

# MACRO-ECONOMIC IMPACT OF THE WINE INDUSTRY ON THE WESTERN CAPE

## SUMMARY

### STUDY DONE BY CONNINGARTH CONSULTANTS FOR SAWIS (SOUTH AFRICAN WINE INDUSTRY INFORMATION AND SYSTEMS)

#### 1 RECENT DEVELOPMENTS

- Establishment of a new regulatory and institutional framework, involving *inter alia* KWV being divested of its statutory obligations to regulate the industry and transforming itself into a company.
- A marked shift in the local and overseas demand for wines in favour of quality red wines. The South African wine industry is unable to capitalize fully on this trend. A shift in the plantings towards red varieties has begun and it is foreseen that the supply shortfalls will be met in a few years time.
- On top of the structural changes, the industry also had to contend with a decline in the overall local demand for products of the vine over the past number of years. Possible reasons being the advent of cell phones, state lottery, casinos and slow increases in real disposable income per capita.

#### 2 MAIN ECONOMIC ATTRIBUTES

##### 2.1 TURNOVER

The total turnover of the wine and associated alcoholic-based beverages industry amounted to R7 369,8 million in 1999. Of that amount R1 595,9 million was from exports. Imports amounted to R500,6 million or  $\pm 8,6$  per cent of domestic sales. Put another way, primary agricultural output valued at R1 435,9 million was beneficiated and added in value downstream to the value of R7 369,8 million i.e.  $\pm 5$  times the initial value of the raw materials. In the process, income (consisting of the remuneration of both labour and capital) to the tune of R7 370 million was directly and indirectly generated in the RSA and overseas (via exports). Furthermore, it is estimated that an additional amount of R3 471,5 million was generated indirectly through tourism in the winelands.

Table 1 provides a snapshot view of the conditions in the wine industry in 1999. Taking into account the following trends it can be concluded that the

wine industry finds itself under pressure to remain profitable and competitive:

- Sharp increases in the average grape prices of noble varietals used to make wine;
- Producers' income increased by 16%, and total litres of wine produced rose by 1,6%;
- Production costs increased on average by 43%;
- The average price of good wine sold in bulk increased by 24%;
- The volume of exports increased by 29 %, and in value terms by 133%;
- Imports, in current terms, also increased;
- Wine and wine-based alcoholic beverages consumed declined by 5,7% in volume terms;
- The South African tourism industry flourished.

**Table 1 Economic structure and the flow of goods and services**

Market Segment Economic sector	Turnover added at each phase	Exports	Domestic Sales	Current import level	Potential Import source of business	Western Cape <sup>1)</sup> sourced production
<b>R Million, 1999</b>						
1 Primary Agricultural Production 2 Cellars		(148,4)				
Total Primary	1 435,9	148,4	1 287,5			1 435,9
3 Manufacturing Wholesale & Retail						
3.1 Manufacturing	2 254,8	743,4	1 511,4	250,3		2 004,5
3.2 Total Trade & Transport	3 679,1	704,1	2 975,0	250,3	953,6	2 475,2
Sub-total	5 933,9	1 447,5	4 486,4	500,6	953,6	4 479,7
<b>TOTAL (1+2+3)</b>	<b>7 369,8</b>	<b>1 595,9</b>	<b>5 773,9</b>	<b>500,6</b>	<b>953,6</b>	<b>5 915,6</b>
4 Tourism						
4.1 Foreign	9 35,1	935,1				935,1
4.2 Local	2 536,4		2 537,4			2 536,4
Sub-Total	3 471,5	935,1	2 536,4	500,6	953,6	3 471,5
<b>GRAND TOTAL</b>	<b>10 841,3</b>	<b>2 531,0</b>	<b>8 310,3</b>	<b>500,6</b>	<b>953,6</b>	<b>9 299,5</b>

<sup>1)</sup> Including Orange River Production

In comparison to 1997 figures, it shows that the industry has been under severe pressure due to the small increase in turnover in volume terms and steep increases in input costs not fully compensated for by final product price increases. Exports performed spectacularly, increasing by 29 per cent in volume terms between 1997 and 1999. In value terms there was a growth of 133 per cent.

The wine industry is still a major primary source of economic growth and development in South Africa in general but also for the Western Cape in

particular. Rough calculations showed that at least 50 per cent of the total turnover (excluding tourism) will be expended in the Western Cape. Viewed from another angle, it was estimated that if the primary agricultural supply of raw material should fall away, the level of business in the Western Cape would reduce to  $\pm 35\%$  of its present size.

More recent information again reconfirmed the important role the wine industry plays with regard to tourism. The attraction of the winelands for tourism is outstanding.

## **2.2 CONTRIBUTION TO GDP**

The wine industry contributes R14 557 million to the annual GDP of the country. Starting at farm level, the initial value of the raw material in terms of income (GDP) created, amounts to R443 million and ultimately leads to a total GDP value of R9 385 million (excluding tourism). This illustrates the exceptional ability of the industry as a creator of wealth. The primary agricultural sector has a high direct/indirect ratio of 3,0 compared to only 1,5 of the wholesale and retail sales sector.

However, the question is whether the wine industry contributes a fair and reasonable share to GDP per unit invested compared to other industries. The study showed that with a GDP/Capital ratio of 0,38 it is lower than the national average. Even though this is not a measure of the profitability of the industry it does signify that its capital "productivity" is slightly lower than the average for the national economy.

The wine industry, obviously, has its roots in the Western Cape. It is estimated that 60 per cent of the industry's activities have a direct impact on the Western Cape's economy. A rough estimate therefore shows that of the R14,5 billion of GDP that the industry creates, about R8,7 billion eventually would remain in the Western Cape to the benefit of its residents. In 1999 terms this would have amounted to approximately 9,7 per cent of the Western Cape's total Gross Geographical Product (GGP).

## **2.3 INCOME DISTRIBUTION**

A total household income of R9 763,7 million is generated by the wine industry. Of this 18,4 per cent or nearly R1 797,7 million is destined for the lower income groups of which a large portion is spent in the Western Cape. Coupled to the annual expenditure by farmers on production inputs, it is clear that the wine industry forms the economic backbone of the economy of many districts in the Western Cape.

The 18,4 per cent of household income generated by the wine and tourism sector combined, destined for low-income households, is slightly lower than

the average for the economy as a whole (19,2), again points to the fact that the wine making industry is slightly more capital intensive than other agricultural based industries.

## 2.4 EMPLOYMENT

The wine industry provides employment opportunities for 208 298 people including tourism. According to the Labour/Capital ratio it is obvious that the capital is applied more effectively regarding job creation as the ratio is slightly higher than that of the national economy. The average for the South African economy is 5,0 compared to 6,33 for the wine industry (excluding tourism). The relative labour intensiveness of the wine industry is specifically the result of the intensive labour production methods which are followed in the primary agriculture i.e. farming (ratio of 7,8).

It is significant to note that the wine industry directly and indirectly supports 159 952 job opportunities throughout the economy. The industry directly employs 103 800 people. The primary agricultural sector of the wine making process directly employs the most people, while directly and indirectly it is also responsible for 42,7 per cent of the 159 952 jobs generated by the wine industry (32,8 per cent of the grand total, including tourism).

**Table 2      Employment**

<b>ECONOMIC SECTOR</b>	<b>TOTAL</b>	<b>%</b>
<b>A PRIMARY AGRICULTURE</b>	<b>68 226</b>	<b>32.8</b>
Direct	55 218	
Indirect	13 007	
<b>B CELLARS</b>	<b>9 461</b>	<b>4.5</b>
Direct	3 455	
Indirect	6 006	
<b>C MANUFACTURING</b>	<b>32 824</b>	<b>15.8</b>
Direct	15 755	
Indirect	17 069	
<b>D WHOLESALE and RETAIL</b>	<b>49 442</b>	<b>23.7</b>
Direct	29 372	
Indirect	20 070	
<b>WINE INDUSTRY</b>	<b>159 952</b>	<b>76.8</b>
Direct	103 800	
Indirect	56 152	
<b>E TOURISM</b>	<b>48 346</b>	<b>23.2</b>
Direct	14 536	
Indirect	33 809	
<b>TOTAL</b>	<b>208 298</b>	<b>100.0</b>
Direct	118 336	
Indirect	89 962	

## **2.5 CAPITAL UTILISATION**

A capital stock of R11 176 million is required directly in the wine industry to sustain the present level of production/turnover of R7 370 million. Indirectly a further R14 088 million of capital is required in the supporting industries to sustain this level of production (excluding tourism).

The wine industry is probably more capital intensive than is believed. Although the primary agriculture portion of the wine industry is relatively labour intensive, the other portions of the industry (i.e. co-operative cellars and refining) are more capital intensive. On average the total industry (including tourism) is on a par with the economy as a whole.

## **3 CONCLUSION**

The South African wine industry has undergone major changes over the past 10 years, as largely reflected by the changes in its economic structure and institutional framework represented in the report. Its re-introduction into world markets has brought about huge opportunities, as reflected by the increase in exports, but on the other hand has also brought pressure on its competitiveness, both locally and overseas.

The wine industry's size and structure in terms of forward and backward linkages has been proved to be substantial. Its magnitude in terms of for example investment, employment and income generating activities, not only in the Western Cape, proves to be of crucial importance to South Africa's economic well-being. This is in terms of the contribution to the economic existence and well-being of lower income groups, especially on wine farms, demonstrating its vital social and development role, particularly in the rural context.

The industry has acknowledged the challenges that need to be addressed in a co-ordinated way to ensure its long-term financial viability. It will have to become more market-driven and will need to ensure its information requirements are met on a more regular basis.

The following table is a summary of the macro-economic impact analysis of the wine industry.

<b>Criteria</b>		
<b>Macro-economic indicators</b>		
GDP (R million)	14 557	
Total labour	208 298	
Total capital (R million)	38 263	
<b>Household income</b>		
Total (R million)	9 764	
Low-income groups (R million)	1 798	
<b>Effectiveness criteria</b>	<b>Western Cape</b>	<b>Total economy</b>
GDP/Capital ratio *	0,38	0,47
Labour/Capital ratio **	5,4	5,0
Low income/total income (%)	18,4%	19,2%
Income ratio	3,1	-

\* The GDP/capital ratio for the wine industry, including tourism is 0,38. It means that for every R1 invested, R0,38 of income (GDP) is generated.

\*\* Every R1 000 000 investment creates 5,4 jobs.

\*\*\* The total income ratio for the wine industry is calculated at 3,1. This means that for every R1 production-factor income generated directly in the industry, R3 will be generated throughout the economy based on its sectoral backward linkage structure.