CONSIDERING COMPETITIVENESS  
IN THE WINE INDUSTRY:  
THE SOUTH AFRICAN CASE

The paper is about:

- Defining and Measuring Competitiveness (Balassa & Porter)
- Application: The South African case
  - Measurement
  - Indicators, determinants & considerations
- Strategies to create & sustain competitiveness

* Based on analysis by Esterhuizen & Van Rooyen (2000-2007)

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**Quote 1**

“For me wine is so much more than a liquid in a glass; the liquid is merely our link to what is often a fascinating story, a spot on the globe, a point in time, a fashion, an argument between neighbouring farmers, rivalry, perhaps proud new owners who want to make their mark at all cost.”


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**Quote 2**

From the movie “Sideways, 2004”

**Maya asks Miles why he is so into Pinot Noir:**

“I don’t know. It’s thin skinned, temperamental, ripens early ……….. Only when someone has taken the time to truly understand its potential can Pinot be coaxed into its fullest potential. And when that happens, its flavours are the most haunting and brilliant and subtle and thrilling and ancient on the planet”

**On hearing this, Maya’s heart open to Miles for the first time:**

“I like to think about the life of wine, how it’s a living thing. I like to think about what was going on the year the grapes were growing, how the sun was shining that summer or if it rained ……….. what the weather was like. I think about all those people who tended and picked the grapes …………… because a bottle of wine is actually alive”
Statement 1
Wine is a wonderful product:
• It is about special people and their cultivated vineyards and crafted wines;
• It is about friends enjoying and having a conversation over a glass of wine (or two……);
• It is about wine writers, readers, wine lovers, scientists and analysts, government and business;
• It is about lifestyle and labels, enjoyment, stress, tension and excitement;
• It represents a country’s national identity;
• It is the product of a global industry.

Wine is not only about competitiveness – but it is also about competitiveness!

Statement 2
“The future of the wine industry (in any country or region) depends on (global) competitiveness performance i.e. the ability to keep on selling your product”

Statement 3
“In today’s (wine) business, the competition will bite you if you keep running; if you stand still they will swallow you!”

William Knutsen, Jr.
Chairman, Ford Motor Company
Defining competitiveness

Competitiveness strategies must enable the firm (sector, country) to attract scarce economic resources from other, less competitive economic endeavours, thus allowing it to grow, reinvest, innovate, expand and perform.

Defining competitiveness

• Competitiveness **is** a dynamic and involved process rather than an absolute or static state of affairs and can only be assessed in a relative sense i.e. relative to your competitors.

• Competitiveness **is** clearly not a theoretical economic concept depending on comparative advantage theories or the economic efficient use of the resource base (land, labour, capital); it rather describes the ability to continue to exploit (the market) for gain; it depends on the ability to innovate and to adapt in order to continue to do so.

Statement 4

In short

“to be competitive in today’s world of wine business is to **continue to trade** your wine products – profitable, innovative, sustainable, appropriate ROR, ……”

In considering competitiveness it is important to analyse and understand trends and expected changes in business performance i.e. to measure the trade performance in a product over time, relative to that of the competition.
Application: The South African Case

The SA wine industry today

- 100,207 hectares of vines; 1,013 million litres
- 4,400 primary wine producers (60% producers less than 100 tons grapes p.a.)
- 750 wine cellars; add 200 over past 2 years (69 cellars deliver plus 4m litres p.a.)
- 700 million litres of drinking wine (66% increase since 1994)
- 36% red and 64% white (1995 12% red)
- 3% of global wine production (9th largest)
- 268 million litres exported (429% more than 1994)
- SA per capita consumption + 7 litres p.a. (declining?)

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Turnover</th>
<th>Contribution to GDP</th>
<th>Contribution to GGP</th>
<th>Total Capital</th>
<th>Total Household Income</th>
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<tr>
<td>1996</td>
<td>R 6,019 m</td>
<td>R 10,054 m</td>
<td>R 9,040 m</td>
<td>R 40,652 m</td>
<td>R 5,940 m</td>
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<td>1999</td>
<td>R 7,369.8 m</td>
<td>R 14,557 m</td>
<td>R 8,700 m</td>
<td>R 38,263 m</td>
<td>R 950 m</td>
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<td>2003</td>
<td>R 10,675.27 m</td>
<td>R 22,549 m</td>
<td>R 14,775 m</td>
<td>R 51,392 m</td>
<td>R 9,764 m</td>
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<td>2006*</td>
<td>R 11,718.82 m</td>
<td>R 24,753 m</td>
<td>R 16,153 m</td>
<td>R 56,416 m</td>
<td>R 1,798 m</td>
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</table>

* 2003 figures adjusted with inflation (CPI)

Main Economic Attributes

<table>
<thead>
<tr>
<th></th>
<th>1996</th>
<th>1999</th>
<th>2003</th>
<th>2006*</th>
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</thead>
<tbody>
<tr>
<td>Producer's profit margin</td>
<td>?%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
</tr>
<tr>
<td>Packaging</td>
<td>8%</td>
<td>10%</td>
<td>10%</td>
<td>10%</td>
</tr>
<tr>
<td>Marketing</td>
<td>16%</td>
<td>6%</td>
<td>6%</td>
<td>6%</td>
</tr>
<tr>
<td>Overheads</td>
<td>11%</td>
<td>11%</td>
<td>11%</td>
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</tr>
<tr>
<td>Grape costs</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
</tr>
<tr>
<td>Winemaking</td>
<td>9%</td>
<td>9%</td>
<td>9%</td>
<td>9%</td>
</tr>
<tr>
<td>Retail</td>
<td>23%</td>
<td>23%</td>
<td>23%</td>
<td>23%</td>
</tr>
<tr>
<td>Tax (VAT &amp; excise)</td>
<td>17%</td>
<td>17%</td>
<td>17%</td>
<td>17%</td>
</tr>
<tr>
<td>Total</td>
<td>51%</td>
<td>54%</td>
<td>54%</td>
<td>54%</td>
</tr>
</tbody>
</table>

Behind the price tag - 2005

White wine

- R30/bottle
- 25% Retail
- 19% Tax (VAT & excise)
- 7% Producer’s profit margin
- 15% Packaging
- 4% Winemaking
- 4% Marketing
- 18% Overheads
- 7% Grape costs
- 55% 30.48/litre

Red wine

- R20/bottle
- 22% Retail
- 17% Tax (VAT & excise)
- 7% Producer’s profit margin
- 15% Packaging
- 3% Winemaking
- 8% Marketing
- 16% Overheads
- 7% Grape costs
- 55% 30.48/litre

Production Areas of South Africa

- Western Cape: Stellenbosch, Paarl, Worcester, Robertson, Swartland, Constantia
- Northern Cape: Kalmoesrivier
- Eastern Cape: Malmesbury, Robertson
- Limpopo: Thabazimbi, Pretoria, Potchefstroom, Rustenburg
- Free State: Orange River, Northern Cape
- Eastern Cape: Addo, Stormberg, Modimolle, Bushveld, Mokopane
- Western Cape: Swartland, Overberg, Franschhoek, Tulbagh
- Northern Cape: Griquatown, Prieska, Kakamas
- Eastern Cape: Great Brak River, klein Karoo, Robertson

DIAGRAMS
Measuring Competitiveness
(The formula):

Relative Trade Advantage (RTA)

- Trade realities i.e. trade performance (including imports & exports), irrespective of policy regimes, subsidisation, etc.
- Ratio’s of trade in wine (by Country A) vs Global trade in wine; relative to Ratio’s of trade in all products (Country A) vs Global trade in all products.

Notes: RTA is formulated as:

\[
RTA_{ij} = RXA_{ij} - RMP_{ij} \quad \ldots 1
\]

\[
RXA_{ij} = \frac{(X_{ij} / \sum_{l, l \neq j} X_{il})}{\frac{\sum_{k, k \neq i} X_{kj}}{\sum_{k, k \neq i} \sum_{l, l \neq j} X_{kl}}} \quad \ldots 2
\]

\[
RMP_{ij} = \frac{(M_{ij} / \sum_{l, l \neq j} M_{il})}{\frac{\sum_{k, k \neq i} M_{kj}}{\sum_{k, k \neq i} \sum_{l, l \neq j} M_{kl}}} \quad \ldots 3
\]

Where:

- RXA = The Revealed Export Advantage index
- RMP = The Relative Import Penetration index

Equations 2 and 3, X (M) refer to exports (imports), with the subscripts i and k denoting the product categories, while j and l donate the country categories. The numerator is equal to a country’s export (imports) of a specific product category relative to the exports (imports) of this product from all countries but the considered country. The denominator reveals the exports (imports) of all products, except the considered commodity from the respective country, as a percentage of all other countries’ exports (imports) of all other products. The level of these indicators shows the degree of revealed export competitiveness/import penetration.

While the indices RXA and RMP are calculated based exclusively on either export or import values, the RTA considers both export and import activities. From the point of view of trade theory and globalisation trends, this seems to be important and given the growth in intra-industry and/or entrepot trade, this aspect is becoming increasingly important (ISMEA, 1999). The RTA indicator implicitly weights the revealed competitive advantage by calculating the importance of relative export and relative import competitive advantages. Values below (above) zero point to a competitive trade disadvantage (advantage).


Drivers of Competitiveness Performance:

Phase 1 - REGULATED COMPETITIVENESS (1930’s to 1970):
- Quotas, surplus removal schemes, price agreements open global markets
- Producers controlled through a cooperative system and legislation

Phase 2 - CONSTRAINED ECONOMIC/POLITICAL ENVIRONMENT (1970-1990):
- Regulated industry; political pressures and economic sanctions

Phase 3 - “MADIBA MAGIC” (Deregulation; democratic government; lifting of sanctions) (1990 – 1996):
- Start of deregulating the agricultural business environment (quotas, pricing, etc abolished)
- Release of Nelson Mandela; political freedom
- International markets opening up for wines of the “rainbow” nation
  - from brandy to (white) wines
  - shortages of red wine
- First democratic government in 1994
- Improved business knowledge & access to international wine supply chains
- Full deregulation of industry (mid 1990’s)
Phase 4 - FACING COMPETITIVE REALITIES (1996 – 2000):
- Wine writers: Style and quality questioned (SA Wines robust, old style, etc)
- New requirements:
  - fruity, non grassy
  - less tannins
  - consistency
  - more reds required
- Reduction in trade
- Australian boom – competition in UK supermarkets
- Imports of red wines (Argentina/Spain)
- blends
- Technological innovation:
  - Planting of improved grape varieties, virus-free plant material
  - Cultivar specific site solutions
  - More red varieties planted
- Wine quality change - "new world wines"
- Supply chain reliability important

Phase 5: TOWARDS BECOMING A GLOBAL PLAYER (2000 >)
- Increased trade - UK, Netherlands, Germany
- Manage exchange rate fluctuations/weak rand followed by strong rand, etc
- Brand development & promotion
  - Establish "Brand SA":
    - "Variety is our nature"
    - Environmental focus (IPW)
    - Social focus (WIETA)
- Market segment selection critical: higher value wines rather than volumes
- Integrity systems tested (wine flavouring)
- Certification important (IPW; authenticity; integrity)
- Develop new markets
  - USA, India, Russia
  - South Africa (Black Diamonds)
- "Unique", "typical", "exotic" SA wines?
  - Pinotage (Red)
  - Chenin Blanc (White)
  - Blends?
- Wine writers again!
  - SA’s tell-tale rubbery red wine pong (Jane Macquitty)
  - "Good value for money" (Jancis Robinson)
- Towards world class technological solutions:
  - Viruses (leafroll) and diseases (Aster Yellow)
  - Cellar technology
  - IPW expanded

A next phase: The South African experience (2010)?
- A strong “SA Brand” image and market segmentation:
  - Eco Friendly/Socially responsible/Clean-n-Fresh/”Magic Kingdom”
- Stronger technological innovation + consumer focus
- The “South Africa Supply Chain”: “good-to-do-business-with”
- 2010 FIFA World Cup opportunities (before & after)
- WINE + TOURISM + FOOD = The ultimate SA experience
**Statement 5**

- "Always keep a "keen eye" on your competition"
- "We need to identify all our competitors, both current and potential and study their strategic positions and tendencies"

(Peter Killing, 1990)

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**Statement 6**

Competitiveness status is determined by a complex and interactive set of factors influencing the (wine) business environment; and the ability to perform within this environment.

**Determining Key Success Factors and Constraints:**

- **Determinants of competitiveness include:**
  - Production factors; demand; supporting industries; firm strategy; structure and rivalry; government policies and actions; and chance.
  - (Michael Porter)

- **Framework of Analysis:**
  2. Wine Executive Survey (WES)
     - 200 wine executives (2006) [2008 results out soon]
     - Three level ratings of factors influencing competitiveness: Enhancing(3); moderate(2); constraining(1)
Priority 1: Demand conditions as determinants of competitiveness
(1 = Constraint; 2 = Moderate; 3 = Enhancement)

Issues/Questions: Demand conditions

1. **SA’s image (Brand SA)**
   - Unique South African: New world, old world?; diversity?
   - Market segment + country focus?
   - Wine writers influences?

2. **Targeting the right markets**
   - Local markets – price/quality segments: growth in LSM 2-6 (lower middle, black groups)
   - International markets – place/price/quality segments (USA or traditional markets?); price cost realities (not volume led strategies); Environmental/Ethical markets – UK, Germany?
   - White wines? Wine styles? Chenin Blanc; Semillon; Viognier; blends
   - Red wines? Pinotage; blends
   - Wine writers?

3. **Marketing strategies?**
   - Brand development – too many brands?
   - Focus: Country/city/market segment?
   - Volume or value?
"Wine Magazine" (July 2007)

The argument has been put often enough that though single variety Shiraz shows promise in this country, it is through blending that local producers will attain even higher quality levels.

"If further evidence was needed to support this thinking, along comes the Saxenburg 2003, consisting of 85% Shiraz but also "a teaspoon of something else" as winemaker Nico van der Merwe puts it. Added into the mix is 8.5% Cabernet Sauvignon and 6.5% Merlot. "I don't usually bother with 0.5% here and 0.5% there, but this wine needed that kind of crafting".

"As for the decision to blend, Van der Merwe admits that he likes what aromatic white variety Viognier can bring to Shiraz, but feels that the nature of Saxenburg Shiraz is such that the two varieties would not combine well. Hence the addition of Cab and Merlot, which he feels "brings flair" to the end-product.

"A top wine shouldn't be a blunt instrument. The tannin structure shouldn't be (excessively) rather soft and smooth."

Hear, hear to that!

Issues/Questions: Structure & rivalry

1. Strategic focus
   - Towards an unique value proposition

2. Intellectual Capital Development Systems
   - Human capital = securing the best?
   - Centre for Wine Marketing and Product Development
   - International exchanges

3. Fragmentation (cost dis-economies/weak bargaining positions)
   - Producer owned structures (critical mass)?
   - Labels – too many
   - Concentration in the value chain?: Power of super markets; negociants – position of farmers

4. Market orientation
   - Market signals: from production driven to market driven (project)
   - Consumer preferences – selected segments

5. Technical innovation, R&D and funding, technology transfer systems
   - Vineyard management (yields vs quality)
   - Cellar management
   - Technology transfer – resource base
   - Link to "Brand SA": environment, social, style

6. Socio-economic considerations
   - Responsible alcohol consumption
   - BEE Transformation
Issues/Questions: Production factor conditions

1. Labour issues
   - Skills development
   - Social development
   - Political interface (unions/NGOs)
2. Attracting new talent and skills
3. Cost of doing business
   - Regulations
   - Legal compliance
   - Skills & competencies (Introduction of Wine-Online project)
   - Taxes
   - Crime factors
4. Water issues
   - Allocation: Scarcity & socio-economic priorities (Transformation Scorecard)
   - Waste water management
   - Water efficiency
5. Land availability
   - Can increase by 50% to 150,000 ha (water constraints)
   - Land reform impact?

Issues/Questions: Supporting systems

1. Technology transfer systems
   - Production (VinPro) → market orientation (Wine Foresight)
   - Cellar level (waste water issues/blending)
2. Value Chain consistencies?
   - CSIR study: Port facilities management
3. Certification labs
   - Bottlenecks
   - Integrity statements
4. Training & skills development systems
   - Focus areas: vineyard level, cellar level
   - Business
   - Marketing
5. Financial systems
   - Management of the fluctuation of the currency
   - Long-term funding support and investment
6. Glassware supply
   - Bottle shapes and sizes
   - Global competitiveness
**Issues/Questions: Government systems**

1. Applicability of policies: “Making wine work for all”
   - Land reform: ownership vs use; new models
   - BEE (Wine Charter & Scorecard)
   - Support systems
     - Trade policy and promotion
     - R & D
   - Legal reform
   - Policy coordination
   - International action (EU policy, etc)

2. Partnerships & cooperation
   - Wine Industry Strategy Plan (WIP)
   - SA Wine Council effectiveness (Representative voice)
     - WIP
     - Wine-BEE Charter & Scorecard agreement
     - Policies – R&D, trade, labour, natural resources
     - Management of political interface

3. Implementation/Coordination
   - Agri, land, water – new Agri-Plan
   - Industrial development plan
   - Trade linkages
   - Social development initiatives – land reform/evictions

**Issues/Questions: Chance factors**

1. Management of financial exchange rate fluctuations
   - Financial hedging? Financial systems
   - Risk management (Supply chain & consolidations)

2. Does the “Brand SA” image create space to exploit “chance opportunities”? (2010 FIFA World Cup)

3. Biotechnology development
   - R&D policy (experimentation protocols)
   - Commercialization issues (root issue)

4. Health in the winelands
   - AIDS
   - FASS

**Statement 7**

- How do you win in the wine business?
- How do you compete?

By understanding the future decision-making environment; by being **confident** about your views of the future.
“Winning comes from confidence. 
Confidence doesn’t come from winning. 
Confidence comes from hard work.”

(Vijay Singh, 2005)

Questions:

- How do Executives view the future?
  - indicators
  - expectations
  - prices
- On what do Business Executives base their decisions for the “next” phase?

SA WINE BUSINESS CONFIDENCE INDEX (Pilot survey 2008)

<table>
<thead>
<tr>
<th>Key indicators* (Weights)</th>
<th>Expectations (Next period)</th>
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<tbody>
<tr>
<td>Turnover (1.26)</td>
<td>Up Same Down</td>
</tr>
<tr>
<td>Net operating income (1.29)</td>
<td>Up Same Down</td>
</tr>
<tr>
<td>Employment (1.10)</td>
<td>Up Same Down</td>
</tr>
<tr>
<td>Capital investment (1.35)</td>
<td>Up Same Down</td>
</tr>
<tr>
<td>Economic growth in South Africa (1.39)</td>
<td>Up Same Down</td>
</tr>
<tr>
<td>Exports (1.17)</td>
<td>Up Same Down</td>
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<tr>
<td>General climatical conditions (1.24)</td>
<td>Up Same Down</td>
</tr>
<tr>
<td>Market share (1.0)</td>
<td>Up Same Down</td>
</tr>
<tr>
<td>Debtor provision for bad debt (1.17)</td>
<td>Up Same Down</td>
</tr>
<tr>
<td>Financing costs (1.17)</td>
<td>Up Same Down</td>
</tr>
</tbody>
</table>

* Before harvest: Oct/Nov
  After harvest: May/June (next year)

Statement 8

The wine industry is driven by fundamental market trends over the long run; and by prices in the short run.
### Scenario development and projecting future price movements?

Scenarios and assumptions (BFAP Macro-Economic Model – www.bfap.co.za):

1. Economic equilibrium through supply & demand responses

2. What will be, is largely based on what was
   - at least for the immediate future i.e. the historical future!

3. Exchange rate will depreciate over time –
   - US$10.50 in 2015


5. Consumption trends positive (endogenous in model)
   - based on population growth, economic growth, lower income groups
   - domestic & global

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### Wine

**Real Wine Prices (constant 2000)**

**Red Vines in Production**

**White Vines in Production**

- Good wine price
- Rebate wine price
- Distilling wine and grape juice price

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### Wine

**Good wine price**

**Rebate wine price**

**Distilling wine and grape juice price**

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### Wine

**Real Cabernet Sauvignon price**

**Real Merlot price**

**Real Pinotage price**

**Real Shiraz price**

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### Wine

**Real Chardonnay price**

**Real Sauvignon Blanc price**

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### Wine

**Real Cabernet Sauvignon price**

**Real Merlot price**

**Real Pinotage price**

**Real Shiraz price**

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### Wine

**Real Chardonnay price**

**Real Sauvignon Blanc price**

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### Wine

**Real Cabernet Sauvignon price**

**Real Merlot price**

**Real Pinotage price**

**Real Shiraz price**

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### Wine

**Real Chardonnay price**

**Real Sauvignon Blanc price**

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### Wine

**Real Cabernet Sauvignon price**

**Real Merlot price**

**Real Pinotage price**

**Real Shiraz price**

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### Wine
Statement 9

- Competitiveness is about sustainability;

- Sustainable competitive performance require trusted and productive strategic partnerships between:

  Firms, Industry and Government

Strategies to promote competitiveness

1. Industry level initiatives

   Strategic Focus:
   - Alignment between all major industry players in strategic direction: Review Wine Industry Strategy Plan (2003) and Vision 2020
   - Clarify image (“Brand SA”) and focus;
   - Create pressures for innovation (R&D, TT, Business structures)
   - Increase productivity (of scarce and costly factors: water, labour, land, capital)
   - Promote domestic rivalry

   Industry actions:
   - Attract new talent into the industry
- Upgrade the wine intelligence system (along the value chain; info flows)
- Seek quality/price improvements: time/place style requirements (alcohol content?)
- Upgrade industry integrity and certification systems: production systems (IPW); environment (BWI); flavouring traceability (wine making)

**Manage the political interface:**
- Commit to social responsibility and the vulnerable (Farm workers) – Linkages to wine image & Fair Trade
- Manage political interface: trade, social, technology, security, tax, labour through “One Voice” (representations)
- Manage politics and social transformation processes (Oversee Wine Transformation Charter and Scorecard)

## 2. Role of Government

**Industry Interface:**
- Focus on the Wine Industry Strategy Plan (WIP); Wine Transformation Charter; environmental agenda (IPW)
- Support funding of technological innovation, R&D, Environmental & Social development
- Support integrity systems

**Policy and regulatory interventions:**
- Enforce strict product, safety & environmental standards
- Promote a sustainable investment climate
- Fight crime (reduce cost of crime)
- Support international ‘Brand SA’ promotion; South Africa’s image
- Reduce regulatory and administrative costs (cost of doing business); improve bureaucracy
- Create a favourable trade environment and “playing fields” for SA wines vis-a-vis EU, USA, etc
- Safety nets for the most vulnerable

## 3. Firm/Enterprise level initiatives

- Create competitiveness culture in organisation
- Promote innovation (+ risk management systems)
- Develop business intelligence focus
- Clarify market focus and segment – country, style, price/quality
- Consider consolidation / cost reductions
- Upgrade value chain management participation
- Ensure a continuous learning culture: Skills development & training; attract new skills & talent
- Establish and manage a clear social transformation agenda: Quality of life of the most vulnerable people in the industry.

### CONCLUSION!

Competitiveness is about embracing opportunity. In South Africa, the 2010 Soccer Tournament provides the biggest opportunity to date to position South Africa as a producer of quality wines on a global scale.

Being a diverse product judged on intrinsic, uniqueness could give a wine producing country a competitive edge: Pinotage in South Africa, for example.
QUESTIONS ?