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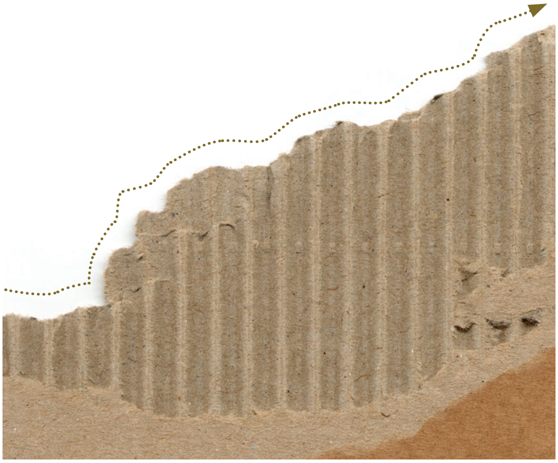

Trends influencing wine consumption globally and in South Africa in particular

PART 1

TRENDS INFLUENCING WINE CONSUMPTION GLOBALLY AND IN SOUTH AFRICA IN PARTICULAR

PART 1

Welcome to this edition of the quarterly newsletter as a value-added service to members of the S A Wine Industry. The purpose is to provide you, the decision-maker, with meaningful insight into events, trends, opportunities and threats through the analysis of the ever-changing competitive environment. The analytical approach is a multifaceted, multidisciplinary combination of scientific and non-scientific processes.

We trust that this publication will become part of your strategic thinking, strategic planning and decision-making process. You are welcome to send comments and suggestions to the publisher.

"We used to market wine to people like ourselves, who loved it and knew a lot about wine. Now, we're trying to learn what people want, what drives them to buy certain wines."

Karla M cKee, Trinchero Family Estates, California

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INTRODUCTION

The image of a traditional wine drinker has changed over time. Whereas once this was the domain dominated by the educated and wealthy, wine consumption is now enjoyed in all areas of society and wine of quality is more accessible to various market segments than ever before.

Historically consumers bought beverages for the basic needs of refreshment, rehydration and nutrition. However, in a global, hi-tech world filled with lifestyle choices there are many more sources of motivation including status, contentment, affiliation, release and discernment.

Having researched published media, it is clear that four factors or drivers in particular currently impact on wine consumption namely the global economic downturn, longer term trends such as moderation for health, expenditure reasons and, finally, product quality. The shift towards premiumisation and a higher value, lower volume consumption pattern is set to continue, but has lost momentum and is not forestalling the sales decline. Economic cycles can depress and alter demand. As a discretionary consumer product, wine is at risk of suffering decreases in demand during period of weakness in the economy. The elasticity of demand for premium wines in particular has been a concern for producers, since these higher-priced products can be easily replaced with cheaper wines or other beverages. However, so far, wine demand has stayed strong despite recessionary conditions.

Health is indeed one of the most significant trends influencing CPG (consumer packaged goods) brands at present and this aspect will be discussed in more detail in this report.

Price and value-for-money are growing as influencing factors in what drinkers consume, where they consume and in what volume. The negative economic backdrop has clearly been a major motivator in this, and has further favored the off-trade over the on-trade.[1] This shift in alcohol sales from the on-trade to the off-trade reflects a trend predating the global economic downturn.[2] The rise and rise of the New World is one reason why the quality of branded wines has improved, too. Facing intense competition, the Old World has adapted and as the result is an on-going transformation of European warm climate areas, such as La Mancha, Sicily and the Languedoc-Roussillon, which were previously dismissed as suitable only for lowly bulk production Its marketing and branding have improved too, to embrace an element of fun and self-mockery.

This edition of VinIntell focuses on how these drivers that give rise to wine consumption patterns globally and in particular in South Africa lead to certain discernable trends. The main trends affecting wine consumption trends as well as a number of sub-trends will now be discussed.

MAIN TRENDS IMPACTING ON CONSUMER CHOICE

The main trends impacting on consumer choice are health, convenience and indulgence / premiumisation.[3] These main trends are underpinned by eight inter-related subtrends namely wellness, pace of life, demographics, authenticity, ethics, sophistication, exclusivity and value.

Each of these trends and sub-trends has implications for understanding consumer behaviour and making product and market-

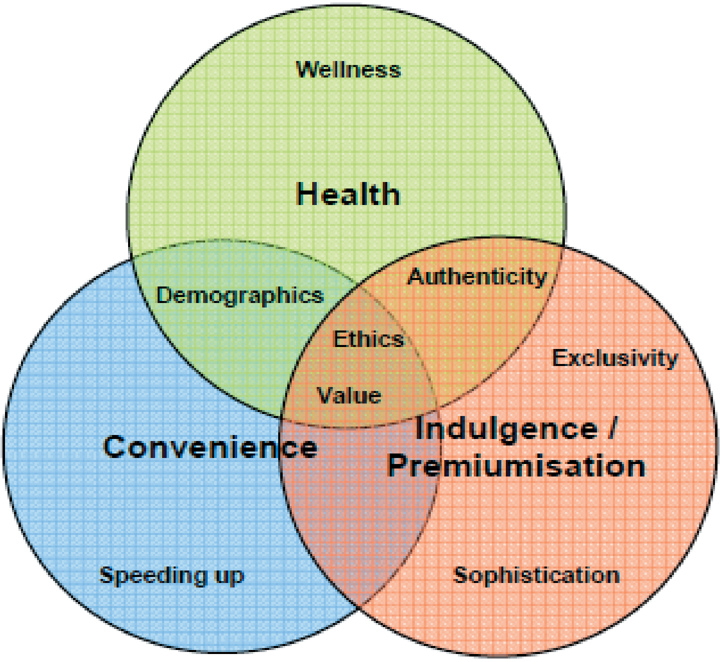

FIGURE 1: Interrelation of 11 key consumption trends
Source: just-drinks.com and Australian Wine and Brandy Corporation (AWBC)

ing decisions. The value of a product has less to do with how real a product's value may be, than with the value perceived by the consumer. Wine brands that can incorporate solutions to these mega-trends and sub-trends are likely to have higher perceived value and positioning than those that do not and can charge higher prices.

The mega trends are not always complementary (many indulgent products can be far from healthy), yet consumers increasingly are seeking products that deliver all three. At the aggregate level, health is the trend leading the strongest volume and value growth in the off-trade, for both alcoholic and non-alcoholic beverages (see figure 1).[4]

1 Health and food safety

Health as a main trend has as sub-trends wellness, demographics, ethics and value and authenticity. Health remains one of the most significant mega trends across the beverage and food industry, driven primarily by rising obesity in especially Western countries and concerns about binge drinking by young adults. This trend is expected to continue in the medium term as governments and industry raise awareness about the issue and the

UK government in particular is active in this regard. The consumer focus on health is also highlighted by the growth of products such as organic foods, dietary supplements and energy drinks.

Wine is best placed of the main alcohol categories to capitalise on the health trend and regular moderate wine consumption has often been linked with health benefits. Moderate consumption, particularly of red styles, is associated with a reduced risk of cardiovascular disease and stroke, and this is increasingly well promoted. In some traditional wine markets, including Spain and France, consumers are turning away from alcoholic beverages, although this is in part also driven by other issues such as stringent legislative regimes and rising taxes on alcohol.

Positive health messages can certainly boost sales. For example, the revival of the distilled alcoholic beverage Shochu in Japan since 2003, particularly among younger consumers, is attributed to publicity about its supposed health benefits, including more rapid renewal of skin cells, prevention of blood clots and reduction of heart attacks and strokes. It is generally accepted that moderate consumption of wine is beneficial to health, but it is still not clear how much the alcohol and the non-alcoholic compounds in the wine contribute to these benefits.[5] Some obvious advantages include reduced risk from alcohol-related diseases, reduced calorie intake, benefits for pregnant women, and advantages for consumers who, for religious or health reasons, cannot consume much alcohol.

The industry has adapted further to this trend and lower alcohol wines have already seen some success. There is momentum in the trade towards lower (as opposed to low) alcohol wines. Research in the UK suggests consumers are wary of lower alcohol wines, however, although it is thought this is in part driven by value for money concerns rather than stylistic considerations. In South Africa, South African consumers have shown a growing demand for lower-alcohol wines, but there continues to be some resistance to alcohol-modified wines, with the idea that their palatability is inferior to standard wines,

Shochu drink being mixed.
Source: The Washington Post, 5 May 2010

even though advances in production methods have lead to a general improvement in quality.[6]

Among the impacting factors on health and environment consciousness are also the following: Concern regarding energy and electricity is by far the most important contributor to the industry's carbon footprint. This is due to the fact that Eskom, the sole electricity supplier, is coal-based and therefore emits large quantities of greenhouse gas emissions, which overshadow most other carbon footprint contributions. Nitrogen-based fertilisers also prove to be significant contributors to the carbon footprint of the industry's producers, due to the high global warming potential of nitrous oxide, a bi-product of the breakdown of nitrogen-based fertilisers. Finally, the production and usage of packaging materials is shown to contribute to the carbon footprint of both wineries and pack houses, particularly where the use of non recycled plastic packaging is concerned.[7]

2 Convenience

Key sub-trends in terms of convenience are demographics and "speeding up." The fast pace in most markets and therefore the demand for fast food and drink options is expected to continue, driven by the pace of business, an ageing population, the growth of single-person households and more women in the workforce. In a recent US survey, for example, 55 percent of respondents said they prefer to spend less than 30 minutes preparing the day's main meal, while 9 percent take less than five minutes. Increasingly consumers also are looking for portability, value and nutritious products as well as speed and food and beverage manufacturers are aware to this trend. In the UK the consumption of convenience food continues to rise. There was a 300 per cent increase between 1997 and 2008, according to a UK government report. Research also revealed that there has been a 20 percent reduction in time spent eating at home, yet the time eating out averages 25 minutes per day mostly spent in fast-food outlets.[8 9]

This speed and convenience needs are being exploited in various manners. In terms of packaging there remains room for innovation in convenient packaging, such as the screw cap and soft pack variations, particularly in markets with existing low penetration for soft packs (see VinIntell August 2010 Issue 6 on trends in packaging). Consumers prefer the convenience and the perception of zero waste, despite higher costs, highlighting the need to straddle a number of consumer motivations to justify higher pricing. Single serves also facilitate trial more readily, which is critical in markets without a wine culture and here packaging also plays an important role.

The demand for convenience also is reflected in the investment by multiple grocers in convenience stores and petrol station forecourts. In South Africa, retailers like Woolworths and Pick n Pay have opened convenience stores in joint ventures with Engen and BP. These outlets tend to skew towards well-known brands.

Technology has also come into play. Something new is on the menu at a renovated Starbucks in Seattle (US): beer and wine. It is the first under the Starbucks brand to offer alcohol. Craft beer and local wines go on sale after 4 p.m. The idea is to offer drinks and a wider variety of savoury food that will attract customers after the morning espresso rush. The particular store also includes a circular coffee bar that brings customers closer to the baristas.[10]

Seattle Starbucks outlet.
Source: Huffington Post, September 2010

Industry experts argue that there will still be a place for iconic wines that represent the pinnacle of wine production, but add that most wines are made with more immediate consumption in mind. People with more modest budgets can drink good wines that fit their taste preferences; and there is probably a writer, reviewer, blogger, retailer, or importer who alerts the market to new discoveries. The world of wine is wide open in terms of the viability of and access to information and therefore the market is far more enlightened and empowered.

3 Indulgence / premiumisation

The sub-trends under one of the main trends indulgence and premiumisation are sophistication, exclusivity, authenticity, ethics and value.

Indulgence / premiumisation is a newer consumer phenomenon and is expected to grow rapidly in the medium term as consumers seek to compensate for feelings of anxiety and insecurity (arising from increased awareness of terrorism) and make use of their rising incomes (assuming no external economic shocks) and increased leisure time. Experts expect the shift towards premiumisation and a higher value, lower volume consumption pattern to continue. However it has lost momentum and is not forestalling the sales decline. As illustrated in figure 1, indulgence is affiliated with the sub-trends of Sophistication, Authenticity and Exclusivity.

Wine is better positioned than many other beverages to participate in the indulgence trend, but to date, hot beverages (coffee and tea) have been the most successful. Coffee has evolved from a staple to a gourmet beverage, assisted by specialty retailers such as Starbucks in the US and in South Africa by any number of coffee shops, providing coffee alongside lifestyle branding for the image conscious. Non-alcoholic beverages offering additional benefits, such as espresso coffee, herbal teas and organic smoothies, may be perceived as a threat to wine consumption, with consumers willing to pay a purchase premium.

Fruit smoothies.
Source: Preferred Entertainment.com

Coffee culture.
Source: Tribune India.com

Some table wines, sparkling wines and luxury spirit brands are considered indulgent, although in some instances this is due to the product's price positioning rather than its inherent values. The positioning of wine as a beverage to be shared makes it a leading choice for indulgent occasions hence the fit with a coffee type culture.

However, indulgent needs are often individual, requiring a single-serve offer. Champagne and sparkling wine producers have best captured this trend. Wine will become more mainstream if the elitist element is neutralised and if smaller wineries and lesser known wines gain access to the market. By promoting the efforts of regional winemakers and relatively unknown regions of popular wine producing countries, more people will open themselves to trying wines from all over the world.[11]

SUB-TRENDS

The eight recognised sub-trends that are discernible under each of the three main trends are wellness, speeding up, demographics, authenticity, ethics, sophistication, exclusivity and value. The first three of these i.e. wellness, speeding up and demographics, pose the greatest challenges for the wine sector with respect to new product development.

1 Wellness

The growth of the wellness industry reflects a consumer focus on improving life balance. There are increasing numbers of products and services that claim to improve health, reduce stress and help consumers enjoy an enhanced quality of life. In the food and beverage industry, this trend has given rise to enriched drinks (juices and waters with added vitamins and minerals), nutraceuticals (products with added ingredients targeted at specific medical or health benefits), sports drinks and energy drinks. Enriched drinks have emerged from health foods shops and pharmacies into mainstream retail outlets. Most new offerings of enriched drinks or nutraceuticals are non-alcoholic beverages.

Examples of enriched drinks: activate.
Source: Activate Drinks.com

Chateau Mercian label.
Source: Château Mercian website, October 2010

Brewers and Japanese drink producers appear to be the most proactive in developing alcoholic beverages. Carlsberg has developed Karla, a low-alcohol (1 percent) blend of beer, fruit juice and vitamins.

The Japanese appear to be leading the way in functional wine beverages; for example, Mercian has started adding gamma-amino butyric acid (the chief inhibitory neurotransmitter in the vertebrate central nervous system) to table wines to further help drinkers relax.[12 13]

Most new sports and energy drinks also are non-alcoholic beverages although brewers and alcopop producers, noting an on-trade opportunity, have entered the market. Both Anheuser-Busch and SAB-Miller have introduced caffeine-enhanced beers, containing such additives as ginseng, guarana and taurine, and alcopops such as Red Square Reloaded (vodka, caffeine and taurine) are available.

Carlsberg's Karla beverage.
Source: trendwatching.com

Energy beer from Anheuser-Busch containing ginseng, caffeine and guarana.
Source: Anheuser-Busch

2 Life in the fast lane

The current technology and efficiency driven society is creating consumers who expect 24/7/365 access to goods and services, meals on the run, and products and people that can multi-task. In the food and beverage category this has resulted in the evolution of sports and energy drinks (as highlighted above) and in the growth in online sales as retailers begin to focus on multichannel retail strategies, particularly the multiple grocers.

Retailers are increasingly using the online environment, catalogues and convenience stores as additional channels to connect with the consumer and meet their diverse delivery needs. In the UK, the grocery multiples, such as Tesco, are using the online channel as a tool to manage their growing wine clubs, for example. Purchases are by the case and a broader product selection is offered, including internet exclusives. This is providing opportunities for producers with smaller (and sometimes higher value) parcels to transact with the grocery channel.

3 Demographics

Two major trends are expected to influence wine industry performance over the next 10 years namely the ageing of the population base and the rise in single-person households.[14] In the period to 2011, the ageing Baby Boomers (those born roughly between 1946 and 1964) should positively impact on wine sales. However, beyond this period growth challenges are likely to present themselves. The 20-something age group market (those born between 1975 and 2000 and known as Generation Y, Millennials or the Internet generation[15]) is not expected to grow for the next 20 years. Pitching alcoholic beverages to this population group will become more competitive and most probably expensive and will have to be sold differently to the previous generations. However, engaging them is critical.

Globally the percentage of traditional households is expected to fall and beyond that single-person households are expected to become dominant in especially the maturing markets. There is also an expectation that these will be dominated by females, many elderly. Assuming this portion of the population continues to consume alcohol, in particular wine, this may require packaging alternatives that are lighter (easier to carry) and offer single serve options.

4 Authenticity

Modern consumers are overwhelmed with information and choice. For many, the response is a greater interest in authenticity and real products and experiences. This is reflected in the rise of farmers' markets and the growing popularity of organic foodstuff in South African and in other markets like the UK. Wine is well positioned to exploit this trend (as it ties in closely with the health trend) given its strong agricultural base, the large number of small producers and proximity of viticultural areas of the Western Cape in particular to major metropolitan regions.

In the last years the market for organically produced wine has developed significantly although hard market data is still wanting.[16] According to a study carried out by the International Organic Accreditation Service, Letis[17], organic wine consumption on the world market still maintains its growth margin in 2010 despite the recent years of economic downturn. Canada seems to be the market with the greatest growth potential for this type of wine, which is made using organic agriculture. In addition, the US, most

European countries, and Brazil have all registered continuous growth in consumption. Germany, the first country to invest in organic wine production, is, together with France and the UK, one of the countries which generates most profits from this type of product.

The authenticity trend is expected to be sustained medium term. It ties in with growing consumer sophistication and health. From a marketing perspective it demands a return of the winemaker as hero but the wine-making process will be under scrutiny.

5 Ethics

Ethics is inter-related with all three mega-trends and closely aligned with the demand for authenticity. Consumers increasingly want reassurance with respect to environmental and social responsibility and accountability including fair labour practices. A tangible reflection of this is the growth of FAIRTRADE goods (www.fairtrade.org.uk). This movement is turning mainstream. From a wine perspective, South Africa, Chile and Argentina are best placed to take advantage of this trend. In South Africa, the Agricultural Ethical Trade Initiative of South Africa (WIETA) operates in the broader agricultural sectors and focuses especially promoting fair standards of employment. Its members include a significant number of South African wine producers, retailers, trade unions, non-governmental organisations and the government and cut flower and deciduous fruit growers.[18]

Ethics as a sub-trend is driving a number of changes within the wine industry. These include the following:[19]

- Considerations about whether to package in the country of origin and potential re-engineering of supply chains (for example, the UK WRAP initiative is focusing on educating the trade with respect to the economic benefits of lightweight bottles and bulk importing to reduce the volume of non-recyclable green glass in the UK market).
- Enhanced use of environmentally friendly packaging.
- Brand marketing programs with a commitment to environmental programs and promoting fair labour practices.
- Highest labelling standards.

6 Sophistication

Sophistication is a part of indulgence, and in the case of food and beverages this is provided in part by the use of exotic and premium ingredients and flavours. This is clearly seen in the growth in the gourmet and specialty food and drinks markets. A recent Business Insights report shows that 28.5 percent of new alcoholic drinks launches are targeted at gourmet or specialty markets. This is more than double the share in 2001. In the wine category, the quest for sophistication is revealed in developing consumer interest in new wine styles and new regions. For instance, in some markets like the UK interest in aromatic light white styles such as Sauvignon blanc, Pinot Gris and Viognier has been a leading driver of growth. Sophistication is positioned as one of the more accessible sub-trends for the wine sector.

Together with sophistication comes the need for real-time information and advice on cultivars, food, health aspects etc. The messenger; whether it is the internet, the local retailer or another news source, has become the brand for sources of wine information. This growth pattern of sources opens up access to a wider range of interests and opinions. This is an indicator of a growing market with an interest in what is consumed.

Taking a cue from this trend software developers are rolling our products that aim to provide real-time product information to consumer. Their premise is that most wine drinkers do not buy wine by region, year, or cultivar but by label (equating that with a finely crafted wine). In hits regard, Snooth.com developed a new iPhone app that allows consumers to browse by aesthetics alone. According to their website, you simply take a picture of a label of a wine you're enjoying, and it will tell you where you can go to a buy it.[20]

Another example is the Food & Wine magazine's iPad app. For the app, Food & Wine reimagined 95 percent of the magazine's content. iPad owners can download the wine issue for free and cover the following special themes: holiday, healthy foods, travel, and chefs. Users can click on each wine, see the photo, and see what dishes pair with it. Then, they can click through to the recipes.

The impact of this trend from a consumer viewpoint is that this has also changed the future of food journalism because wine and food are so connected. Everything could intersect in the future: The print version, then the TV show, and the additional behind-the-scenes footage for the app. Users are commenting and blogging and it not just TV in

Wine product information application (app) for iPhone.
Source: snooth.com

Online magazine app for iPad.
Source: Food and Wine Magazine

that there is someone talking at you and you can't talk back. It's not just print where you read something and you have no interaction. It is all about being accessible, drawing people in, and building a whole community around it.[21]

7 Exclusivity

Running parallel to the wealth creation trend that has taken place through the 1990s and 2000s is the concept of mass prestige luxury goods. As defined in book Trading up: the New American Luxury by Michael Silverstein and Neil Fiske, these products "are not always the most expensive items in the category, nor are they always the top of the line for the brand. They always sell at a premium to conventional goods, but are always affordable by the middle-market consumer".[22]

As luxury goods become more accessible and larger, higher income consumers are again seeking to set themselves apart (aspirational, individualised and exclusive). This is leading at one end of the spectrum to personalised product offerings by the high-end luxury goods manufacturers, and at the other to mass customisation. Personalised drinks are not a new phenomenon and consumers appear willing to pay a premium for drinks that are tailor-made to their specifications.

Although wine seems well positioned to leverage from the exclusivity trend, it is proving difficult to execute, for brand owners and retailers alike. This may be attributable to price being the key marketing tool currently used by the trade. The US is the standout market where wine has benefited from this trend and where Foster's Group launched the Penfolds Grange VIP Club, a 24/7 members-only concierge service that includes access to exclusive evenings with contemporary wine raconteurs. Initiatives such as these assist in reinforcing the brand ladder.

In the same vein, winemakers have become revered personalities and producers have cult status. The vineyard and origin of the wine have diminished and played second fiddle to the personality of the winemaker. Despite industry consolidation that has affected the number of large wine producers in the last three years, new independent wineries are opening continuously and this provides impetus to the exclusivity trend and the need for a unique selling point. These small boutique wineries provide the increasing variety of wines that consumers demand.

8 Value

A research report by the Australian Wine and Brandy Corporation (AWBC) in 2009 found that the demand for premium products and services is creating a convergence of expectations with respect to value and consumers are demanding value across the pricing spectrum, not only in the higher pricing ranges. This is a global phenomenon and has been reinforced by leading grocery retailers lowering operating cost structures in order to enable Every Day Low Pricing (EDLP). The growing power of the multiple grocers in liquor retailing internationally (where legislation permits) has seen such pricing strategies impact on wine retailing and marketing. There is a danger that wine could become regarded as a commodity, damaging its quality reputation. Research has shown that the global recession has changed the mind sets of wine consumers in South Africa as well and they have now changed their buying habits and now look rather at the value of the wine rather than the pedigree of the wine.[23]

Leading retailers in South African and elsewhere in the world have combined information technology with distribution efficiencies to drive down costs as a percentage of sales. EDLP is now taken as a given by consumers and they often want more. As a consequence, retailers not only seek to improve internal cost efficiencies, they also require improved pricing and margins from suppliers. Price differentials are a major driver of store choice for consumers globally and, as a consequence, this focus on pricing pressure is not expected to abate. The focus on lower pricing is also spreading to some on-trade environments e.g. pubs in the UK. Generation Y, the next generation that wine producers must focus on, are particularly driven by good value for money.

Large retail chains will continue to grow at the expense of independent retailers. Wine is becoming more established in supermarkets and therefore more accessible to more people.

Part 2 to follow in February 2011. The focus is on the impact of these trends on growth and markets.

ENDNOTES

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