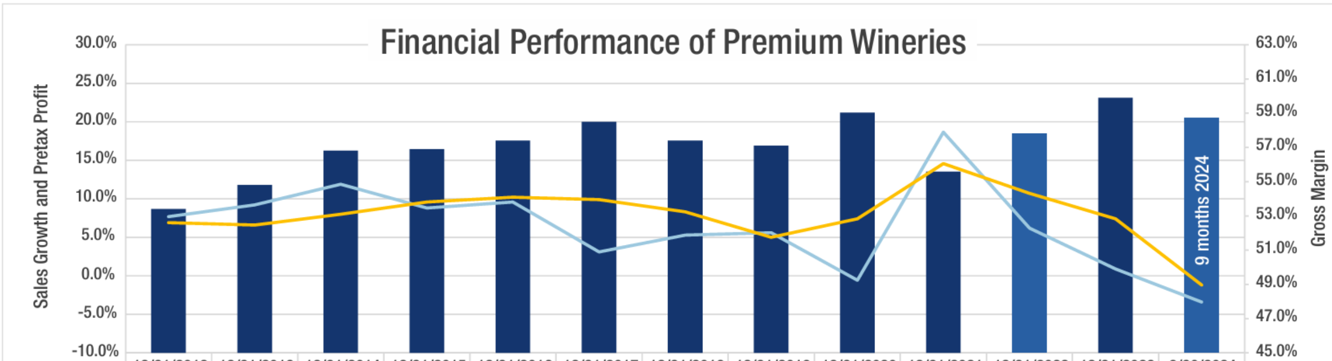


"It's the worst I've seen it in 40 years". That's the common refrain I'm hearing.

According to the OIV, the organisation responsible for global wine statistics, the average bottle of wine cost 24% more at the end of 2023 than it did in 2020. But surely that's OK, isn't it, if we're selling less volume at better prices as in the US market example above?

Regular readers will be familiar with the leverage effect that raising revenue has on profits. The issue, as Paul Holmes à Court, owner of Vasse Felix, pointed out to me at Wine Paris last week, is that costs are rising faster than most brands can recover through price rises. You can see this borne out in US winery data below, albeit that 'margin creep' appears to have been managed reasonably well against the maelstrom of rapidly rising costs and the price rises they necessitate. A 'minus' on the bottom line, however, is never a good thing. A lot of you are hurting right now, I know, and I don't want to make light of this.

Figure 2 – US Winery Profitability. Source, Silicon Valley Bank.



	12/31/2012	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018	12/31/2019	12/31/2020	12/31/2021	12/31/2022	12/31/2023	9/30/2024
Gross Margin	53.4%	54.8%	56.8%	56.9%	57.4%	58.5%	57.4%	57.1%	59.0%	55.6%	57.8%	59.9%	58.7%
Sales Growth	7.7%	9.2%	11.9%	8.8%	9.6%	3.1%	5.3%	5.6%	-0.6%	18.6%	6.2%	0.9%	-3.4%
Pretax Profit	6.9%	6.6%	8.0%	9.6%	10.2%	9.9%	8.3%	5.0%	7.4%	14.6%	10.7%	7.4%	-1.2%

Source: Silicon Valley Bank Peer Group Analysis Database.

Figure 3 – Sales growth for Silicon Valley Bank's Database of Wineries.

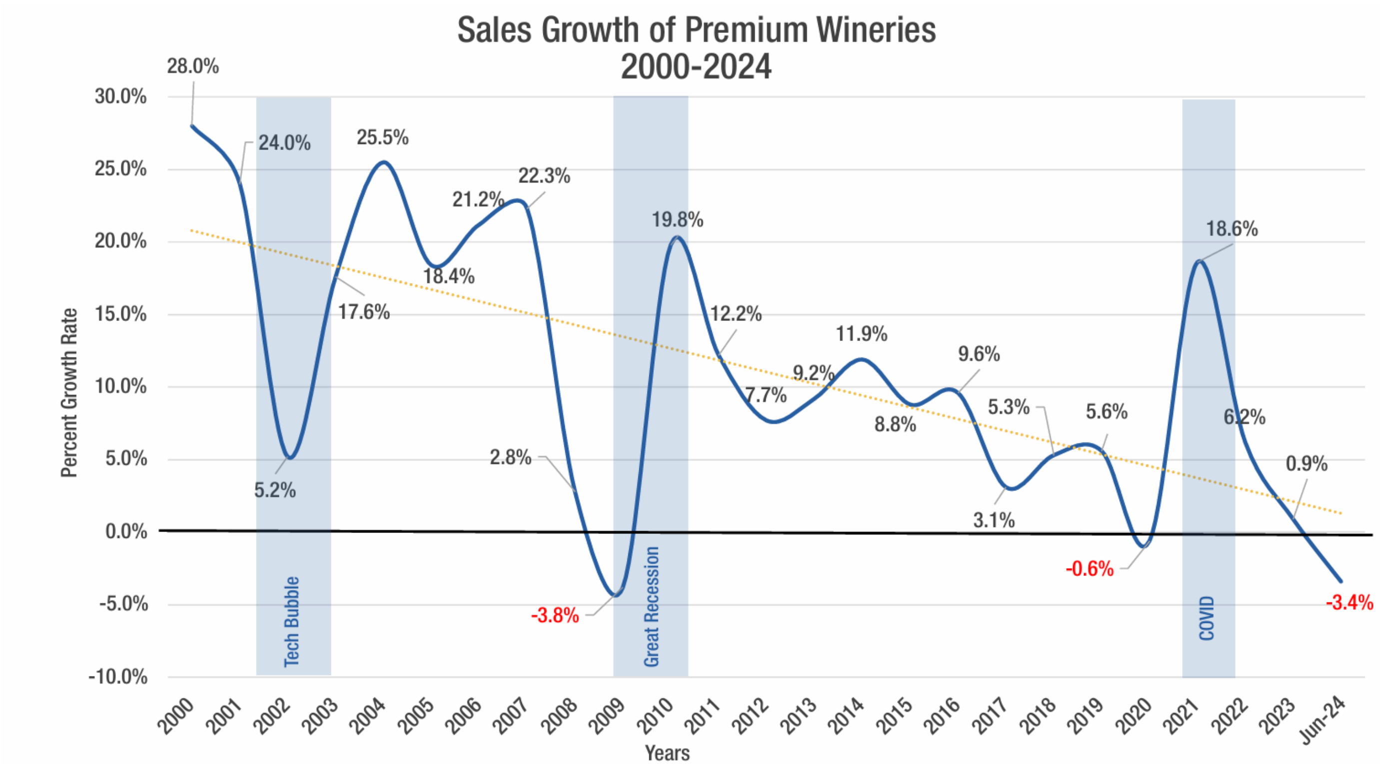
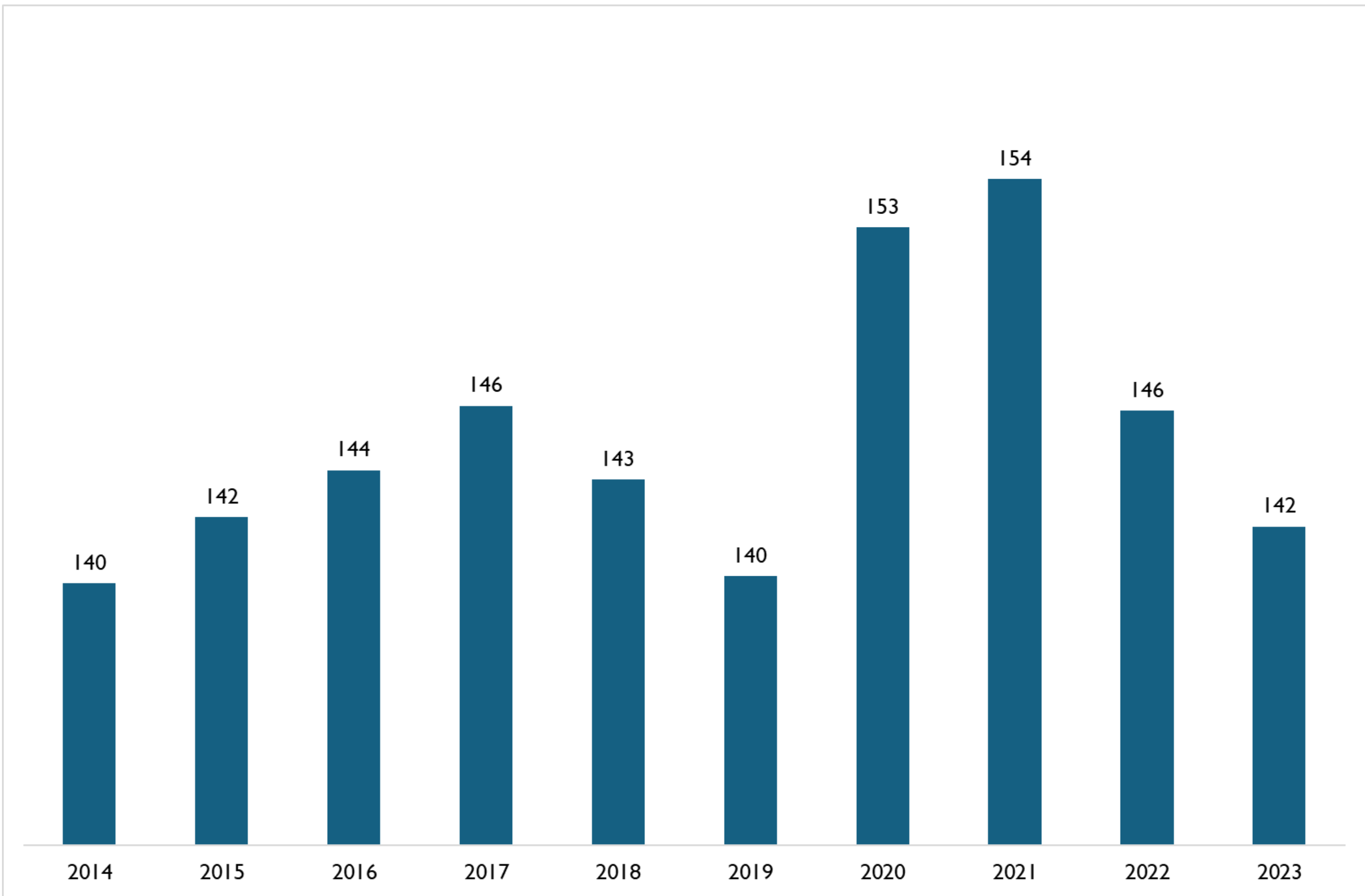
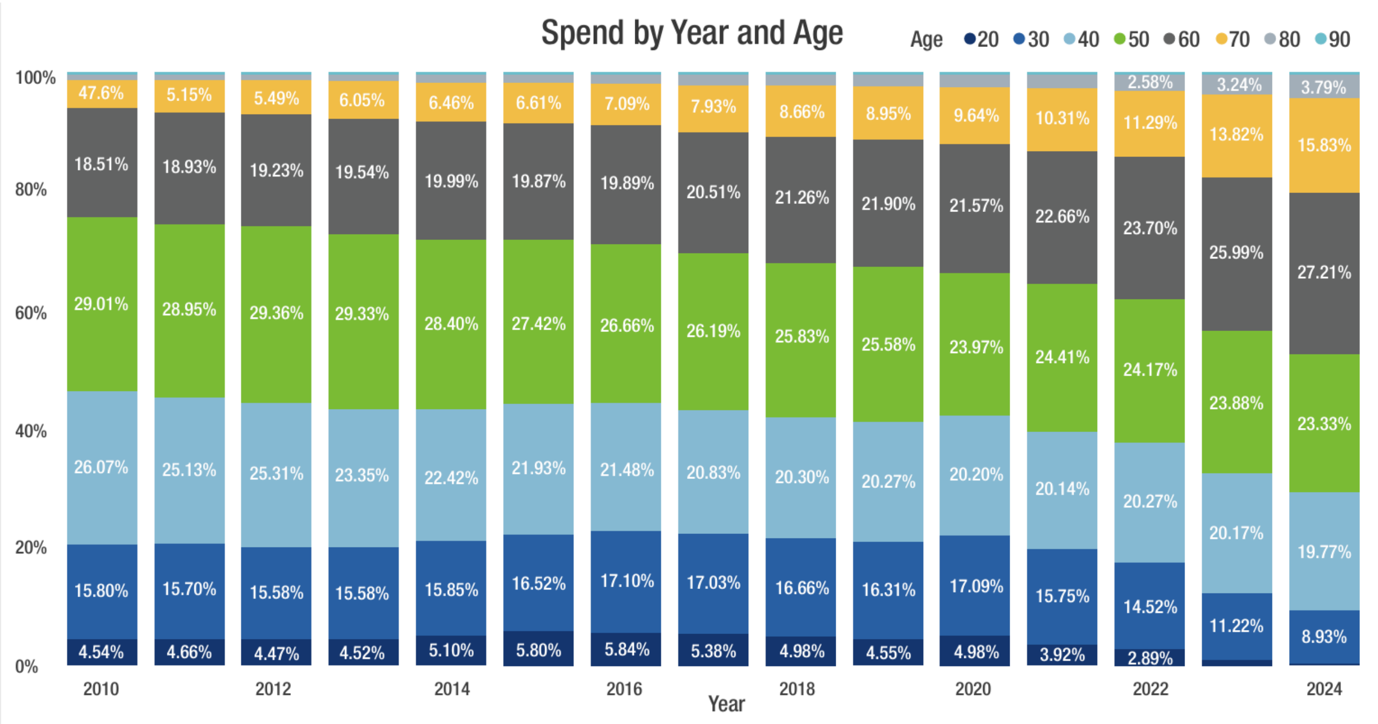


Figure 4 – Total UK Wine Consumption (Millions of 9 litre cases) – Source OIV



When you compare the UK with the US, or any other developed market, you see the same pattern. Slowing sales going into the pandemic, a boom during COVID, and rapid sales deceleration afterwards. The challenge for analysts, of course, is to carve out the effects of supply chain disruption, inventory overshoot adjustment, excise increases and threatened new tariffs from the prevailing consumer trends. Not easy to do.

Figure 5 – Spend by Year and Age – Source SOVOS Ship Compliant



Source: Customer Vineyard, Sovos - ShipCompliant

We would all like to believe that the main causes of the sales slow down are those supply chain, legislative, political and other factors and that after the 'no-low' and 'good for me' trends do their worst, then everything will bounce back to 'normal'. They started making wine in Georgia 8000 years ago, after all.

The chart that makes it most clear, I believe, that this may not be the case, is the one above. To address the question – "Won't these 'Zelennial' people simply adopt wine, in time, like we all did?" - you need to look at spend by age group over time. This shows under 40s being responsible for over 20% of DtC wine expenditure in the US right up to the pandemic and less than half of it today.

You can blame the 'cost of living crisis' and sky-high US tasting fees but Circana's European research across the 6 largest markets for alcoholic beverages says that 71% of the population claim to be drinking, stocking and consuming less. Meanwhile, 23% of people aged between 25-35 claim to have stopped drinking.

If this were true, then the impact on sales would be far greater, of course. What people say they do and what they actually do are always very different. We have always avoided selling research and making recommendations based on people's opinions accordingly. No disrespect to Circana. Understanding people's intentions and measuring their actions are both important in gaining real consumer understanding.

Based, even, on the relatively cursory summation of the situation preceding, I believe that it's best to assume that the market may stay on its current trajectory unless we as, an industry, take control of our destiny and implement significant change.

Unfortunately, there is more that just the sales slow-down and changing consumer tastes to have to work on in such a serious market adjustment as the one currently faced.

1. The anti-alcohol lobby has smelt blood in the water and have redoubled their efforts right at the point at which they know the industry is in the worst position to fight back. I don't think this is an accident. I believe it to be smart politics on their part. The industry should follow the lead of Felicity Carter, Willi Klinger and Liz Thach et al and go just as hard in promoting the case for wine as a unifying, moderating, socially connecting medium that brings people together around a table.

2. Following the example of Jackson Family Wine Estates, a plan needs to be put in place to control the narrative and ensure that we, as an industry, don't talk ourselves into being an unfashionable anachronism. Focus on the joy. Show your customers how to use their senses to better enjoy life.

3. We need to be hypervigilant. The worst things I have ever seen or heard about in the wine industry are happening right now as people get desperate. Good decisions under pressure are the key.

4. We need to prioritise innovation. And we need to be very clear about what that means. I have heard everyone from global research companies to national industry bodies essentially say that if you can't dealcoholise it, flavour it, put it in a can and sell it as a compliment to the burgeoning better-for-you snack food market then we are all, basically, stuffed.

Yes, this is what large companies' so-called innovation programs are all about – incrementalism, line extension and jumping on trends.

To underscore the folly of this, Circana's latest data shows that the No-Low wine category is already mature in the US, that it is dominated by a small group of brands, and that only one of the Top 4, Giesen, is still growing and then modestly (4.9% year on year dollar growth). In other words, it is doing what all categories typically do.

By the time competitors start to pile on, it's already too late, just as it is now for craft beer, craft spirits, gin etc and as it was for the 37 Australian producers who put a kangaroo on their label chasing [yellow tail].

That has never been the way of the most successful winemakers and nor should it be. In their Harvard Business Review article "What the Wine Industry Understands About Connecting with Consumers", Gregory S. Carpenter and Ashlee Humphreys explain that what the wine industry does best is: -

Step 1: Envision something extraordinary. Just like Steve Jobs did with Apple Computers, best to start with a vision of what customers want and create it rather than relying on what your customers tell you.

Step 2: Mobilise those with influence. Meaning wine critics, wine specialist YouTubers, notable sommeliers and others whose opinions are trusted.

Step 3: Let consumers react and share.

And, finally, move from learning to education. Apple has the highest per square metre retail floor space sales realisation on the planet because people go there to be educated and will pay more as a result. There's a lot we can learn from that. There's a better way that we can 'do' education making it fun and desirable.

Now, those of you who are on your toes will have heard all this before but who is practising true disruptive innovation in the wine industry right now when we need it most and what can we learn from that?

The hottest wine brand on earth right now, XXL, does the exact opposite of everything we are told the emergent generation wants. It's flavoured, it's 16% alcohol and it is, well, rocket fuel. It is the fastest-growing brand in Nielsen audited retail in the US, having hit $ 70 million in sales in only months.

Originally sourced out of Moldova (not exactly what, John Barker, Robert Joseph and I recommended when we put together their country strategy), XXL's European Marketing Director tells me that the opening order from Walmart is 80,000 cases. Even at $10 a bottle, Tri Vin will be minting money. You would have to wonder what Gallo's innovation team were doing not to see this one coming.

Is this 'Wine without Manners' any kind of good for the rest of the wine industry? Probably no more than [yellow tail] was. I'm not seeking to judge here, only to point out that if you look around the compass of genuine innovation opportunities for wine, the possibilities are endless.

In creating a product using consumer understanding, insight, and value innovation principals, rather than jumping on the trends that everyone is already talking about, you can make it big.

Let's look at another example. A good friend of mine, Paul Koks, was going to be the European arm of Wine Business Solutions. He already had a consulting business and had worked as a European Sales VP for Constellation and Hardys before that. He had also had a top buying role with a major Dutch retailer.

Unfortunately for me, but good for him, he received a 'better offer' to run Felix Solis's business in Europe. They are the third largest producer in Spain. Their most successful brand right now, with 350,000 cases of sales, is Mucho Mas (much more). It is a red wine with (wait for it, here's that number again) 16 grams per litre of sugar.

Now you might think that that sounds vile but, particularly as you move up into the 'Gold' version, you really have to think about where that sugar is hiding as the acid and tannin balance it out.

The fascism I've faced from the orchestrators of the Australian show judging system in relation to sugar has had an effect on wine producers lasting through to this day. Yes, sugar does not make most wines better and can be used to mask imperfection. That is why it is outlawed in many appellations.

It does have a place for a certain type of consumer and within certain wine styles and Felix Solis has nailed it with their answer to the opportunity.

The other thing I like about Mucho Mas is that it, again, follows the principles of value innovation. They've gone for a very clean packaging style making use of 'negative space' in a way that suggests highest quality in much the same manner that Tim Rands did with his hugely successful Chocolate Block brand.

Wines that have been engineered to have a distinctive flavour profile like The Chocolate Block and Barista (Coffee Pinotage) were a huge trend that has come and gone in South Africa but has rarely been adopted anywhere else. In the SA market, The Chocolate Block and Barista remain after the rest of the category dropped away. The quality elements in the marketing mix sustain the brand.

The point of these examples is not to encourage people to go out and make sweet alcoholic wine that smells like mangos and pineapple. It's about, as mentioned earlier, working your way right around 'the wine compass' and thinking about innovations that your customers might love that they have yet to experience.

So, how can this work at the premium level? Domaine Faiveley has a Mercury appellated wine that sells for more than 40 euros ($80 plus in Australia) called La Framboisière (The Raspberry Patch). Of course, it has the most exquisite raspberry flavours and aromas you could wish for, something I love in Pinot Noir.

Just as in the HBR article, people reacted and shared. It was recommended to me twice, once by a store manager of a Nicolas in Paris and once by a client who is looking to be Faiveley's importer in Georgia. I then dropped it into a lineup to benchmark Pinot Noir for a South African client.

Was this all coincidence? Only a little bit. You create something unique, you turn up the things that make it distinctive, adding maximum value, and the sort of excitement that ensues can make your brand unstoppable. All we need to do now is work out how to do that for the entire wine category, right? The French Paradox, Sideways, what's next? If you would like help with your innovation efforts, do be in touch.

No one can deny that Silicon Valley Bank's annual 'State of the US Wine Industry' report is the world's best wine industry writing. Everyone involved with the wine business anywhere in the world should read it. The only shortcoming I see is that it is compiled using a US 'world view'. And that is completely reasonable. That suits the intended audience. It is already a massive body of work.

But what is being missed as a result? Wherever in the world you look at the research, the results are the same. Whether it be the UK, the US, Circana's 'Big 6' European markets, Australia or even South Africa, the same people are drinking less wine for the same assumed reasons. I say 'assumed' as we can only go on what people tell us. As already discussed, that is not completely reliable. Nor is it the only driver.

With one massive, rarely talked about exception. Australia, Germany and Spain all consume roughly the same amount of wine. Australia, Germany and Spain have very little to do with one another culturally. That amount of wine is exactly double what Americans drink. Imagine if the US consumed a 'normal' amount of wine, for a wine-producing country, and that the world's largest wine market then becomes twice the size.

What are we missing? I believe that marketers and researchers are responsible for a glaring oversight. So much liquor industry research focuses what people are drinking at parties, bars and in social situations. You don't want to lose any of those moments to another drinks category. A lot of the conversation on social media right now centres around what poor value wine now is, compared to craft beer and cocktails. But that is not where wine is consumed. Over 90 per cent of wine is drunk at the shared table either when out for a meal or at home. Winning in the US is all about normalising the moderate consumption of wine with a meal with friends and family. Robert Mondavi knew that. We are still a long way from achieving his dream.

Why must all US depictions of alcohol consumption on screen be about solo self-destruction following loss? If the big tobacco can still engineer product placement in almost every movie, why can't we pay to have our product seen to be consumed in a more enjoyable, responsible and, for the rest of the wine-producing world, 'normal' way, instead of what you do to yourself when your girlfriend / boss / friend dumps you?

How do we bring more people in? What about supporting an outlet to pour a more premium version of your wine? What about creating a moment, say 5-6 pm when your poured wine gets paired with something small that shows the talent of the restaurant, the skill of your winemaker and how good wine and food can be together? What about shifting the entire focus of social media away from grapes, vats and bottles to what fun looks like when enjoying great wine and food with great people? Of course, people are doing that now, but if we all get more focused on the joy wine brings and communicating that, we all win.

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 of 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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