

Australia's evolving role in the world's wine markets

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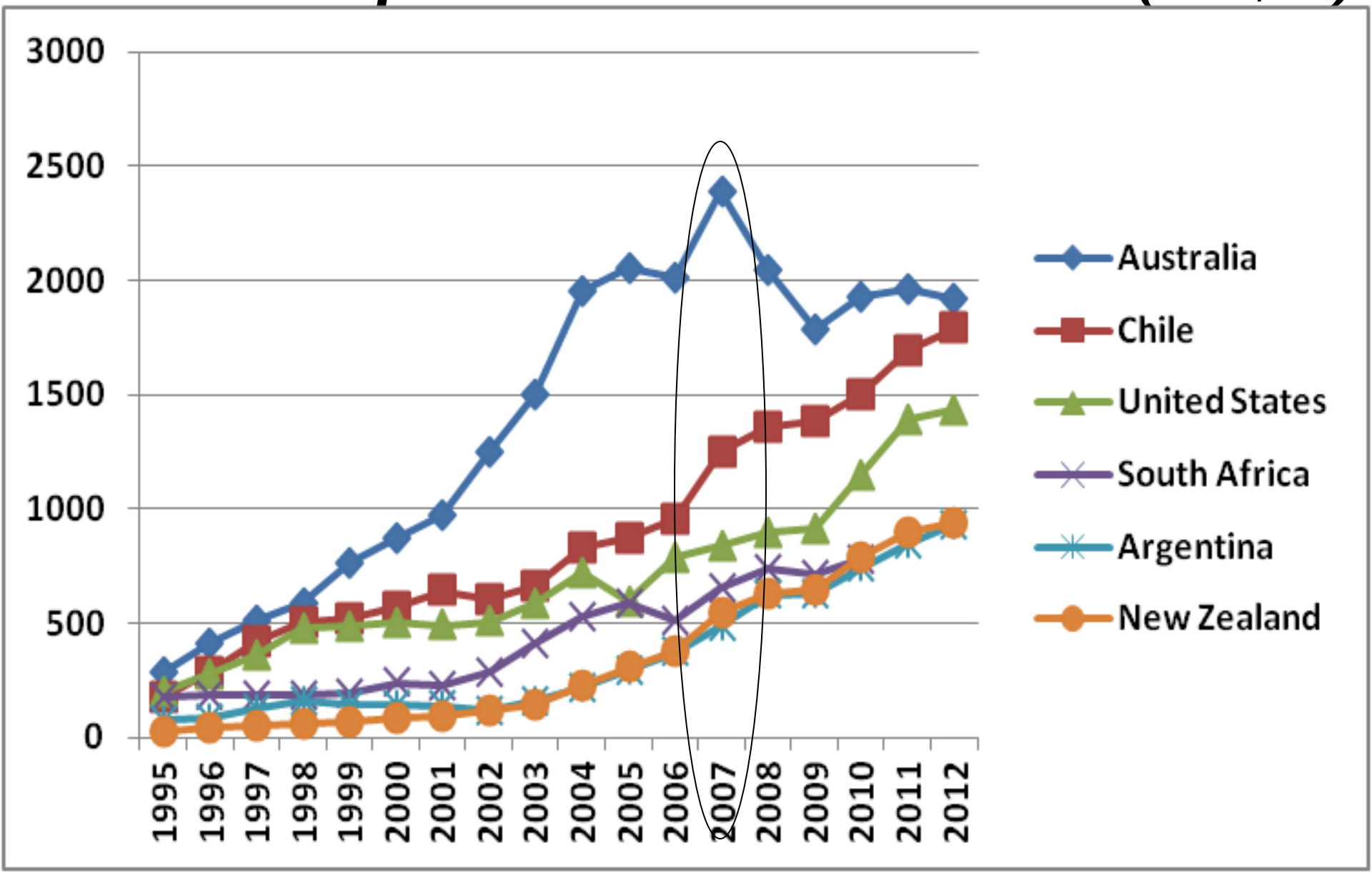
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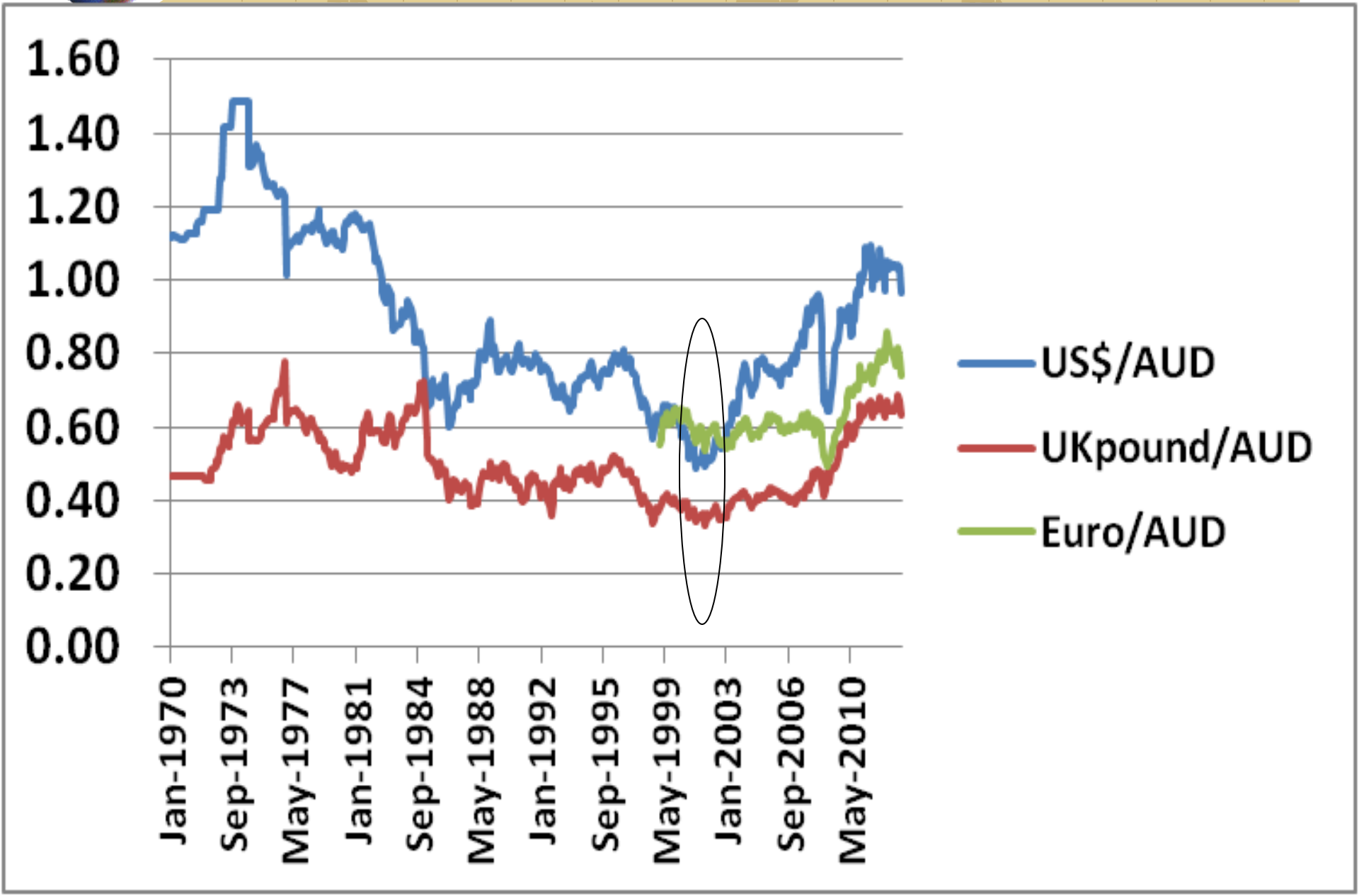
Symptoms of current challenges in Australia's wine industry

- **Profits of wineries and growers:** low/negative
- **Winegrape prices:** still low, esp. compared with Calif.
- **>50% of exports sold in bulk:** less processing here
- **Import share of domestic wine sales:** risen 5-fold, from 3% in 2001 to >15%
  - NZ (2/3^{rds} of vol.), but also from France and Italy

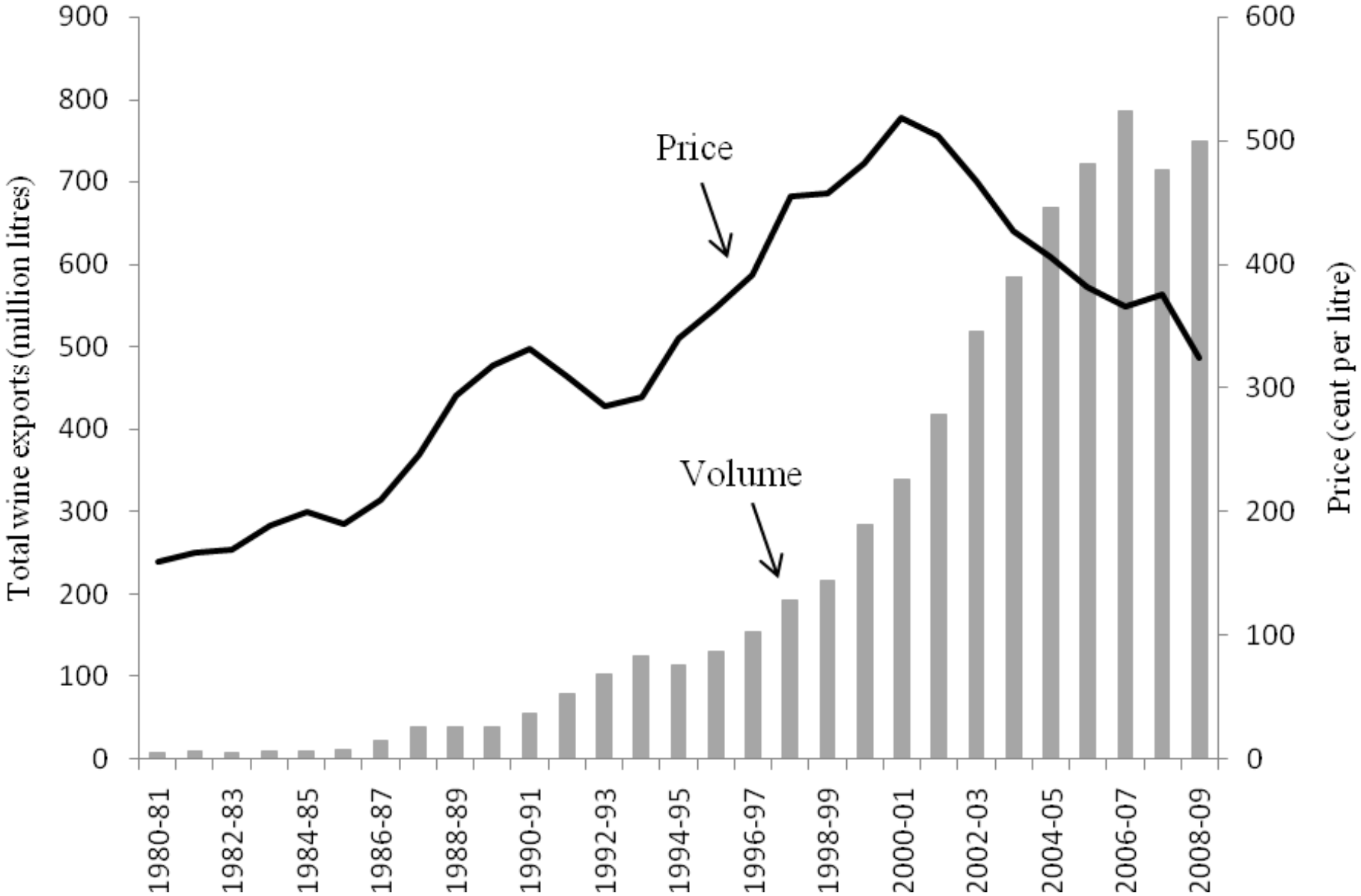
Gap between Aust & smaller New World wine exporters: halved since 2007 (US$m)



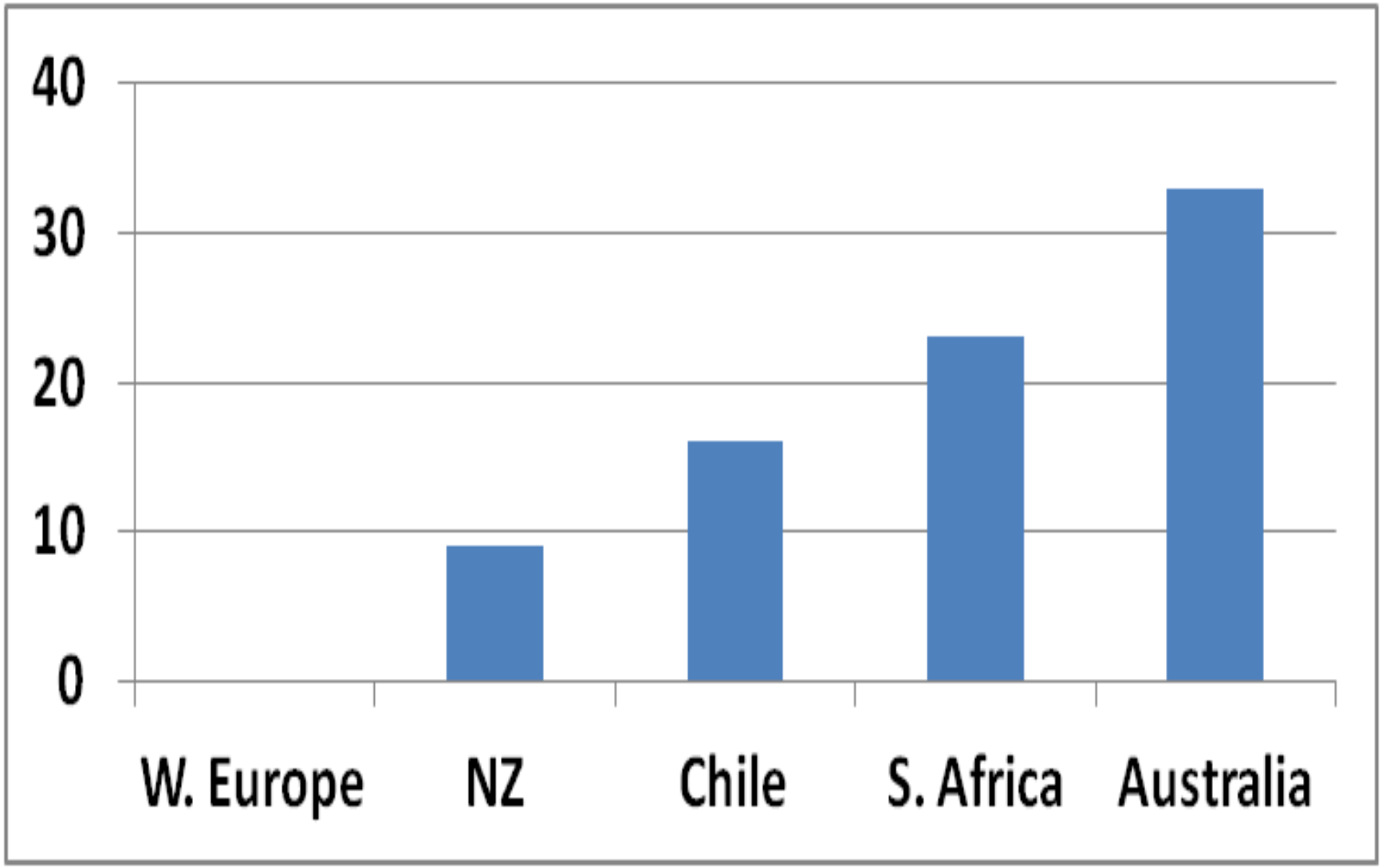
Nominal value of AUD, 01/70-05/13



Aust av. export price peaked in 2001



Real *exchange rate changes, 2007-2011*
(% currency appreciation relative to US$)
Wine exporters



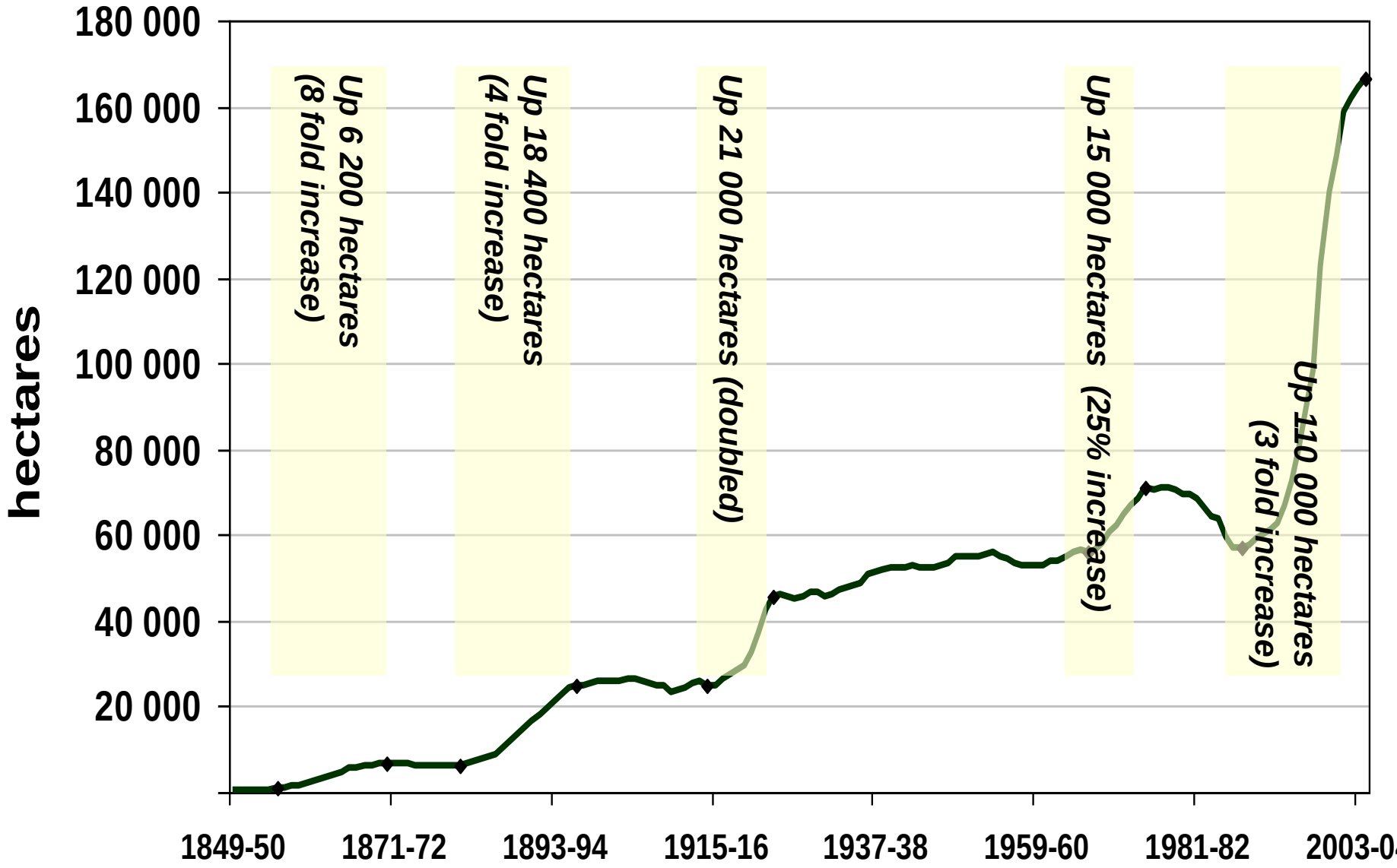
% changes in RERs and model-estimated impact on grape & wine prices, wine exporters, *2007-11*

	RER (real exchange rate)	Real local-currency producer price of:			
		Grapes	*Non-premium wine*	*Comm. premium wine*	*Super premium wine*
W. Europe	0	5	6	7	5
US	0	4	8	8	3
Chile	16	-12	-12	-11	-13
Australia	33	-32	-31	-30	-26

Key questions

- 1. In addition to strong AUD, why else did the industry get to this situation?
  - From crisis to boom and back to crisis over the past 25 years
    - Is this any different from earlier boom-bust wine cycles?
- 2. What is Australia's likely future place in the world of wine?
  - Prospects over the next 5 years

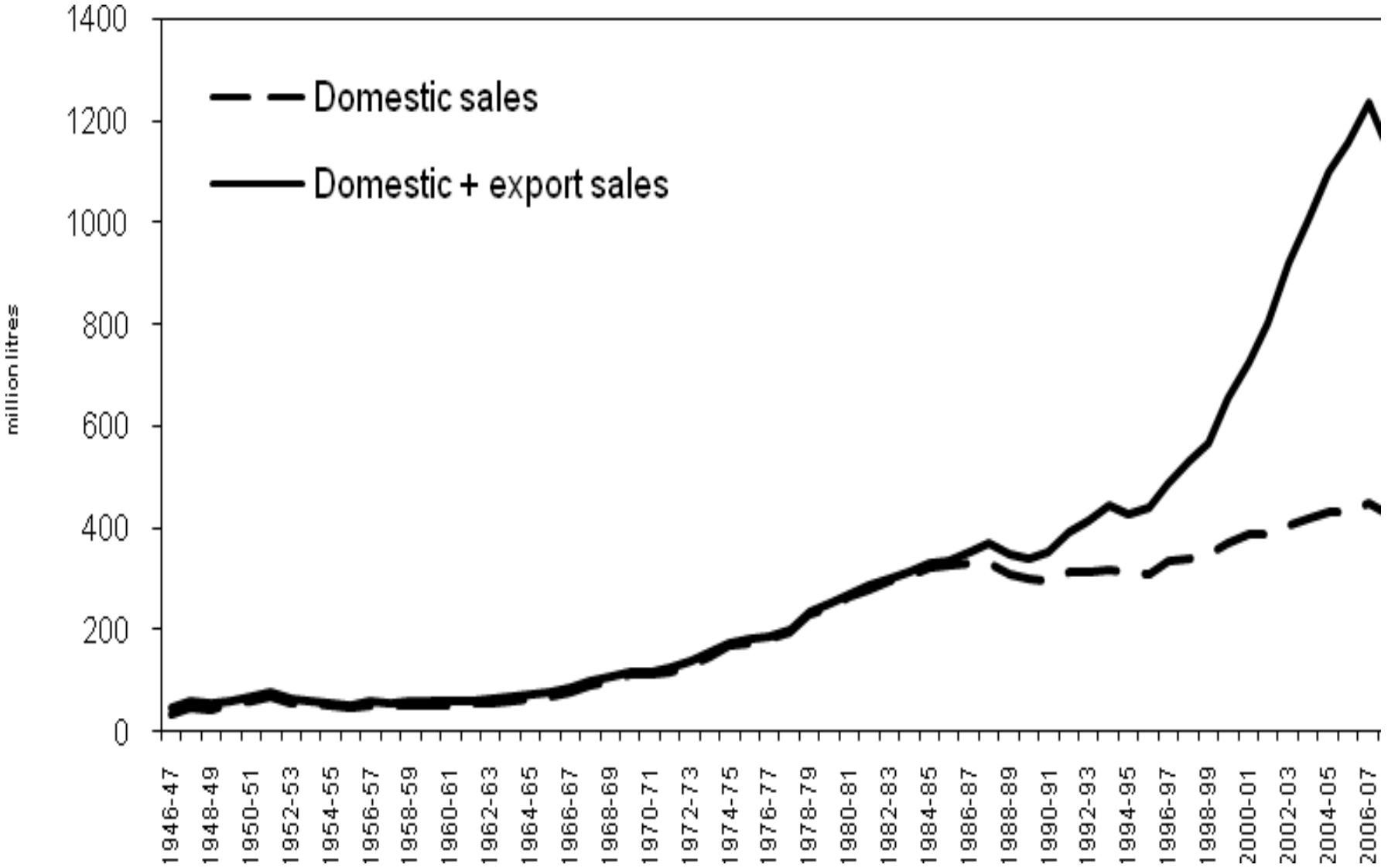
Surges in Australian vineyard area, 1850-2004



The latest is Australia's 5th boom

Wine booms in Aust:	No. of boom (flat) years	Vine area growth (%pa)	Wine export growth (%pa)	Share of prodn exported (%)
1854-71	17(10)	16	14	2
1881-96	15(19)	10	23	10
1915-25	10(43)	7	5	9
1968-75	7(12)	3	-1	3
1987-04	17(??)	18	22	32 (now>65%)

Domestic and export sales of Aust wine, 1947 to 2007



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 econ. reforms)

  => new market for **commercial-premium wines**
  - **Devaluation of AUD** in mid-1980s, plus flexible production structures, allowed Aust to fill niche
    - Labor's new 20% wine cons'm tax also encouraged exports
- Strong industry leadership motivated investors during 1990s, particularly once WFA launched, in 1995, its ***Strategy 2025***

Why the crisis now?

- **Excessive exuberance of investors**, fueled by tax incentives, led to 30-year targets as of 1995 being achieved in ¼th of that time
  - Too much fruit from young vines for marketers to sell
- **Other New World producers** copied Australia
  - grew their exports even faster in 2000s than Aust in 1990s
- **Old World also exported much more**
- **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 Italy and France
- **Drought: led to higher pricing of water**

Globalization: Old and New World's wine exports as % of prod'n volume

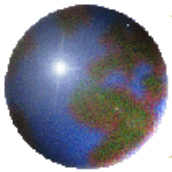
	1980-84	2009
Old World 5	18	37
New World 6	2	23
Rest of world	11	13
TOTAL WORLD	**14**	**34**

... plus several factors affecting all countries' vingerons

- Policy-induced **chronic oversupply in Europe**
  - esp. non-premium winegrapes (but eased last vintage)
- **Climate change**
  - effects differ across regions & winegrape varieties
- **Supermarket revolution**
  - increasing concentration in many countries
- **Environmental concerns** of European consumers
  - 'buy local', 'buy organic/biodynamic',
- Alcohol consumption **regulations and taxes**
  - under pressure from health lobbies

Consequences of concentration of wineries and retail outlets

- Biggest wineries have best chance to match the increasing buying power of supermarkets
- Commercial-premium branded wine (either winery's or supermarket's brand) is gradually replacing non-premium wine globally …
  - … with location of grape production becoming less relevant than consistent style and value for money
  - Hence region and even country of grape origin may become less important for commercial-premium wines
    - and growers of lesser-quality grapes will face increasing int'l competition as suppliers to large multinational wineries
- So small and medium firms will increasingly have to focus on unique super-premium grapes/wines



2. What is Australia's likely future place in the world of wine?

Some encouraging developments

- AUD is devaluing, and is forecast to fall more

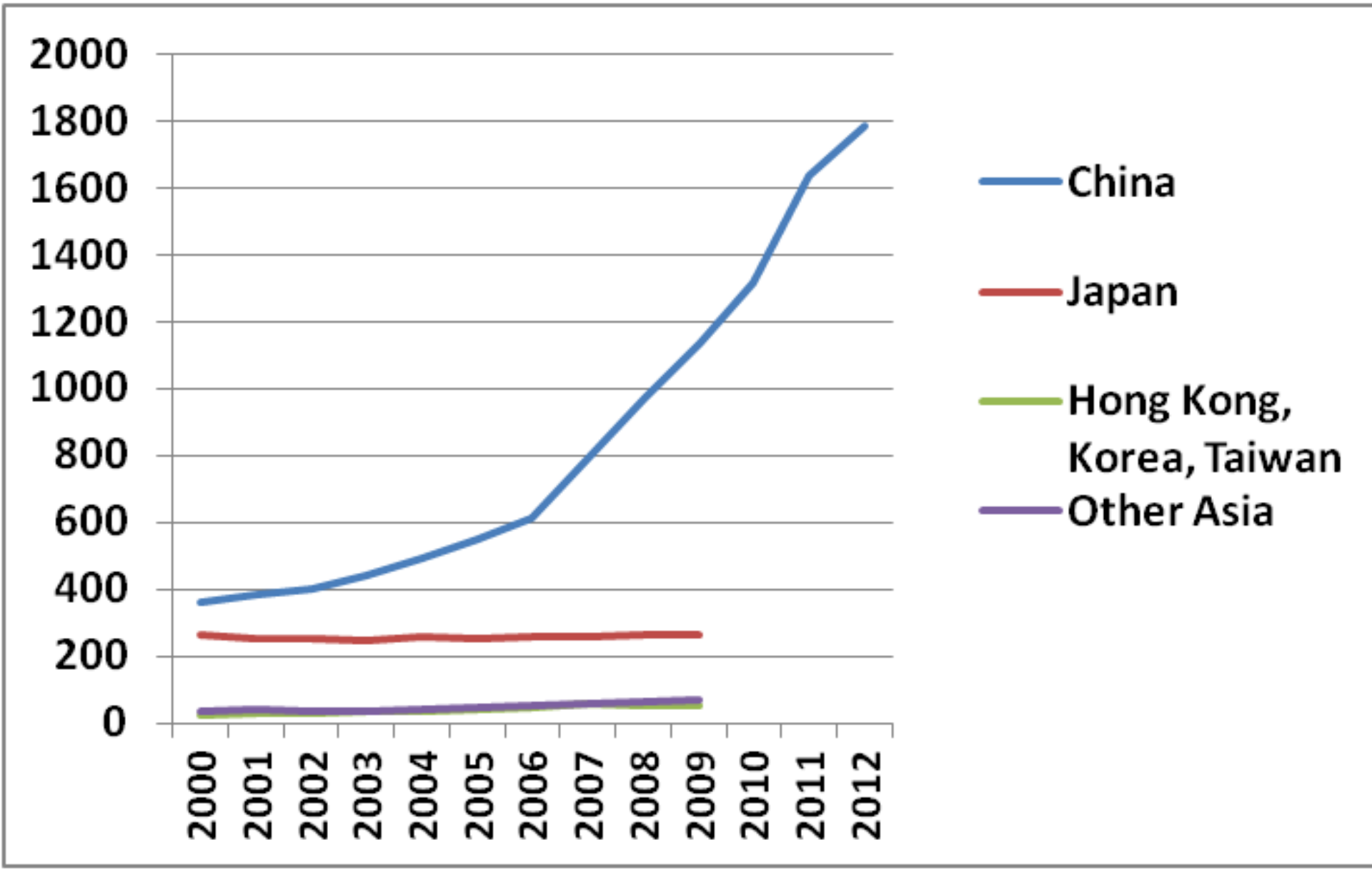
Nominal US$/AUD, 10/12 to 05/13



Some encouraging developments

- AUD is devaluing, and is forecast to fall more
- China's net imports are rising rapidly, and forecast to continue

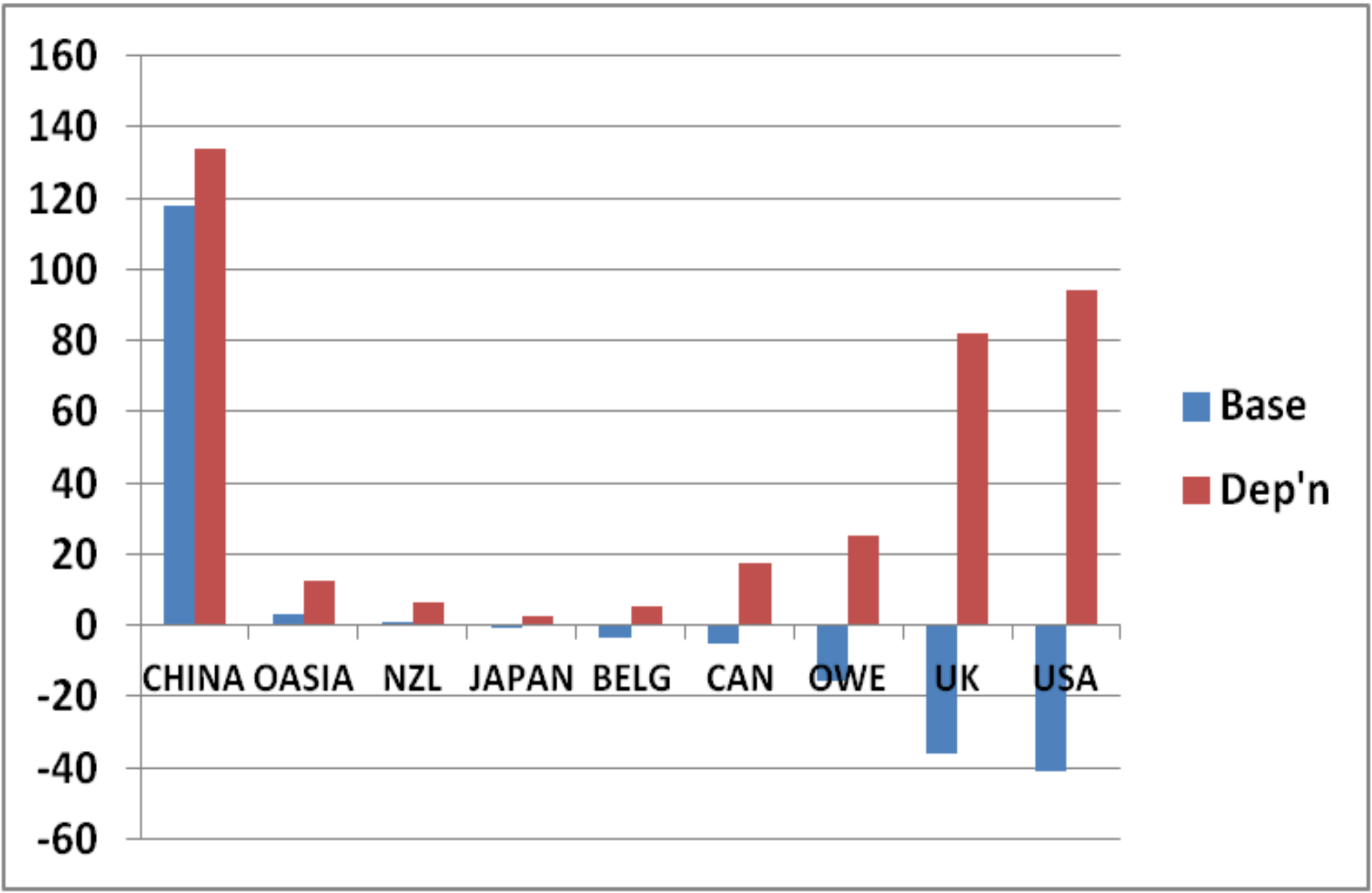
China dominates Asian wine cons'm (ML)



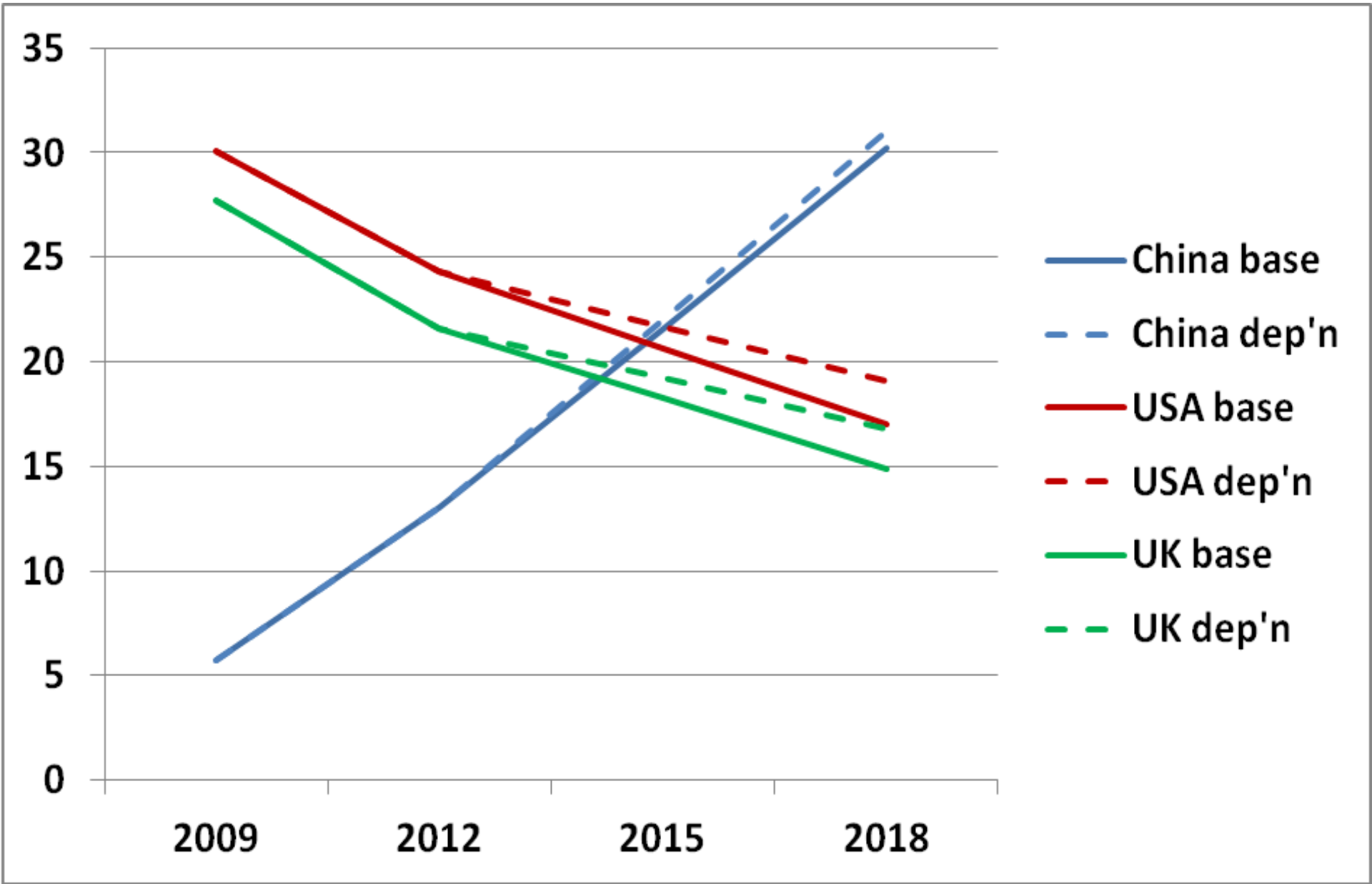
Some encouraging developments

- AUD is devaluing, and is forecast to fall more
- China's net imports are rising rapidly, and forecast to continue
- **Model results:** Without any currency changes, Aust export volume won't grow much
  - but China will replace US and UK as major market
- But if exchange rates return half-way to 2009, Aust export volume could rise by 50%
  - and China will still replace US & UK as major market

Change in Aust exports (ML), 2011-18



Shares of value of Australian wine exports (%)



Adjustments already under way in marketing Australian wine

- Aust already has **6 of the world's top 15 most-recognized still wine labels** (Intangible Business 2010), some of which are adding a regional reserve range
  - Higher quality, more-differentiated wines of place, including by large wineries
- Greater emphasis being given to environmental stewardship at all stages along value chain
- Wine Australia: Brand Champions, Regional Heroes; and its website allowing fine wine producers to tell their story
  - www.australiaplus.com
- First Families of Wine
  - www.australiasfirstfamiliesofwine.com.au

Most-recognized still wine brands globally

1. *Gallo*
2. *Concha y Tora*
3. *Mondavi*
4. **Yellowtail**
5. **Hardys**
7. **Jacob's Creek**
9. **Lindemans**
13. **Wolf Blass**
15. **Penfolds**

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 Southern Hemisphere and Southern Europe
  - higher costs for Australian irrigators, especially with global warming and higher-priced/less-reliable water
  - prospect of wine consumer tax switching from an *ad valorem* to a volumetric basis
- But is that where profitability will be highest?
  - bearing in mind growth of supermarket brands and of China market?

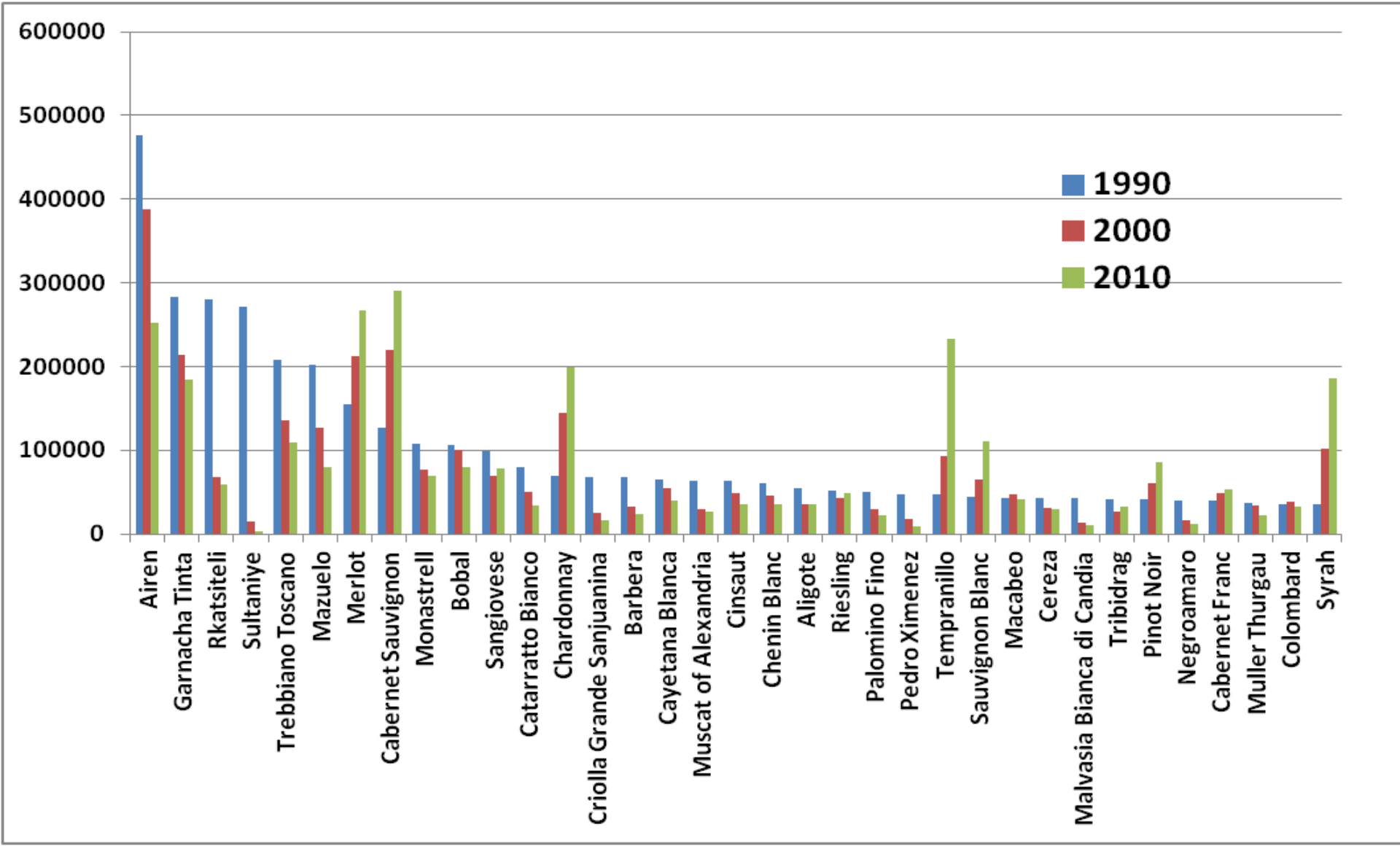
More needs to be invested in R&D

- Benefits could be huge (yet unwillingness to pay?)
  - Very high payoff from past grape & wine R&D
  - Needed even more now, with climate change, variable water prices/availability, increasing buyer interest in sustainable practices, and stiffer competition from rest of world
  - Include more collaboration internationally? (2-way spillovers)
- Australia's output of research papers per litre of wine produced has slipped over past 2 decades, relative to other key producing countries

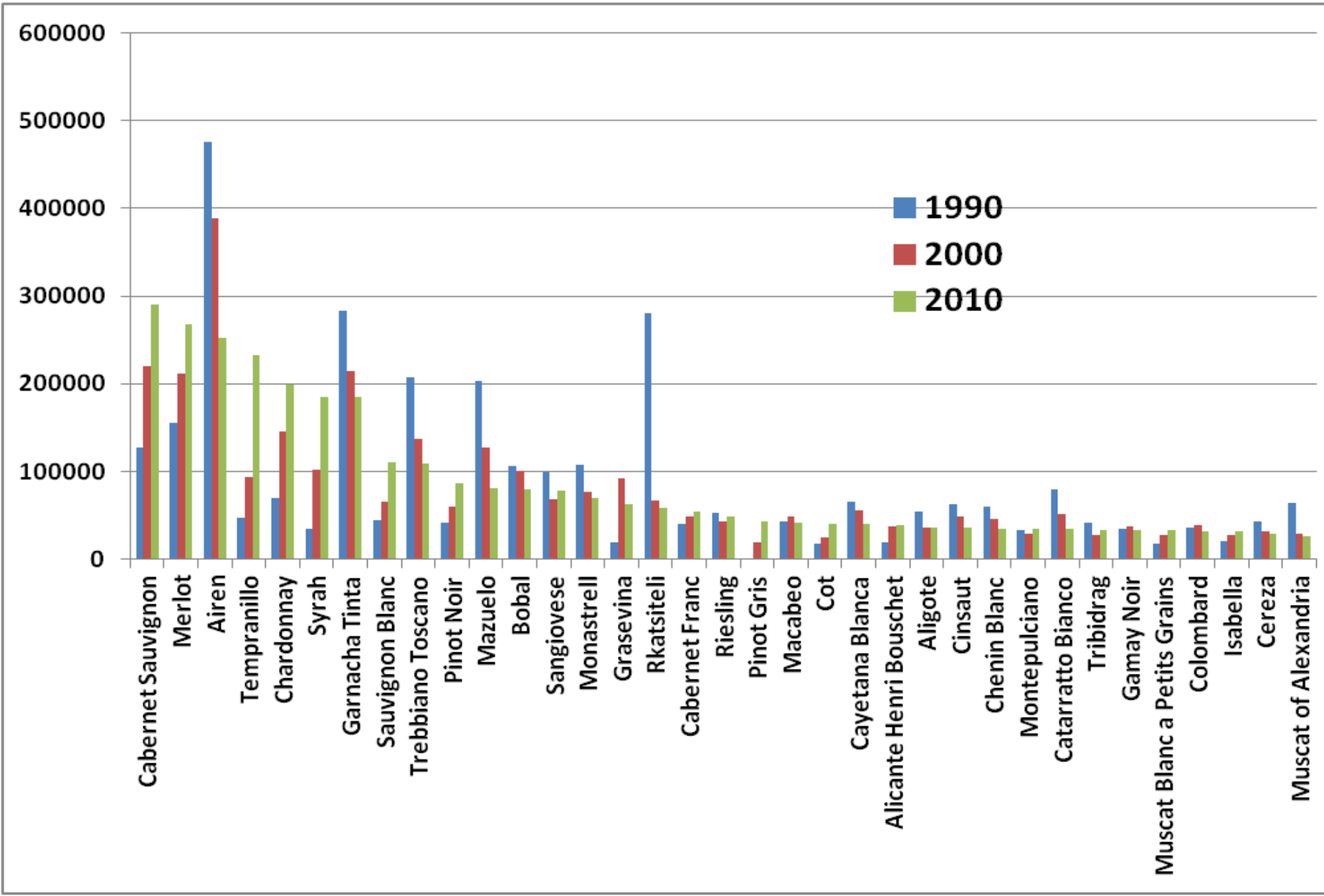
Take-home messages

- Boom/bust/slow-recovery cycles are normal for the wine industry
  - But this one involved a more sudden and severe downturn than expected due to GFC, drought, strong A$, stronger competition
- Vine-grubbing in Aust and EU is easing the over-supply, as will growth in Asian wine imports
- Climate change requires altering varietal mix and/or moving to higher latitudes and altitudes
- If we switch to volumetric tax, expect quality upgrading
  - but climate change & tax change will hurt irrigated areas most, as is growing competition from lower-cost exporting countries
- Foreign investment could put a floor on asset values
- More investment in innovation vital (R&D + promotion)
- "Only first 200 years are tough", so we'll be OK by 2050

Global winegrape areas (ha., top 35 in 1990)



Global winegrape areas (ha., top 35 in 2010)



Thanks!

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- www.adelaide.edu.au/wine-econ
- www.adelaide.edu.au/press/titles/global-wine