Wine’s globalization: New opportunities, new challenges for Australia

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Symptoms of current challenges in Australia’s wine industry

- **Profits of wineries** have nose-dived
  - => fire sales of some winery and vineyard assets
- **Winegrape prices** fell sharply in 2009, a further 12% in 2010, & another 11% in 2011
- 47% of **exports sold in bulk** in 2010-11, compared with 15% during 1996-2003
- **Import share of domestic wine sales** has risen five-fold, from 3% in 2001 to 15% in 2010-11
  - NZ (68% of vol.), but also from France (13%) and Italy (10%)
- ABARES projects no improvement for next year
- Nor is volatility of weather expected to lessen (CC?)
Three key questions

1. How did the industry get to this situation?
   - From crisis to boom and back to crisis over the past 25 years

2. Has wine globalization reached its limit?
   - Or will new/growing export markets allow Aust. to trade its way back to prosperity?

3. How best to influence Australia’s future place in the wine world?
   - Prospects affected by policy & institutional changes
     • and producer, consumer and researcher responses
1. How did the industry get to the present over-supply situation? … and is this any different from its earlier boom-bust wine cycles?
5 surges in Australian vineyard area, 1850-2004

- Up 6 200 hectares (8 fold increase)
- Up 18 400 hectares (4 fold increase)
- Up 21 000 hectares (doubled)
- Up 15 000 hectares (25% increase)
- Up 110 000 hectares (3 fold increase)
### The latest is Australia’s 5th boom

<table>
<thead>
<tr>
<th>Wine booms in Aust:</th>
<th>No. of boom (flat) years</th>
<th>Vine area growth (%pa)</th>
<th>Wine export growth (%pa)</th>
<th>Share of prodn exported (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1854-71</td>
<td>17(10)</td>
<td>16</td>
<td>14</td>
<td>2</td>
</tr>
<tr>
<td>1881-96</td>
<td>15(19)</td>
<td>10</td>
<td>23</td>
<td>10</td>
</tr>
<tr>
<td>1915-25</td>
<td>10(43)</td>
<td>7</td>
<td>5</td>
<td>9</td>
</tr>
<tr>
<td>1968-75</td>
<td>7(12)</td>
<td>3</td>
<td>-1</td>
<td>3</td>
</tr>
<tr>
<td>1987-04</td>
<td>17(???)</td>
<td>18</td>
<td>22</td>
<td>32 (now&gt;65%)</td>
</tr>
</tbody>
</table>
### Aust. shares of global wine markets (%)

<table>
<thead>
<tr>
<th></th>
<th>1980-84</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vine area harvested</td>
<td>0.7</td>
<td>2.3</td>
</tr>
<tr>
<td>Wine production</td>
<td>1.2</td>
<td>4.4</td>
</tr>
<tr>
<td>Wine consumption</td>
<td>1.1</td>
<td>2.1</td>
</tr>
<tr>
<td>Wine exports</td>
<td>0.2</td>
<td>8.9</td>
</tr>
<tr>
<td><strong>Exports/prod’n</strong></td>
<td><strong>2%</strong></td>
<td><strong>66%</strong></td>
</tr>
</tbody>
</table>
Why such a dramatic boom from late 1980s?

Stars were aligned:

- Change in UK liquor retail laws in 1970s, then rapid UK income growth (Thatcher’s economic reforms)
  => new market for commercial-premium wines

- Devaluation of AUD in mid-1980s, plus flexible production structures, allowed Aust to fill niche in UK
  - New wine cons’m tax also encouraged exports (10% in 1984, raised to 20% in 1986)

Strong industry leadership (plus MIS policy) motivated investors during 1990s, particularly once WFA launched, in 1995, its *Strategy 2025*
Aust av. export price peaked in 2001, down to 269 cents/litre in 2010-11.
% fall in Shiraz grape price, 2008-11

<table>
<thead>
<tr>
<th>Region</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adelaide Hills</td>
<td>-34</td>
</tr>
<tr>
<td>Barossa</td>
<td>-30</td>
</tr>
<tr>
<td>Clare</td>
<td>-34</td>
</tr>
<tr>
<td>Coonawarra</td>
<td>-50</td>
</tr>
<tr>
<td>Langhorne Cr.</td>
<td>-59</td>
</tr>
<tr>
<td>McLaren Vale</td>
<td>-30</td>
</tr>
<tr>
<td>Padthaway</td>
<td>-48</td>
</tr>
<tr>
<td>Riverland</td>
<td>-47</td>
</tr>
</tbody>
</table>
Why the crisis now?

- **Excessive exuberance of investors**, fueled by MIS tax incentives, led to 30-year targets as of 1995 being achieved in \( \frac{1}{4} \text{th} \) of that time
  - Too much product from young vines for marketers to sell
- **Other New World producers** copied Australia
  - grew their exports even faster in 2000s than Aust in 1990s
- **Exchange rate appreciation**, due to mining boom
  - in contrast to, eg, Argentina
- **Fashion swing** against Oz wine abroad
  - and at home, from NZ initially but now also from Old World
- **Long drought**
  - Limited water availability and associated high water prices
Other New World wine exports continue to grow in value (US$m)

- Australia
- Chile
- USA
- South Africa
- New Zealand
- Argentina
- Canada

Year: 1995-2010
Other adverse factors affecting all countries’ vigneron

- Policy-induced **chronic oversupply in Europe** as demand shrinks in traditional producer countries
- **Supermarket revolution**: increasing concentration in many countries, beginning (& most intense) in UK
- **Climate change**: effects differ across regions & winegrape varieties
- **Environmental concerns** of European consumers
  - ‘buy local’, ‘buy organic/biodynamic’
- Alcohol consumption **regulations and taxes** under pressure from health lobbies
**Old and New World’s wine exports as % of production volume**

<table>
<thead>
<tr>
<th></th>
<th>1980-84</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Old World</td>
<td>5</td>
<td>18</td>
</tr>
<tr>
<td>New World</td>
<td>6</td>
<td>23</td>
</tr>
<tr>
<td>Rest of world</td>
<td>11</td>
<td>13</td>
</tr>
<tr>
<td><strong>TOTAL WORLD</strong></td>
<td><strong>14</strong></td>
<td><strong>34</strong></td>
</tr>
</tbody>
</table>
2. Has wine globalization reached its limit?

… or can Australia expect to trade its way back to prosperity by growing non-traditional export markets?
New World (esp. ANZ) now very dependent on exports
(share of prod’n volume exported, %, 2007-09)
... but globaliz’n still has a long way to go

... given the wide divergence still of wine expenditure as % of income, because of

- current taste differences, but also
- consumption tax differences
  - Some may be cut, but might others increase?
New wine globaliz’n opportunities

- Rapid Asian demand growth, dominated by China
  - China now exceeds Russia in wine cons’n volume, and is several times that of Japan
  - India’s cons’n and prod’n are only 1% of China’s
China dominates wine consumption in Asia (ML)
Total wine cons’n vol. (ML, 2009)
Wine cons’n value in 2009
(wholesale pre-tax, US$m)
New opportunities (continued) …

While China’s domestic wine production also is growing, its wine self-sufficiency is falling

fell from 93% to 85% during 2000s

- China is still dependent on imported bulk wine for blending
China’s wine prod’n & cons’m (ML)
China & New World wine prod’n (ML)
New opportunities (continued) …

In terms of the average price of bottled still wine imports, 5 of top 10 countries globally are Asian.
Price of still bottled wine imports, 2009: Asia dominates (US$/litre)
### Aust wine exports to East Asia, 12 months to 03/11

<table>
<thead>
<tr>
<th>Country</th>
<th>Share (%) of Australian export value (terrorism)</th>
<th>Unit value of exports (A$ / litre)</th>
<th>% change in value of exports, 2005-06 to 2008-09</th>
</tr>
</thead>
<tbody>
<tr>
<td>China (mainland)</td>
<td>8.5 (4th)</td>
<td>3.14</td>
<td>350</td>
</tr>
<tr>
<td></td>
<td>(bottles 5.28)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hong Kong</td>
<td>2.4 (7th)</td>
<td>7.94</td>
<td>72</td>
</tr>
<tr>
<td>Japan</td>
<td>2.0 (9th)</td>
<td>4.66</td>
<td>20</td>
</tr>
<tr>
<td>Singapore</td>
<td>2.0 (10th)</td>
<td>7.82</td>
<td>13</td>
</tr>
<tr>
<td>Malaysia</td>
<td>1.2 (14th)</td>
<td>9.34</td>
<td>9</td>
</tr>
<tr>
<td><strong>All five E. Asians</strong></td>
<td><strong>16.4</strong></td>
<td><strong>4.22</strong></td>
<td><strong>72</strong></td>
</tr>
<tr>
<td><strong>Five key markets</strong></td>
<td><strong>66.9</strong></td>
<td><strong>2.37</strong></td>
<td><strong>-20</strong></td>
</tr>
<tr>
<td>(UK, US, Ca, Ger, NZ)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Prospects for Australian (& other) wine exporters in emerging Asia

Asian markets promise to grow steadily (albeit from a low base) because:

- Incomes are rising rapidly, as is adult middle-class population
- Wine from grapes currently accounts for just 3% of volume of Asia’s recorded alcohol consumption (4% in China), compared with 16% globally
- Domestic grape production is growing slower than consumption, esp. for premium wines
- Joint venture options in China (and India) offer prospects to influence tastes
  - especially as China is also investing in vineyard/winery assets in Aust (but also France, ...)


## Emerging Asia’s shares of the global economy: 2004 and 2030

<table>
<thead>
<tr>
<th></th>
<th>GDP share (%)</th>
<th>GDP per capita (rel. to world=1)</th>
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<tbody>
<tr>
<td></td>
<td>2004</td>
<td>2030</td>
</tr>
<tr>
<td>High-income countries</td>
<td>80</td>
<td>65</td>
</tr>
<tr>
<td>Developing Asia</td>
<td>11</td>
<td>22</td>
</tr>
<tr>
<td></td>
<td>Volume, ML (&amp; share, %)</td>
<td>Value, US$m (&amp; share, %)</td>
</tr>
<tr>
<td>------------------</td>
<td>-------------------------</td>
<td>--------------------------</td>
</tr>
<tr>
<td>France</td>
<td>48 (24)</td>
<td>306 (38)</td>
</tr>
<tr>
<td>Australia</td>
<td>44 (22)</td>
<td>102 (19)</td>
</tr>
<tr>
<td>Chile</td>
<td>56 (28)</td>
<td>54 (10)</td>
</tr>
<tr>
<td>United States</td>
<td>12 (6)</td>
<td>35 (7)</td>
</tr>
<tr>
<td>Italy</td>
<td>8 (4)</td>
<td>27 (5)</td>
</tr>
<tr>
<td>South Africa</td>
<td>8 (4)</td>
<td>7 (1)</td>
</tr>
<tr>
<td>All exporters</td>
<td>202 (100)</td>
<td>538 (100)</td>
</tr>
</tbody>
</table>
Take-away lessons from history

- Australia led the New World in its contribution to wine market globalization
  - But it expanded too quickly, and was unlucky to be hit by AUD currency appreciation and GFC – *just when exports needed to grow most*
- It now **needs to structurally adjust to new realities**, incl. to export growth prospects in new markets in Asia -- but mainly super-premium (if China’s production growth is non-premium)?
  - and in strong competition with France and others
3. How best to influence Australia’s future place in the wine world
-- roles for tax reform, R&D, ...
Adjustments to production in Aust.

Savvy firms are moving more toward finer wines in cooler parts of Australia, in response to:

- increased competition from lower-cost producers in Sthn Hemisphere, China and Sthn & Eastern Europe
- higher costs for Australian irrigators, especially with global warming and higher-priced/less-reliable water
- prospect of wine consumer tax switching from *ad valorem* to volumetric
  - which will accelerate the upgrading of Aust consumer tastes

Is that where profitability will be highest?

bearing in mind growth of supermarket brands and of China market?
Adjust Aust. wine institutions?

- Combine GWRDC and Wine Australia?
  - Could then better invest combined levies in highest-payoff areas (whether R,D&E or generic promotion)?

- Raise levies?
  - Very high payoff from past grape & wine R,D&E
  - R,D&E needed even more now, with climate change, variable water prices/availability, increasing consumer interest in sustainable practices, & stiffer competition from rest of world
  - Expanded generic promotion needed (esp. in Asia), to position Australia as a producer also of fine wines of place?
    - Aust in 2011-12 to spend A$8.9m (0.7 cents/litre, 0.2% of VOP), compared with Bordeaux’s A$23.3m (3.3 cents/litre)
    - 1/3rd of China’s upper-middle-class drinkers of imported wine do not know Australia produces wine!

- Will need to deal more constructively with tension between high-quality and lower-quality producers
Thanks!

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