

**An Analysis of Globalization Forces in the Wine Industry:
Implications and Recommendations for Wineries**

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ABSTRACT. This paper examines the driving forces and key success factors related to the increasing globalization of the wine industry. It further analyzes the current competitive advantage positions of four Old and five New World wine producing countries. The group with the strongest sources of competitive advantage position includes the United States, Australia, and Chile. The group of countries with moderate competitive advantages includes Italy, Spain, Argentina and South Africa, and the countries with the weakest competitive advantages in the global wine industry are two traditional strongholds of wine production from the Old World: France and Germany. This competitive advantage scenario should be a wake-up call to many countries. The study offers three specific recommendations for wineries of all sizes in all nations. They are: i) increased emphasis on market orientation, ii) increased export assistance, iii) managing trade barriers effectively.

KEYWORDS. Competitive advantage, globalization, market orientation, wine marketing

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I. INTRODUCTION

Globalization, by definition, is not a new phenomenon for the wine industry as regional wine producing and consuming countries have been trading for thousands of years. However, until the early 1990's the production and consumption of wine was relatively localized. Wine producers in distant countries were traditionally isolated from each other, and most of the world's wine drinkers consumed either local wines or imports from nearby producers, such as the United Kingdom's historical penchant for French wine. As winemakers had minimal cross-border interaction, they followed local traditions.

However, competitive positions and consumption patterns in Old and New World countries have changed radically and rapidly in recent years. For example, global wine exports as share of global production have increased from 15% to 25% percent over the 1990s (Anderson et al, 2001). Decreasing tariffs, logistical cost reductions and the lowering of certain trade barriers have afforded wine producers the opportunity to sell their products outside of their own region. This new international access is reshaping how wines are produced and consumed alike, and those countries best able to adapt to this wider and more competitive playing field will gain significant national competitive advantage.

Moreover, there has been a significant increase in export orientation by both New and Old World producing countries. In 2001 five New World countries, Australia, Canada, Chile, New Zealand, and the US, joined forces to "diminish barriers by reducing regulatory burdens faced by winemakers" by signing the Mutual Acceptance Agreement on Oenological Practices (Wine Institute, 2004). In response to increased competition from the New World, many Old World countries have expanded their target markets to Asian

countries such as China and India (Business News Onlypunjab.com, 2005).

Finally, increased global trade in the past 20 years has resulted in shifts in wine consumption patterns. For example, although China ranks as only the 24th largest importer of US wine, “few countries can boast the long-term potential that this largely undeveloped market represents” (AgExporter, 2004). Moreover, Dewald (2003) reports an emerging pattern in Hong Kong from consuming Chinese tea and brandy to drinking red wine. Chinese and Indian consumers have shown increased demand for foreign wines (Wine Institute, 2004). China’s emerging middle class, enriched and open to purchasing non-traditional products, could provide significant new opportunities for wineries worldwide.

The purposes of this paper are to i) examine driving forces and key success factors related to the increasing globalization of the wine industry, ii) analyze the competitive advantage positions of four Old and five New World wine producing countries, and iii) offer a few recommendations for global wineries to sustain competitive advantage in the long run. First, each country will be profiled using key industry data and analyzed regarding their national capabilities to address five qualitative success factors contributing to their competitive advantage positions.

II. PROFILES OF SELECTED COUNTRIES

To better understand the major national players in the wine industry this section profiles nine large wine producing countries based upon key trade data. The Old World countries, defined as those within Europe, have a long, uninterrupted history of wine production and consumption. The four largest European producers, France, Italy, Spain, and Germany, accounted for almost 55% of global production and 40% of consumption in 2004, the most recent year for which complete data are available (Table 1).

New World countries are defined as those outside Europe. Five of the largest and most established New World producers are the United States, Argentina, Australia, South Africa, and Chile. These five countries

comprised 23% of global production and 21% of consumption in 2004. Thus, the four Old World and five New World countries accounted for 78% of the world's production and 61% of wine consumption in 2004 and are profiled below.

TABLE 1
Wine Production and Consumption by Country, 2004

| | | 2004 Production | | 2004 Consumption | | |
|---------------------|---------------|-----------------|-----------------------|------------------|------------------------|--------------------------------------|
| | | billion liters | % of world production | billion liters | % of world consumption | per capita consumption (liters/year) |
| Old World Countries | France | 5.7 | 20% | 3.4 | 14% | 55.3 |
| | Italy | 5.1 | 18% | 2.8 | 12% | 48.7 |
| | Spain | 4.2 | 14% | 1.4 | 6% | 34.5 |
| | Germany | 1.0 | 3% | 2.0 | 9% | 24.6 |
| | total | 16.0 | 55% | 9.6 | 40% | |
| New World Countries | Unites States | 2.4 | 8% | 2.8 | 12% | 9.4 |
| | Argentina | 1.5 | 5% | 1.1 | 5% | 28.1 |
| | Australia | 1.4 | 5% | 0.4 | 2% | 21.9 |
| | South Africa | 0.9 | 3% | 0.4 | 2% | 8.8 |
| | Chile | 0.6 | 2% | 0.2 | 1% | 14.3 |
| total | 6.8 | 23% | 2.2 | 21% | | |

Source: Adapted from Wine Institute's Key Facts, Wine Institute (2006).

Old World Wine Producing Countries

France. Traditionally known as the leader France ranks as the largest producer and consumer of wine, accounting for 20% of world production and 14% of consumption (Table 1). Impressive as these figures are, France's wine consumption is actually in decline as per-capita consumption has dropped from 60 liters to 55 between 1997 and 2004 (Wine Institute, 2006). At 1.4 billion liters, France is the number three exporter of wine behind Italy and Spain (Table 2). French exports decreased during the 2000-2003 timeframe as have French wine imports to the large markets of the US and UK (Cholette, 2004).

French wine makers also face external economic, social and political challenges, and competition from

the New World intensified dramatically starting in the 1990s. France lost market share in the United States due to informal boycotts in the wake of the Iraq war. The rise of the euro against other currencies, such as the 30% increase relative to the dollar in the last few years, has put French wines at a comparative pricing disadvantage. Yet the consensus among experts is that the primary threat to the French export market is internal to the industry: the inability of the appellation system to appeal to what is becoming a global way of understanding wines (Business Report, 2004).

TABLE 2
Top 10 Exporters of Wine in the World, 2004

| 2004 rank | Country | 2000 Exports | | 2004 Exports | | Growth in Volume, 2004 vs. 2000 |
|--|--------------|----------------|----------------------|----------------|----------------------|---------------------------------|
| | | billion liters | % of world's exports | billion liters | % of world's exports | |
| 1 | Italy | 1.76 | 28% | 1.45 | 19% | -17% |
| 2 | Spain | 0.89 | 14% | 1.45 | 19% | 63% |
| 3 | France | 1.52 | 24% | 1.43 | 19% | -6% |
| 4 | Australia | 0.31 | 5% | 0.65 | 9% | 108% |
| 5 | Chile | 0.27 | 4% | 0.47 | 6% | 73% |
| 6 | USA | 0.28 | 4% | 0.39 | 5% | 40% |
| 7 | Portugal | 0.19 | 3% | 0.32 | 4% | 68% |
| 8 | Germany | 0.25 | 4% | 0.27 | 4% | 8% |
| 9 | South Africa | 0.16 | 3% | 0.26 | 3% | 64% |
| 10 | Argentina | 0.10 | 2% | 0.16 | 2% | 63% |
| total exports from 9 nations profiled | | 5.54 | | 6.54 | | |
| worldwide exports | | 6.27 | | 7.60 | | |

Source: Source: Adapted from Wine Institute's Key Facts, Wine Institute (2006).

Italy. Italy is the second largest producer and consumer of wine (Table 1). At 1.45 billion liters, Italy was

tied with Spain as the largest exporter of wine by volume in 2004, accounting for 19% of all the wine exported worldwide (Table 2). In recent years, Italy has witnessed internationalization of its wine industry, as many foreign-based companies acquired or formed joint ventures with Italian wineries, such as Gallo's Ecco Domani, and the partnership between Italian producer Frescobaldi and US-based Constellation. A few Italian wine companies are also investing abroad; Masa and Antorini have ventures in South America. While large companies exist, most of the country's production is fragmented in many small wineries.

Spain. Spain is the third largest producer of wine, accounting for 4.2 billion liters in 2004 (Table 1). Spaniards have a strong tradition of wine consumption with the country ranked fifth in the world, though the 1.4 billion liters is a third of national production (Table 1). Spain is a major exporter, tied with Italy for first place with 1.45 billion liters of wine exported in 2004 (Table 2). Spain's openness to foreign trade and investment has encouraged foreign producers' investment. For instance, Allied Domecq has recently acquired two large Spanish brands, Maques de Arienzo and Bodegas y Bebidas.

Germany. Germany, a heavy consumer of wine at 2 billion liters in 2001, produced only 1 billion liters in 2004 (Table 1). German wine is dominated primarily by inexpensive, sweet white wines, such as Riesling which accounts for 80% of the wine produced (Wickham et al, 2001). While Germany has always been a large wine producer, Germany is now a net importer. For a European country, German per-capita consumption is relatively low at under 25 liters per year (Table 1). At 270 million liters, Germany accounted for 4% of the total world wine exports in 2004 (Table 2).

New World Wine Producing Countries

United States. Started primarily by French and Italian immigrants in the late 1800's California's winemaking tradition is only a few generations old. A global reputation for fine wine is recent, when two

Napa Valley wines won gold medals at a 1976 blind-tasting competition in Paris, an unexpected victory by everyone, even the winning winemakers (Lukacs, 2000). While over 2000 wineries exist, the top five wine companies have cornered two-thirds of the domestic wine market (Silverman et al, 2002). In addition to large wineries like Gallo, diversified conglomerates and wine groups account for a large fraction of US wine production and are able to leverage their size to enjoy both economies of scale and scope.

With 90% of production concentrated in California, the United States is the fourth largest global producer of wine at 2.4 billion liters in 2004 (Table 1). The US is the third largest consumer, at 2.8 billion liters in 2004. However, as shown in Table 1 the US per-capita consumption is less than 10 liters a year, putting the US in 34th place behind all other major wine producing countries. Diverse consumer behavior patterns explain the low consumption rate; only 10% of adults make 90% of all wine purchases (Himelstein, 2002). Research of adult American consumers shows that of the remaining 90% who are not regular wine consumers, half are teetotalers and the other half prefer beer or spirits (Moulton et al, 2001). Converting more Americans to wine from other spirits has great potential. If 10% of beer purchases were substituted with the same volume of wine, the US wine market would double.

Interestingly, US consumers have always shown strong preference for foreign wines. Not only has the US been a net importer of wine but its imports to exports (in value) ratio between 2000 and 2002 has significantly increased from 4:1 to 5:1 despite a declining dollar (Cholette et al, 2005). Many domestic producers worry that they will continue to lose market share both overseas and locally to foreign producers. Nevertheless, the United States has a strong export presence with the largest importers being UK, Canada, and the Netherlands (Table 3).

TABLE 3
Total US Wine Exports 2003 and 2004

| Importing country | Value (million \$) | | % change | Volume (million liters) | | % change |
|-------------------|--------------------|-------|----------|-------------------------|-------|----------|
| | 2003 | 2004 | | 2003 | 2004 | |
| United Kingdom | 212.9 | 299.1 | 40.5 | 119.0 | 142.9 | 20.1 |

| | | | | | | |
|-------------------------|--------------|--------------|-------------|--------------|--------------|-------------|
| Canada | 112.4 | 123.8 | 10.5 | 59.6 | 66.1 | 10.9 |
| Netherlands | 74.7 | 85.6 | 14.7 | 33.7 | 33.2 | -1.6 |
| Japan | 60.7 | 82.1 | 35.3 | 37.3 | 71.3 | 88.3 |
| Germany | 19.3 | 26.8 | 38.9 | 19.3 | 27.7 | 43.4 |
| Switzerland | 14.4 | 14.0 | -2.7 | 7.8 | 7.6 | -1.9 |
| Belgium | 14.0 | 13.4 | -3.7 | 8.3 | 11.7 | 41.6 |
| Ireland | 13.0 | 13.9 | 13.0 | 6.4 | 6.4 | 0.7 |
| France | 12.2 | 10.3 | -15.5 | 8.6 | 8.9 | 4.3 |
| Denmark | 10.4 | 14.0 | 35.2 | 6.3 | 9.6 | 51.1 |
| US Total Exports | 621.0 | 794.3 | 27.9 | 349.2 | 449.7 | 28.8 |

Source: Adapted from Wine Institute's Key Facts, Wine Institute, 2006

Argentina. Argentina has the oldest wine culture outside of Europe and is the sixth largest consumer of wine worldwide. Argentina ranks second among the New World countries in both production and consumption at 1.5 and 1.1 billion liters respectively (Table 1). Argentineans consumed 28 liters per-capita in 2004, the highest rate outside Europe. Argentina's exporting performance is lackluster compared to the other New World countries profiled, at 160 million liters in 2004 (Table 2). In 1990 Chile and Argentina exported almost equal volumes of wine. Over the following decade Chile's exports grew more than six fold to 309 million liters in 2001, whereas Argentina's exports merely doubled to 88 million liters (German Wine Institute, 2005). To catch up, Argentina recently developed its own version of the successful Australian "Strategy 2025" plan that established wine industry goals.

Australia. Australia accounted for less than 1% of the world production prior to 1970 (Dutruc-Rosset, 2001). By contrast, Australia produced 1.5 billion liters of wine in 2004 which accounted for 5% of global production (Table 1). There are many reasons for the Australia's success in the global market. The initial motivation to succeed in export markets stemmed from low domestic consumption rates. Per-capita consumption is only 22 liters/year, thus Australia's small population generated only 400 million liters in 2004 (Table 1). Developed by wine producers and government officials alike, "Strategy 2025" has been the force behind domestic and international expansion of the Australian wine industry through measures promoting exports and preventing high taxes (Winemakers' Federation of Australia, 2003). The plan

envisioned Australia becoming the most influential wine producer in the world by 2025. As to industry structure, Australian wine industry is highly concentrated with four companies accounting for 80% of production, providing economies of scale in producing value-for-money wines, as well as promoting them (Geene et al, 1999).

Australian wines have also been successful at what has traditionally been an American forte – brand building. Top-selling brands like Jacob’s Creek, Alice White, and Yellow Tail were developed mainly for international markets (Walker, 2003). Colorful labels, imaginative names and a decent value proposition helped to make Australians the fourth largest exporter in 2004, with over 100% growth in 4 years (Table 2). The main export markets for Australia are the UK and US which means that Australia is the most threatening competitor to US wineries domestically, as well as in their export markets.

South Africa. With a production and consumption of 0.9 and 0.4 billion liters of wine respectively (Table 1), South Africa ranks among the top ten countries in both categories. While South Africa has been expanding into global markets, its wine industry may be facing challenges in both production and domestic consumption, including regulatory and other procedural requirements emanating out of an ever-evolving new South African government and the overall uncertainties of national social, economic, and political stability. The South African wine industry is also consolidating as seen by the proposed merger of the nation's Distillers Corporation with Stellenbosch Farmers Winery Ltd, which would form the largest alcoholic beverage corporation in South Africa (Murchie, 2001). Larger corporations and strong collaboration within the national industry have enabled aggressive and effective marketing efforts abroad.

Chile. Chile has the benefit of an ideal climate for grape growing. With their return to democracy in 1990, the economic climate also improved. Large foreign investments enabled significant production expansion and export of quality wines that continues to this date (Foderaro, 2003). Among the New World

countries, Chile proved to be a top producer and exporter of wine in the world (Tables 1 and 2). At 14 liters per year, Chilean per-capita consumption is lower than Argentina's but higher than that of the US (Table 1) though Chile's small population limits the potential for domestic consumption growth. Chile exported 470 million liters of wine in 2004, ten times as much as in 1990 (German Wine Institute, 2005). The primary export markets for Chilean wines are the US (35%) followed by the UK (18%) and Canada (7%). Exported wines are produced by a handful of large companies, with few labels and consistent brands. With its ideal growing climate and low costs for land and labor, Chile has been an attractive target for foreign investment (Hulot, 2003).

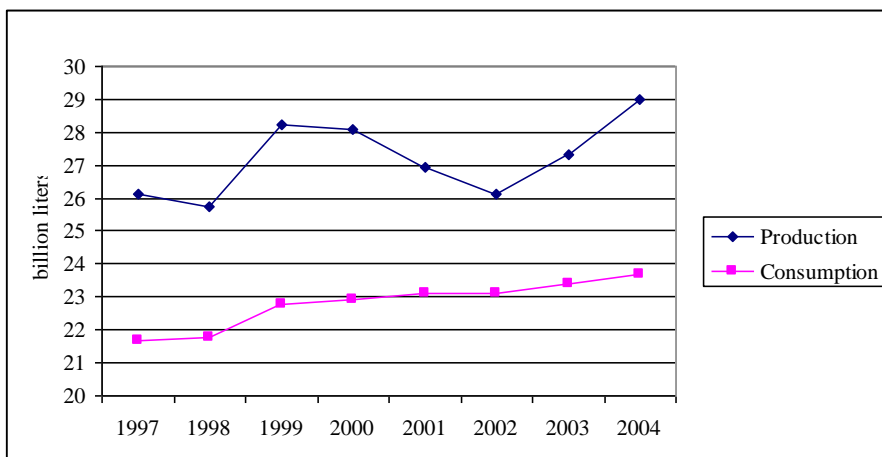
III. DRIVING FORCES IN THE WINE INDUSTRY

The repercussions that wine producers are experiencing from globalization, especially wider and stronger competition, are further exacerbated by the following driving forces: 1) a worldwide over-supply of grapes and the incumbent pricing pressures 2) increased consolidation at the producer, distributors and retailing sectors, and 3) shifting consumer behavior patterns.

Worldwide Over Supply of Grapes and Incumbent Pricing Pressure

Given increased plantings and favorable weather conditions in the past few years, the oversupply of grapes has been a driving force. Since there is a several year lag between planting vines and increasing or shifting production to varietals that are more popular, it should not be surprising that the supply of wine grapes is often at variance with demand (Cholette, 2004). As shown in Figure 1, although worldwide wine consumption has been growing it is below world production every year for the past 5 years, and surpluses have ranged between 15% and 20% of total production.

Figure 1
Global Wine Consumption and Production, 1997- 2004



Source: Cholette et al, 2005.

To prevent prices from falling further due to this excess capacity, some wine producers have had to resort to drastic measures. France has introduced per-hectare caps on production introduced, and the EU is currently subsidizing distillation of wine into industrial alcohol. In California’s Central Valley, 70,000 acres of vines were plowed under in the height of the domestic oversupply (Murphy, 2003).

The second challenge caused by oversupply stems from price-cutting by rivals. Imported wines account for one out of every four bottles sold in the US, and domestic wine producers need ways to compete with the low price and high quality of imports in order to regain market share. Pricing pressures could decrease overall industry profitability if wineries engage in price wars. The more unpalatable alternative is to not compete and then lose market share to other domestic or international producers who offer quality wines at lower prices. Historically, in times of oversupply a country restricted its markets to imports. However, many countries have signed trade agreements to keep markets open. For instance, Australia, Canada, New Zealand, and the US have agreed to accept differences in winemaking techniques and will be approving differences on labeling laws and tariff agreements to reduce trade barriers; oenological differences can no

longer be used as an excuse for protectionism (Wine Institute, 2004). While barriers such as quotas and duties are still impeding the wine industry and are discussed later, they are on the decline.

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Consolidation of Wine Producers, Distributors, and Retailers

Through mergers and acquisitions, consolidation is occurring among wineries worldwide. When an industry starts to mature, firms enhance profits by consolidating to become bigger players, creating competitive advantages through economies of scale and in gaining negotiating power with distributors. Some industry experts predict that in the next five years the vast majority of wine sales will be dominated by ten or so borderless mega-consortiums (Gettler, 2003). Closely tied to these mergers and acquisitions is the increased rate international technology transfer; employees from big and small firms alike are spending more time abroad studying the other countries winemaking techniques (Williams, 1995).

In regard to distribution, the 20 largest wholesalers control 70% of US distribution (National Spirits & Wine, 2004 Annual Report). Large distributors enjoy economies of scale and are able to pass some of their lower costs to the retailers, increasing the total efficiency of the supply chain. However, distributor consolidation has made it increasingly difficult for smaller producers to get their product onto the retailers' shelves. Wholesalers prefer to distribute only the top selling brands, in lieu of small or new labels, since their profits come from markups on products they are able to replenish quickly (Cholette, 2004). Distributors wish to avoid products that may sit on store shelves too long and prefer brands that are proven bestsellers. The recent US Supreme Court ruling that effectively relaxes some direct shipping prohibitions, offers some recourse to small wineries to reach US wine consumers (Wine Institute, 2005). It remains to be seen how small wineries can employ creative marketing and distribution strategies to enjoy the benefits of direct marketing when shipment involves small quantities and a nontrivial cost.

At the retail level, consolidation is occurring in both restaurants (on premise) and in supermarkets (off

premise) sectors. Smaller brands have a harder time gaining placement on the shelves and on wine lists because the head office may choose a few brands to use in all of their locations. Supermarkets accounted for a 41% share of US retail wine sales in 2000, so consolidation of these chains is relevant to the industry (Wickham et al, 2001). The shift to mega-supermarkets is no longer solely an American phenomenon as the International Wine Investment Fund estimates 60% to 80% of global wine sales now occur through such supermarkets (Gettler, 2003). As a result, tens of thousands of international wine brands vie for space on the store shelves of these fewer, larger, and more powerful supermarkets.

Shifting Consumer Behavior Patterns

Ultimately, what drives the wine industry is the consumer. The Old World producers have had the advantage of tradition behind them in their home markets. Over the centuries wine has become an integral part of many European cultures and is considered standard accompaniment at lunch and dinner. However, there is little room for expansion in their home markets and most countries are experiencing declining per-capita wine consumption, as social campaigns against alcoholism and drunk driving have increased.

Per-capita wine consumption in most of the New World countries substantially lags that of Europe. Pushing affordable wine on to the shelves of world markets will not necessarily increase global consumption by itself. Consumers have to pull the bottles off the shelves in consistent purchases. For instance, US per-capita consumption has been increasing modestly, but in order to increase further wine must be marketed in a way that will promote everyday drinking among a greater percentage of the population in a socially responsible manner.

Currently 80% of US wine consumers consider themselves “uninvolved” or uneducated about wine (Stallcup, 2005). Consumers feel intimidated by “wine geek speaks” on the back of wine labels and have trouble remembering which wines they bought and liked. Researchers watching consumer behavior have

noticed shoppers appear to be confused during the wine selection process. Customers have expressed that they want to easily and consistently identify the wines they will enjoy without having to solicit personal assistance in the store. Many inexperienced wine drinkers feel confused about all the wine choices, especially the intricacies of foreign appellations. Producers need to design and label wines that consumers can better understand. The other design feature that may make wine more approachable to the consumer is using twist top closures instead of corks. Recently, an Australian packaging designer company, which invented a synthetic substitute for cork won the prestigious gold medal for the "Technical Innovation Award" at the Australian Packaging Awards. Once again, Australian producers proved more adept in simplifying wine packaging for of consumer (Zork, 2005).

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IV. KEY SUCCESS FACTORS AND NATIONAL COMPETITIVE ADVANTAGE

Globalization and other driving forces will continue to exert significant influence on the wine industry. Some countries are better positioned to gain from globalization than others. Figure 2 presents a matrix of the nine countries profiled with respect to how they stack up five key success factors that contribute to global competitiveness in the marketplace. The factors analyzed include 1) existing domestic market position, 2) domestic market growth potential, 3) economies of scale and/or underlying cost structure benefits, 4) adaptability to industry changes, and 5) potential to attract foreign investment. Identification of these factors is consistent with extant literature on international trade and marketing. On the demand side, consumer preference, represented by domestic market size and its growth, account for a country's proclivity to produce certain products. On the supply side, an industry's cost structure and other dynamic characteristics (such as, flexibility) contributes to a country's competitive advantage in that particular sector. For elegant expositions of these factors and driving forces behind international trade, see Markusen et al, (1995) and Porter (1998).

The first factor is the existence of a strong domestic market, defined as where a large volume of wine is purchased and where consumers readily select domestic wines. The second factor is the potential for growth in the producer's domestic market where producers may have local knowledge and other national advantages such as distribution. The third factor, economies of scale and cost structure benefits addresses the advantages of company size and the low cost of factors of production in certain nations. Countries where larger firms dominate the production have the advantages of scale and scope as well as improved power in promoting and pushing their wines to consumers and retailers. Additionally countries with scarce or high priced land and labor incur higher costs of production. Fourth, industry adaptability to change summarizes the willingness and ability of producers to experiment with cost saving production methods or

to pioneer new marketing techniques. It also addresses if producers are free from excessive regulations and blind adherence to long-standing traditions. Finally, countries that are politically stable and have industry-friendly climates or other natural comparative advantages that will attract foreign investment in wine production, which makes these countries stronger global competitors (Collins, 2004).

Old World producers were the first to define tastes and quality standards and have traditionally been supported by a strong local consumer base. The New World has had to work hard to build their wine industry, both in infrastructure and reputation. Large-scale wine production is relatively recent, and many of the New World producers recently faced difficulties such as currency collapse, prohibition, and international sanctions. Per-capita consumption also lags that of the Old World countries. Yet New World producers have recently been successful in producing consistent quality wine and in capturing global market share. The Old World countries are gradually losing market share as New World producers increase the scale and quality of production as well their branding expertise (Wickham et al, 2001).

Figure 2 presents how each country stacks up on each key success factor and rates its overall competitive advantage. In order to provide a comparison among these wine producing countries we used a qualitative ranking of these nine countries on each factor respectively on a 3-point scale (1=strong, 2=moderate, and 3=weak). Thus, we place them into three groups with respect to their comparative competitive advantage position. The group with the strongest competitive position includes United States, Australia, and Chile. Australia and Chile both have small populations that provide for a tiny domestic market with little potential for growth. However they are very well positioned to produce and export wine with their adaptive, large-scale producers and their great lure for foreign investments, providing them with a position of a strong competitive advantage. With respect to production, cost structures suggest Australia and Chile may be better positioned than the US. However, economies of scale and economies of scope in

marketing offer an advantage to the US because it is a populous and affluent nation. While the US wine market is already significantly larger than Australia and Chile, it has even more potential to expand. With all other key success factors strongly favorable, the US also possesses significant competitive advantages.

FIGURE 2
Competitive Advantage Position by Nation

| | Exiting Domestic Market Position | Domestic Market Growth Potential | Economies of Scale/ Cost Structure Benefits | Adaptability to Industry Change | Potential to Attract Foreign Investment | Overall Competitive Advantage |
|---------------------|----------------------------------|----------------------------------|---|---------------------------------|---|-------------------------------|
| New World Countries | | | | | | |
| United States | Strong | Strong | Moderate | Strong | Strong | Strong |
| Australia | Weak | Weak | Strong | Strong | Strong | Strong |
| Chile | Weak | Weak | Strong | Strong | Strong | Strong |
| Argentina | Moderate | Weak | Moderate | Strong | Moderate | Moderate |
| South Africa | Weak | Weak | Moderate | Strong | Moderate | Moderate |
| Old World Countries | | | | | | |
| Italy | Strong | Weak | Weak | Moderate | Moderate | Moderate |
| Spain | Moderate | Weak | Weak | Moderate | Moderate | Moderate |
| France | Strong | Weak | Weak | Weak | Moderate | Weak |
| Germany | Strong | Moderate | Weak | Weak | Weak | Weak |

The group of countries with moderate competitive advantages includes Italy, Spain, Argentina and South Africa. Lingering economic concerns and disadvantages of scale prevent Argentina from being ranked as competitively as neighboring Chile. Likewise, South Africa has strong marketing economies of scales and moderate production economies of scale, but currently domestic unrest has diminished its attraction for foreign investment and ability to expand its home market. Spain and Italy are hampered by decreasing consumption rates and small economies of scale in production, but they have shown promise in their ability to adapt to an increasingly internationalized marketplace and to attract foreign investment. These are the two Old World countries profiled that show a moderate overall comparative advantage.

The countries with the weakest competitive advantage positions in the global wine industry are two traditional strongholds of wine production in the Old World: France and Germany. While they have large

domestic markets, there is little opportunity for further growth. The concentration of production into small wineries, scarce land and labor, complex labeling practices and inability to leverage new production, and marketing techniques does not bode well for effective competition in a global market place. Nor does either country hold much potential for attracting foreign investment, save for some traditionally undervalued areas of France, like Languedoc.

In conclusion, it is clear that the New World countries are currently positioned better to capitalize on the opportunities created through industry globalization and other current driving forces. Italy and Spain emerge as the best positioned Old World nations. Not surprisingly, Australia recently ousted France to become the largest wine supplier to the UK despite being thousands of miles away and producing only a third as much wine as France (Beveragedaily.com, 2005). This competitive advantage scenario should be a wake-up call to wine producing countries. Indeed, some Old World countries have begun efforts to better adapt to industry-wide improvements in production and marketing practices (Business News Onlypunjab.com, 2005). However, it is clear that many nations need to increase support that will encourage production and marketing innovations to improve their competitive advantage position to help local wineries succeed in the changing and increasingly competitive wine marketplace.

V. IMPLICATIONS AND RECOMMENDATIONS FOR WINERIES

What lessons can be learned at the winery (firm) level? In this section, we would like to find what insights the above country and industry level analyses offer for the individual wineries as well as small and medium enterprises (SMEs) that aspire to compete and thrive on a global level. While strong national competitive position is a necessary condition, it is not sufficient to guarantee long-term success of individual countries. In order to maintain competitive advantage and cope with the dynamic forces of globalization, the wineries need to adopt multi-pronged strategies. Given the analysis of driving forces and key success

factors, we would also like to proffer recommendations in three areas. We believe wineries of all sizes in all nations can benefit from: (i) more emphasis on market orientation, (ii) increased export assistance, and (iii) coping with trade barriers. Below we discuss these recommendations in details.

Increased Emphasis on Market Orientation

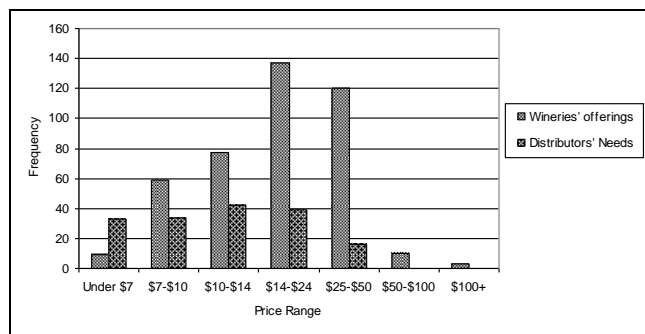
First, as previously discussed in the paper, shifting consumer behavior pattern is a major driving force in the wine industry. Therefore, wineries should assign higher significance on consumer behavior in the form of developing a stronger market orientation. Slater and Narver (1995) define market orientation as “the culture that (1) places the highest priority on the profitable creation and maintenance of superior customer value while considering the interest of other stakeholders; and (2) provides norms for behavior regarding the organizational development and responsiveness to market information.” market orientation is the antecedent of creativity for both new products and marketing programs (Im and Workman, 2004). Market driven companies base their production and distribution plan on a clear understanding of end-user’s need through proper segmentation and targeting.

We find evidence that many wineries are integrating market orientation into their strategies. Beaujanot and Lockshin (2003) present empirical evidence that market orientation helps an organization develop positive long-term buyer-seller relationship. They emphasize that wineries should first create a business culture focused on customer orientation and cross-functional coordination. For example, wine businesses in Australia and New Zealand have made substantial progress in the area of both strategic marketing (segmentation, targeting, and positioning) and in tactical marketing (unique product, brand strategies, pricing, and packaging). Even if a winery seeks to limit its marketing activities within the domestic markets, they need to understand the motivation and needs of their consumers. For example, selling the same wine (i.e., tangible product) to baby boomers and millennial generation consumers warrants different positioning

strategies based on a solid understanding of consumer behavior (Moulton et al, 2001). Additionally, a well-developed market orientation can enable wineries to appreciate the vast potential of the ever-expanding market beyond the borders of their respective domestic markets.

The area of distribution deserves a special mention. In the case of US wineries, a lack of market orientation explains the difference between these wineries' supplies and distributors' demands. Figure 3, which draws on data collected from US wine producers and distributors attending a tradeshow, illustrates this demand mismatch. The graph shows the suggested retail price of over 200 wines offered by 45 wineries and compares it to the desired price points sought by 15 distributors. While the distributors' price range is broad, it is centered well below the majority of the products offered. Although the data are from a self-selected survey, they do represent a wide cross section of distributors and wineries.

Figure 3
Mismatch between Wineries' Offerings and Distributors' Needs at the 2004 World Wine Market



Source: Cholette, 2007.

While distributors in other sectors are re-inventing themselves to cope in an environment marked with increased importance of direct marketing, most of the wineries are still heavily dependent on distributors. To minimize their reliance on distributors, small wineries (examples of SMEs) could devise alternative strategies to promote their wine (product). One such strategy could be forming a manufacturers'

cooperative, which, in marketing jargon, is called a contractual vertical marketing system (VMS). We envision a ‘Wineries-Sponsored-Retailer Franchise.’ Recently this concept seems to have drawn interest from private and small entrepreneurs in the US, although in a very limited scale. Their goal is to help foreign buyers and retailers to deal directly with several wineries simultaneously without seeking help from any intermediaries (Wineteam, 2006). In the past, the former Chalone Group also allowed individual wineries with autonomy to create their own products yet still provided competitive advantages in procurement, marketing, and distribution. For example, small wineries in the US could also explore various ways to leverage the distributive rights vested by the Supreme Court ruling that effectively relaxes some direct shipping prohibitions to direct marketing (Wine Institute, 2005). This can set a very useful precedence for wineries or SMEs in all countries so they can exploit the technology and legal support to explore new avenues to establish direct contact with consumers.

Overall, a lack of market orientation may lead them to lose sight of the market dynamics. For example, in an interview with Lance Cutler two leading experts in the wine industry opine that most wineries cast a “*deer-in-the-headlights*” look when asked to identify their competition or needs of their buyers (Cutler, 2005). Even an industry giant like Coca Cola failed when it decided to attack industry leaders, like Gallo, with generically similar products. Coca Cola’s sale of Wine Spectrum illustrates the consequences of a lack of market orientation. Without an innovative approach, it faced a substantial cost disadvantage to Gallo. Consequently, Coke failed to attain sustainable sales and profits (Porter, 1998).

Increased Export Assistance

The second area for wineries is a need for increased export assistance from external sources. Typically US wineries depend on domestic sales and do not usually consider export to augment their revenues. The recommendations on external assistance are drawn from empirical evidence collected in the US.

Export assistance to wineries. In many countries, governments instituted programs to provide up-to-date information on export markets. For example, the California Wine Export Program managed by the Wine Institute uses resources from USDA’s Market Access program (MAP) to help US wineries. Yet small wineries need education and training assistance from external sources. Castaldi et al (2002) identify export assistance needs as perceived by US winery managers. Table 4 summarizes the major export assistance needs as perceived by exporters and non-exporters alike. Wineries should also meet annually with regional and statewide trade associations to determine how various regional and state programs, such as generic promotions and events can improve export sales (Walker, 2005).

Table 4
Export Assistance Needs of U.S. Wineries

| Exporters' needs | Non-Exporters' needs | Both exporters' and non-exporters' needs |
|---|--|--|
| <ul style="list-style-type: none"> • Information regarding competitors, consumers, and distributors in specific export markets. • Assistance in finding distributors or agents for specific export markets (especially for inexperienced exporters and those dissatisfied with their current export program). | <ul style="list-style-type: none"> • Training and assistance in understanding the fundamentals of developing a successful winery export program. • Assistance in finding appropriate distributors or agents to sell their wine in foreign markets. | <ul style="list-style-type: none"> • Opportunities to learn about the export experiences of other wineries (rated as the most valuable need for exporters and the second most valuable assistance need for non-exporting wineries). |

Source: Castaldi et al, 2002.

Managing Trade Barriers

Finally, the third area in which wineries need help is dealing with trade barriers. While these barriers have softened in recent years, they still present formidable challenges to wineries attempt to reach international markets. In the US, the Wine Institute plays an important role in identifying barriers that limits access of US wine to different countries and regions in the world (Table 5). Wineries in other countries could also work with federal and local governments in persuading foreign governments to eliminate or reduce trade barriers. For examples, in recent years the US Department of Agriculture has increased Market Access Program (MAP) funding to \$135 million of which \$5.4 million was allocated to US wine industry

Comment [c3]: Tie in with globalization part in the first part!

(Wine Institute, 2004 and US Department of Commerce, 2005). The Office of the U.S. Trade Representative and EU Commission for Agriculture and Rural Development reached an agreement on wine-making practices and labeling of wine to increase bilateral trade in wine between the two regions (i.e., old world and new world). This agreement expands the global market for wineries in both regions by eliminating a long-standing non-tariff barrier.

Table 5
Trade Barriers in Major Current and Potential Importers of US Wine

| Countries/Regions | Quantitative barriers | Qualitative barriers |
|---|--|---|
| European Union (58% of US Wine Exports) | <ul style="list-style-type: none"> • Average tariff – 50% higher than the average US tariff • Value Added Taxes (VATs) – imposed by individual countries • Subsidies for domestic wine production | <ul style="list-style-type: none"> • Labeling regulations, marketing regulations (prevention of use of terms such as "reserve") • Rejection of oenological practices not specifically recognized in EU regulations • Certification regulations – vague |
| Canada (17%) | <ul style="list-style-type: none"> • Additional taxes levied by provinces (e.g., mark-ups, sales taxes, bottle taxes, environmental fees) • Cost-of-service mark-ups • Minimum pricing requirements | <ul style="list-style-type: none"> • Discriminatory delivery systems • Warehousing restrictions |
| Japan (12%) | <ul style="list-style-type: none"> • Tariff – 15% ad valorem (high for a developed country) • Liquor tax | <ul style="list-style-type: none"> • Food sanitation law |
| Latin America and the Caribbean (4%) | <ul style="list-style-type: none"> • High tariff plus VATs (preferential treatment to MERCOSUR countries) • Processing tax (Brazil) • Laboratory fees (Chile) | <ul style="list-style-type: none"> • Mandatory/special import licensing • Certification process (Brazil) |
| China* (<1%; potential market) | <ul style="list-style-type: none"> • 17% VATs (in addition to import duty) • 10% Consumption tax • Minimum invoice value (\$2.70 per bottle) | <ul style="list-style-type: none"> • Government monopoly • Labeling requirements • Prohibition on US importing and distribution companies |

Source: Adopted from Wine Institute, 2004.

Conclusion

This paper profiles nine old and new world wine producing countries, identifies the forces driving the global wine industry, as well as discussed implications of recent changes for the US wine industry. Although the forces of globalization pose new challenges for these wineries, they are less likely to drive the wineries that adopt a market orientation out of business. The presence of heterogeneous consumer

preference, coupled with numerous opportunities for experimentation, ensures a long-term existence and even growth of the small and medium sized wineries that can adapt and compete effectively.

In order to thrive in a challenging world marked by merger and acquisition, increased global trade and investments, and wider scope for spillover effects across borders, smaller wineries need to adapt to the changing forces. As noted earlier, having national competitive advantage is no guarantee for long-term success of individual countries. Competitive advantage needs to be nurtured to create a match between a winery's distinctive capabilities and consumers' demands. The driving forces imply that wineries of all sizes in all nations can benefit from (i) more emphasis on market orientation, (ii) increased export assistance, and (iii) managing trade barriers. In this paper, we provide recommendations focused on the needs of US wineries but this advice can be applied to wineries of all sizes and nationalities given their need to adapt to changes caused by the increased pace of globalization and to thrive in a challenging environment.

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