The Impact of Liberalisation:

Communicating with APEC Communities

Wine Industry in New Zealand

November 1998

STUDIES IN APEC LIBERALISATION

Acknowledgments

In Vancouver in November 1997, APEC Leaders and Ministers requested that work be undertaken to promote community understanding of the impact of liberalisation. A broad project was conceived by a Steering Group established under the APEC Committee on Trade and Investment (CTI).

This series of papers, “The Impact of Liberalisation: Communicating with APEC Communities”, was prepared as part of the broader initiative. The papers include a review of research on the effects of liberalisation, a series of case studies and a summary report.

The publication series was implemented jointly by a consortium of the APEC Study Centres Network and the Pacific Economic Cooperation Council (PECC) under a contract from the APEC Secretariat. Project managers were Alan Oxley, Director of the Australian APEC Study Centre, and Christopher Findlay, Chair of PECC’s Coordinating Group and Associate Professor of Economics at the University of Adelaide, with the support of PECC Director General, PC Leung.

The author of this paper, *Wine Industry in New Zealand*, is Mia Mikic, Senior Lecturer, Department of Economics, The University of Auckland, New Zealand. The author would like to thank Joel Aurisch, Geoff Sanderson, Philip Gregan, and John Gilbert for their contributions and comments.

The Summary was prepared by David Uren.

The reports were produced at the Australian APEC Study Centre at Monash University in Melbourne, Australia. Publications were coordinated and edited by Jo Bosben, Assistant Director, Australian APEC Study Centre. Design and print production was done by Lazy E Dude Ranch.

November 1998

APEC #98-CT-01.5

ISBN 1-876238-15-1

APEC Secretariat

438 Alexander Road 14-61/64, Alexander Point Singapore 119958

Contents

Summary

In 1993, the award for the "World's Best Sauvignon" wine went to a small New Zealand vineyard, Jackson Estate, with just four employees. It was an achievement both for the company, and for the New Zealand wine industry .

The industry has developed a reputation for producing quality wines, particularly sauvignon blancs, over the past ten years. New Zealand wines sell around the world but Britain is its largest market, taking two thirds of its exports.

New Zealand's reputation for quality is evident in the fact that its wines achieve a higher unit value than any other exporter into the British market. New Zealand wine fetches an average GBP5.14 a bottle in Britain, while the nearest competitor is GBP4.64 a bottle.

The success of New Zealand winemakers in world markets is relatively recent. Exports were negligible until the mid-eighties. The industry had developed behind prohibitive tariff barriers supplying the domestic New Zealand market with relatively low quality wine.

Commercial development of wine started in the sixties, although a number of companies had been producing wine successfully for longer. Like most New Zealand industry at the time, wine production was heavily protected.

The wine industry became the subject of particular government attention in the late seventies, when it was decided special support was warranted to help the domestic industry earn foreign exchange itself, and save foreign exchange by import substitution.

A complex structure of composite tariffs, tariff quotas and a tariff threshold was introduced that had the effect of making imports of cheap wine prohibitive. New Zealanders were not, at the time, sophisticated wine drinkers and cheaper wines comprised the bulk of the market.

Domestic producers started to expand and there were also some first forays into the medium and higher quality ends of the market. The industry had established a representative body, the Wine Institute of New Zealand, in the mid-seventies.

The industry was then, as it still is today, composed of a few medium sized to large producers, and many small boutique producers. The membership of WINZ in 1998 comprises 293 wineries, of which 17 are medium scale and only four are large.

The institute's assessment of the industry in the late seventies was that it was not sustainable. The domestic market was too small and transport costs were too high. A development plan, geared at exports, was devised covering the period 1981-1986.

Production of grapes grew more rapidly than did the markets for New Zealand wine and, by the mid-eighties, there was a grape glut that threatened a number of wine companies – both big and small – with bankruptcy.

A scheme was introduced in the 1985 to subsidise vineyards to remove grapevines. This accelerated a shift in the market position of the country's wine production towards higher quality produce. The percentage of the crop accounted for by the cheaper Muller Thurgau variety declined from 37.9 percent to 13.5 percent between 1986 and 1998.

At the same time, a significant reform in tariff policy started to take effect. The specific tariffs of 68 cents a litre, which penalised cheaper imports, were phased out, and replaced with an ad valorem tariff which was to be cut at a predetermined rate from 25 percent in 1990 to 5 percent by 2000. Tariff quotas were removed. The exposure of the domestic wine market was increased by the establishment of a free trade area with Australia which enabled Australian wine to enter New Zealand duty free.

Imports started to rise. From 2.8 million litres in 1986, which represented just 6.5 percent of New Zealand's wine consumption, imports soared to a peak of 32.7 million litres in 1994, which represented just under half domestic consumption. The domestic wine producers have won back a portion of market share since then, but imports still hold 40 percent of the market.

The New Zealand wine market has grown since the mid-eighties, however virtually all of that growth is accounted for by imports. Australia increased its share of New Zealand wine imports from 36 percent in 1988 to 72 percent by 1997. Imports also increased from European suppliers such as Italy and Spain and Latin American suppliers including Argentina and Chile.

The growth in imports has been more than offset by a surge in New Zealand's exports. Although, in volume terms, the country imports significantly more wine than it exports, the high value of New Zealand wine means that the country has, for the first time, started to record a trade surplus in wine. The total volume of wine production has shown a modest increase over the last ten years, however the average value of wine has increased dramatically.

One of the pioneers of New Zealand's wine industry, the publicly listed Montana Wines, illustrates the change in the profile of the industry. Founded in the forties, it was a volume driven producer until the late eighties. Since then, it has concentrated upon building profitability by developing quality and high value wines. Although it still sells cheaper wines, it imports them.

The shift involved a geographic relocation of its vineyards to grow more desirable grape varieties. The company established strategic production alliances with the French winemakers, Deutz and Cordier and, through them introduced new production techniques and products into the New Zealand market. It has also invested in its own research and development focusing on improving the quality of grapes by advancing environmental protection practices.

Montana Wines has also been sophisticated in its approach to marketing, including collaboration with Italian brand designers that have resulted in design and packaging awards for the brand wine, Azure Bay. The company had sales of $141 million in 1997, of which $31 million was derived from exports.

One of the first New Zealand wine companies to start marketing sauvignon blanc in the United Kingdom was Hunter's Wines, based in the Marlborough area. It entered export markets using mail-orders, with momentum building after it had won some international awards for its wines. It also produces some mid-range wines which are an essential category to gain entry to supermarket sales. A small business with 35 staff, Hunter's has contracted in advice, including the senior wine adviser to the French company Moet & Chandon. It invests in research and development to improve its vines and has won ISO accreditation for quality.

At the small boutique end of the market, Jackson's, which started business in 1987, had a strategy of growing only the best quality of grapes. It makes extensive use of outside contractors, including for winemaking, bottling and labelling, storage, excise tax compliance, wholesale marketing and distribution. This enables it to focus upon growing grapes. It retains control over its wine production, retaining an internationally renowned winemaker to supervise production. Its export sales, which are handled through distributors, now exceed its domestic market.

The industry still has its challenges. The number of small producers has doubled, so it is a difficult battle for market share. Despite a far-reaching liberalisation of licensing laws and a much greater sophistication in wine appreciation, New Zealand market has not brought growth to the domestic producers because of the 40 percent share taken by imports. However the industry's positioning as a producer of premium quality wine for niche markets still promises export growth.

Background

The story of the New Zealand wine industry is that of an "ugly duckling". It has transformed itself from an inward-looking industry producing cheap and bad quality wines, into a dynamic global competitor that regularly wins top international awards for quality and design.

The wine industry of New Zealand is considered small from the national economy perspective. Its contribution to GDP, total merchandise exports and employment is still under 1 percent. However, since the mid-eighties, this industry has experienced a dramatic change in policy. It has become more open to world trade and investment. These policy changes have led to adjustments which have advantaged consumers while at the same time creating new opportunities for producers.

There have been some big achievements.

- Twenty years ago, less than 1 percent of the industry's production was exported. In 1998, close to 26 percent of produced litres of wine were exported.
- In late 1970's, only 4 percent of domestic consumption of wine originated from imports, in 1998 almost 40 percent of consumption was imported.
- In this 20 year period, the number of wineries has more than doubled, each producing a number of new varieties with greatly improved quality.

The main features of the industry include its youth; small scale operations with relatively high unit costs; a distinctive "green and clean" image; and a focus on high quality wines.

In the 1960s, the commercial production of wine was limited to the distant regions in which wine making originally started: West Auckland and Hawkes Bay. By the 1980s, the industry featured two contrasting types of producers: large scale and boutique companies.

The Wine Institute of New Zealand (WINZ) was formed in 1975 as a self-regulatory and representative body of the industry. By 1998, the WINZ membership increased to 293 wineries, but still with 4 large scale and only 17 medium scale producers.

One of the first actions undertaken by the WINZ, between 1981 and 1989, was development of a strategic outlook for the industry. On the basis of this study, the Industries Development Commission produced "The Wine Industry Development Plan to 1986" (WIDP). The central message of the plan was that the industry as it was structured at the time was not sustainable. The study recommended restructuring towards export expansion in order to overcome the smallness of the domestic market. The study further recommended development of pre-

The main features of the industry include its youth; small scale operations with relatively high unit costs; a distinctive "green and clean" image; and a focus on high quality wines.

The focus of the industry has changed dramatically from being an import substituting industry to exports oriented.

mium wine production to offset relatively high transport costs.

Assistance to the proposal was delivered predominantly through trade policy. Even so, the plan helped create distortions such as the grape glut in the mid-eighties. The grape oversupply marked the beginning of a turbulent period for the industry. It went through extensive restructuring based on the so-called Grapevine Extraction Scheme of late 1980s, which provided financing for pulling out 1,517 hectares of vines. Combined with overall liberalisation and deregulation, this restructuring of the resource base enabled the industry to become internationally competitive.

The focus of the industry has changed dramatically from being an import substituting industry to exports oriented. Between 1991 and 1996, the volume of wine exports grew at just under 10 percent a year. The value of exports grew even faster, at 16 percent a year. Volume and value of wine exports in the period 1991-96 were 9.8 percent and 15.8 percent, respectively.

The industry is now becoming globally oriented. Consequently, import competition is no longer viewed as threatening. The number of wineries has doubled throughout the 1990s. Competition comes from imports as well as from domestic companies.

The growth of the wine industry has had a number of other important effects which are relevant to social and economic policy goals. It has contributed significantly towards the diversification of agriculture-based exports. The impact of the expansion of the industry has been felt on government revenues because the duty on wine has been steadily increasing over the past decade. The growth of industry was credited with having a positive social impact by allowing alcohol consumers to acquire more sophisticated and more socially acceptable drinking habits.

Policy review

There are four distinct phases in the development of the wine industry with respect to government policies and their impact on competition in the industry:

- *Phase of passive protection* – period from the establishment of the industry until the late 1970s;
- *Phase of "picking winners"* – period preceding and including the Wine Industry Development Plan, from the late 1970s to 1986;
- *Phase of restructuring and early trade liberalisation* – period of the grape extraction scheme and trade liberalisation, from 1986 to 1990;
- *Phase of committed liberalisation* – period of the continued trade liberalisation and deregulation, from 1990 to present time.

The wine industry has had solid protection from its early days. Tariff rates on wines (expressed as specific tariffs) before WWII included most-favoured nation (MFN) rates, British Preferential Tariff (BP) rates, and special preferential rates to Australia and South Africa

In the late 1970s, the industry was "hand picked" for an assessment by the Industries Development Commission (IDC) which marked a period of special attention by the government.

The industry however did not win everything it wanted. For example:

- Distribution was not fully deregulated;
- Import of grape juice was banned, despite industry requests for access to supplies depending on seasonal conditions. This was done on the grounds that local wine quality of wine would be diminished; and
- The level of protection granted was not as high as demanded.

Under the plan, wine was exempt from import licensing, but was made subject to a complex tariff structure featuring tariff quotas, a tariff threshold and composite tariffs. The structure included:

- Tariff quotas (global quota restricting value of wine imports and a separate one for Australia);
- A tariff threshold of $2.00 per litre f.o.b.: when the world price was less than the threshold a penalty was applied – combined specific and ad valorem duty.

The above protection structure translated into the following ad valorem equivalent tariffs:

- Inside quota 35-40%;
- Outside quota 65-70%;
- Tariff rates were effectively many times higher again when world prices fell below the threshold.

It is important to note that in New Zealand the supply of domestic wine consisted mostly of cheaper varieties. Deliberate setting of high combined tariffs on cheap imported wines was expected to result in imports of cheap wines drying up, thus leaving room for domestic expansion. It was hoped that the elimination of imports would 1) allow time for the industry to restructure, and 2) trigger the production of medium-to-high quality wine varieties. The implementation of the plan, however, resulted in the overplanting of cheap grapes and led to the grape glut of the mid-eighties.

In late 1985, the Labor Government announced the Wine Industry Assistance Package, offering a cash grant for the extraction of grapevines amounting to $6,175 per hectare. By 1990, vines were pulled out of 1,517 hectares and the resource base of the industry was significantly changed so that grape varieties used in the production of cheaper wines became less represented.

While officials judge this intervention by the government as a success, others within the industry claim that the scheme had an adverse effect on the industry's development because it 1) permitted much slower restructuring, and 2) prevented exit of the less efficient and poorly managed companies by providing them with an extra cash flow.

Table 1: Changes in tariffs on wine imports, 1986 – 1998

Date (as 1 July of)	Specific tariff (cents / litre)	Ad valorem tariff (%)	Imports in mil litres	Imports as % of total consumption
1986	68	20	2.792	6.5
1987	51	21.25	3.732	9.2
1988	34	22.5	4.376	10.8
1989	17	23.75	6.798	13.6
1990		25	7.988	13.8
1991		22	11.397	20.4
1992		19.5	8.418	19.6
1993		19	19.694	45.2
1994		17	32.695	49.6
1995		15	25.515	34.4
1996		13	21.318	31.5
1997		11	22.409	40.6
1998		9	28.231	39.3

Note:

* Imports of champagne and vermouth are free as of 1990.

Source: New Zealand Tariff Schedule, Statistics New Zealand

Table 2: Trade policy and regulatory changes and the expansion of wine industry

Period	Wine consumption per capita in litres (year beginning the period)	Wine production mil litres (year beginning the period)	Trade policy and regulatory changes
1958-1964	1.74 (1960)	4 (1960)	1958 Higher taxes on beer and spirits 1960 Restaurants licensed to sell liquor 1961 Taverns licensed
1965-1969	3.08	8	1967 Restrictions on wine imports
1970-1974	4.94	19	1971 Theatres and cabarets licensed
1975-1979	7.63	24	1976 BYO restaurants licensed
1980-1984	11.9	43	1981 Import control removed 1984 Increase in sales tax on wine
1985-1989	13.10	60	1985 Grapevine extraction scheme 1986 Duties on wine imports reduced
1990-1994	11.7	54.4	1990-94 Further tariff reductions 1990 Supermarkets licensed to sell wine 1992 Wineries licensed to sell wine on own premises
1995-1997	8.7	56	1995- 97 Further tariff reductions 1996 Customs and Excise Act

Source: M. Workman, "Geographic Orientation of the Wine Industry", The University of Auckland, thesis 94 – 127, P40, 1994.

The process of restructuring started by the Grape Extraction Scheme and by the redesign of the protection structure of the late 1980s was sped-up by further trade liberalisation and de-regulation in the 1990s. By 1990, tariff quotas and specific tariffs were replaced by ad valorem tariffs which were to be reduced along a pre-announced path from 25 percent in 1990 to 5 percent in 2000 (see table 1).

As part of overall reforms, the government has changed its ways of collecting revenues, and an excise duty on alcohol beverages has been increased frequently. However, it has been imposed on both domestic and imported wine implying no direct impact on competitiveness. WINZ claims, however, that high excise duties inhibit growth of the industry and indirectly affect its export potential. The excise duty on table wine has risen to the equivalent of $14,540 per hectare involved in wine production

Among other regulatory policies affecting wine, production and labelling requirements (PLR) and export certification had the largest impact. PLR was established under the Food Act and Food Regulations of 1984 (and subsequent amendments). The rules are considered less rigorous than those in more tra-

Impact of Trade Liberalisation

ditional wine producing countries. Moreover, they have not been enforced by the Ministry of Health in the 1990s. As a result, many local and imported wines contravene the regulations. Export certification is required by all wine exporters and is issued by WINZ. Given that only a few wineries have invested in obtaining ISO certification, and that WINZ has only imposed low fines on those without certification, quality control is left primarily to self-regulation.

Table 2 records the most important trade policy and regulatory changes and the impact of these changes on wine consumption and production over a 30-year period.

The wine industry of New Zealand before trade liberalisation was producing mostly low quality cheap wines. Consumers bought what was available. Two policies have contributed to the restructuring of the wine industry. First, in the late 1980s with government assistance, substantial quantities of relatively low-quality vines were pulled out of ground (see table 3). Second, trade policy was reformed from being based on complex non-tariff structure, to being based on tariffs only. Moreover, the government commitment itself to reducing tariffs along a pre-announced path.

Producers abandoned production of cheap wines because they realised they could not compete in the low-price segment of the market. The new emphasis on competition, within a predictable medium-term economic framework, increased the industry's confidence. Grape growers and wineries responded with an increase of new investment in quality plantings allowing for a dramatic change towards production of medium and high quality wines. High quality new wines substituted for cheap wines and total production has risen by almost 20 million litres over the 1988-98 period (see chart 1).

Production expansion has had predominantly favourable effects on employment. In 1998, the wine industry provided permanent

Table 3: Production structure
(production by grape variety in tonnes)

	1986	1988	1990	1992	1994	1996	1998
Muller Thurgau	20740	19411	25767	17491	13687	13838	10579
% of total	37.9	37.7	36.7	31.5	25.3	18.4	13.5
Chardonnay	2594	2722	6026	6172	8786	13870	18169
% of total	4.7	5.3	8.6	11.1	16.2	18.4	23.2
Sauvignon Blanc	2096	1993	4659	6137	5083	12354	15136
% of total	3.8	3.9	6.6	11.1	9.4	16.4	19.3
Chenin Blanc	4718	3402	3652	2446	2112	2609	2768
% of total	8.6	6.6	5.2	4.4	3.9	3.5	3.5
Palomino	3103	2485	2446	1888	1197	1144	293
% of total	5.7	4.8	3.5	3.4	2.2	1.5.	
Riesling	1885	2765	3658	3144	2699	2877	3400
% of total	3.4	5.4	5.2	5.7	5.0	3.8	4.3
Semillon		1081	1443	1317	1385	2342	2319
% of total		2.0	2.0	2.4	2.6	3.1	2.9
Cabernet Sauvignon	2591	3143	3148	2596	2689	4169	4220
% of total	4.7	6.1	4.5	4.7	5.0	5.5	5.4
Pinot Noir	1216	729	1425	1597	2593	4617	4489
% of total	2.2	1.4	2.0	2.9	4.8	6.1	5.7
Merlot	362	562	1062	803	1237	2857	3430
% of total	..	1.1	1.5	1.4	2.3	3.8	4.4

employment to close to 4,000 people and seasonal employment to 1,000 more. Employment figures in wine manufacturing are considerably lower in larger businesses. Numbers also vary from year to year (see table 4). Since 1993, however, employment has been rising steadily.

Consumers have benefited from liberalisation in a number of ways:

- Improved average quality and increased supply of wine;
- Reduction of price (per same quality);
- Increase in wine varieties supplied;
- Access to wine improved through changes in sales regulation;
- Ability to substitute wine for higher alcohol content drinks.

Trade liberalisation has also given producers more options. Despite sharply increasing import penetration to almost 40 percent in 1997, producers were able to increase production by almost 20 million litres (see chart 1). This is a result not only of the expansion of domestic consumption but also of a ten-fold increase in exports, to account for nearly 30 percent of production in 1997.

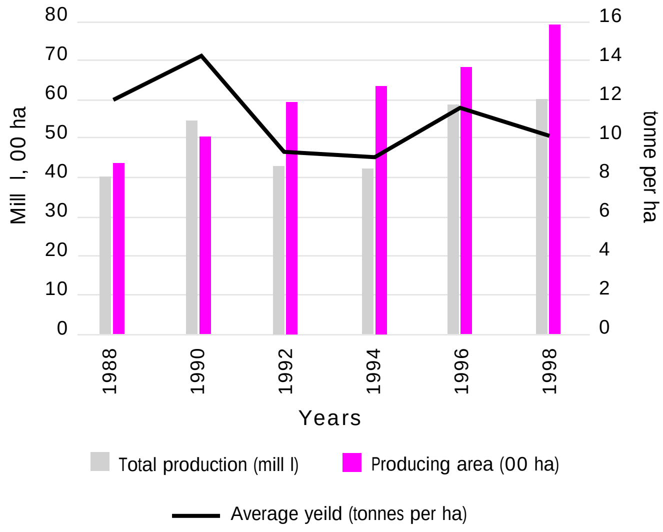
Table 4: Changes in employment in wine manufacturing

Year	Persons Engaged FTE*	Total Production (mil l)	Production per person (000 l)	Exports (as % of Production)	Imports (as % of consumption)
1987	810	37.7	46.5	2.7	9.2
1988	823	39.2	47.6	7.5	10.8
1989	777	45.6	58.7	5.8	13.6
1990	788	54.4	69.0	7.6	13.8
1991	907	49.9	55.0	11.5	20.4
1992	796	41.6	52.2	17.4	19.6
1993	801	32.5	40.6	26.1	45.2
1994	924	41.1	44.4	19.4	49.6
1995	1053	56.4	53.5	14.1	34.4
1996	1186	57.3	48.3	19.3	31.5
1997	1260	45.8	36.4	29.1	40.6

Source: Employment data is from Business Statistics Analysis, Statistics New Zealand, and production data is from WINZ and Statistics New Zealand

* Businesses that must register for GST are only counted in the period 1987-93, while from 1994 only economically significant enterprises are counted.

Chart 1: Movements of production, producing area and average yield



Implications for Trade Opportunities

The New Zealand wine industry demonstrates that it is easier become a competitive exporter if there is opportunity to learn from competition in the domestic market place. Before the first steps of trade liberalisation were taken in early 1980, wine exports were negligible. In 1998, for the second year in a row, New Zealand was a net exporter of wine. After the domestic wine market was freed from all quantitative barriers 15 years ago, domestic wine producers have faced strong competition from low price, low quality wine producers around the world.

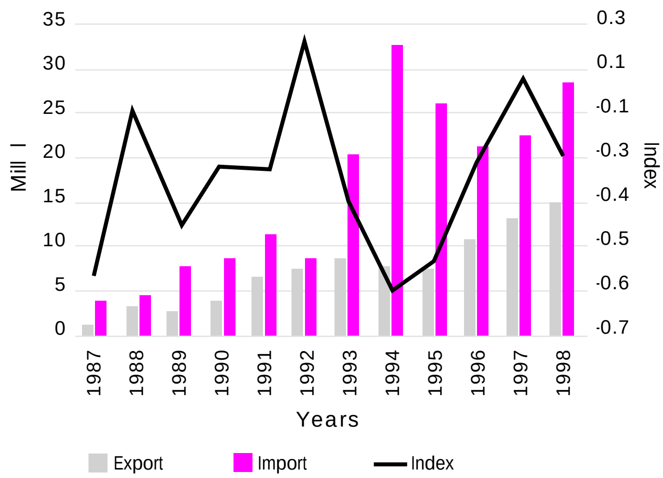
The regional distribution of trade in wine has also changed. On the export side, the United Kingdom, Australia and the USA were absorbing 75 percent of wine exports in 1987. In 1997, their joint share has increased to 83 percent with the United Kingdom's share shooting up to 66 percent and Australian's share doubling to 26 percent. On the import side, Australia is maintaining its role as the biggest supplier of imported wine (36 % in 1988 and 72 % in 1997), but the shares of some European suppliers (such as Italy and Spain) and Latin American suppliers (such as Argentina and Chile) are increasing.

A valuable indicator of the benefits of exports is their unit value, or, the amount of dollars earned by a unit (litre) of exported wine. Assuming no changes in exchange rates, an exporter is better off when the unit export value increases. In the ten-year period between 1988 and 1998, the unit value of wine exports increased from $4.0 per litre to $6.4 per litre.

Another useful indicator is the so-called trade volume specialisation ratio. It is calculated as the ratio of wine net exports (exports minus imports) to the sum of exports and imports of wine. This index ranges between -1 and 1. The closer the index to -1 (1), more specialised country is with respect to importing (exporting) of this product. The indexes for 1988-1998 are presented in Chart 2. The values of the New Zealand's indexes have remained in the negative indicating that in terms of volume New Zealand maintained its position as a net importer of wine.

To sustain the expansion of exports, WINZ has undertaken to coordinate "generic export promotions" which include a number of international promotional activities. Another important item on the WINZ agenda is the introduction of more rigorous production and labelling standards for local and imported products, and, enforcement procedures for these standards.

Chart 2: Volume of exports and imports and the index specialisation



Foreign Investment Development

The wine industry in New Zealand has attracted increasing interest from foreign investors.

One effect of the internationalisation of the wine industry is the integration of the industry into international capital movements. While there is no official statistical data on the capital movements related to this industry, information available from WINZ indicates that the wine industry has attracted increasing interest from foreign investors. The focus has been primarily on the existing wine production units due to their ability to deliver relatively high returns with low risks.

There are also likely positive effects on capacity-building and growth of the industry. Investment provides necessary funds for 1) planting new grapes and purchasing land, 2) obtaining the latest technology to enhance production and product quality, and 3) development of new products, including packaging.

Out of all foreign investment in New Zealand wineries, a high proportion is in small size wineries with a clear bias for full foreign ownership (see table 5). This bias is a consequence of "family" ownership with no space for outside equity partners, local or foreign. Only one of the four largest companies in New Zealand is partially foreign owned.

With respect to the outflow of Foreign Direct Investment (FDI), according to the available data, only one of the large companies is actively investing overseas. Montana Wines Ltd. has opened a subsidiary in Australia (with offices in 3 states). It claims that the benefits from being able to import and distribute its own wines significantly outweigh the costs.

Table 5: Extent of FDI in NZ wine industry, 1998

Number of wineries	Size*	Nationality of interest
Wineries with 100% foreign ownership		
2	B	US
3	B	Australian
1	B	French
1	B	Swiss
1	B	Japanese
1	M	French and Australian
Wineries with less than 100% foreign ownership		
1	B	US and NZ
1	B	Japanese, French and NZ
1	L	Dutch and NZ

* B=boutiques (sales up to 200,000l); M=medium (sales between 200,000 and 2,000.000l) and L=large (sales over 2,000.000l)

Source: WINZ

Response of Local Firms

The following case studies highlight the adjustment of the wine industry to liberalisation.

In an industry which previously had been highly oriented to the domestic market, there is now a focus on exports to provide sustainable growth.

Since liberalisation of the wine industry began, there has been an effort to produce higher quality wines as a competitive strategy against imports and to facilitate penetration of the world market. The proliferation of small family owned boutique wineries has enlarged consumer choice. The number of brands has grown. At the same time, the diffusion of new technologies among producers has tended to be relatively slow. Their interest in maintaining full control over their business has limited their access to new sources of capital.

On an international scale, the industry has remained relatively small. Its members have been able to pursue their marketing strategies for high quality wines with less concern about reactions from global competitors or about projectionist reactions to penetration of export markets.

For large companies, foreign direct investment provides access to new technology and facilitates access to world markets.

Successful exporters are investing in learning about product choice, design, advertisement, marketing, and management.

In an industry which previously had been highly oriented to the domestic market, there is now a focus on exports to provide sustainable growth.

Montana Wines Ltd.

Montana Wines Ltd. is owned by Corporate Investment Limited (CIL), a publicly listed company in whose ownership belong a number of companies, with Montana Wines being by far the largest.

Montana Wines has led the way for the New Zealand wine industry. Ivan Yukich started Montana Wines in the 1940s in Auckland's Waitakere Ranges as a family business. By the late 1960s, the company was the largest vineyard in New Zealand. Montana Holdings Ltd. was formed in 1964. The existing winery provided sufficient facilities for the production of the company's trend setting sparkling wines (such as "Cold Duck" and "Pearl") in the early 1970s. The success of these wines was taken as a strong signal to further expand the company.

When Montana was floated on the stock exchange in 1973, 40 percent of its shares were purchased by the multinational distilling and wine producing company Seagrams. This not only provided capital needed for growth but also access to the US market. However, further expansion was not possible without more grapes and land. The increased value of land already under vine cultivation (such as Gisborne) encouraged Montana to investigate new areas resulting in the purchase of 1,620 hectares of Marlborough farmland. In years to follow, a considerable investment of capital, skill and innovation went into making this region one of New Zealand's premium grapes growing regions.

Today, the Marlborough region contributes more than a third to the total New Zealand wine production in terms of volume of production and vineyard area. New Zealand wine has been put on the world map mostly due to the popularity and quality of wine made from Sauvignon Blanc grown in Marlborough. Montana is credited as the very first company commercially planting this grape variety.

Since the early 1970s, when Montana Wines changed owners, the company has substantially increased its asset base. It has also created significant alliances with internationally renowned brands such as Deutz and Cordier. Montana Wines today has wineries in Auckland, Gisborne, Hawkes Bay and Marlborough. The Marlborough winery, with its capacity of 21 million litres, is the largest winery in the country. Montana also became an owner of one of the country's oldest wineries when it purchased the McDonald Winery in the Hawkes Bay in 1988. In terms of the area, Montana Wines Ltd. owns over 1,000 hectares of vineyards, which is more than half of winery-owned vineyards in the country.

Although Montana uses contract growers (who supply up to half of the grape resource needed), it is a strong believer in developing its own vineyards. According to Montana Wines, the advantages of having its own vineyards are:

- Assurance of a necessary degree of control over grape quality and yield;
- Opportunities to experiment and obtain grapes with optimum flavours and maximum ripeness;
- A reduction of costs and minimisation of risks.

Each of these factors has played an important role in supporting the company's re-orientation brought about by policy changes in the areas of liberalisation and regulation.

Montana Wines was volume driven until the late 1980s. Since then, it has been increasingly focused on profitability growth. In 1992, profits were just over $10 million. In 1997, profits trebled to more than $31 million. Sales in the domestic market increased to $100 million and the value of exports more than doubled (from under $15 to over $30 million) over the same period.

The biggest challenges that Montana Wines has faced in the liberalisation process are:

- Geographical restructuring of the company to grow different grape varieties,
- Partnerships with foreign firms to develop new products and improve quality;
- Increased competition from foreign (particularly Australian, but also all New World producers) and small domestic producers of high value wines;
- The high value of the NZ dollar in the mid 1990s; and
- Stagnant domestic demand.

Montana Wines has a vision of becoming a key player on the international wine scene. It is likely that the most important challenge in the future will be how to expand export sales in the European market and other developed countries markets given the existing protective barriers and uncertainty of market conditions.

Hunter's Wines (NZ) Ltd.

Hunter's Wines (NZ) Ltd. is privately owned company with Jane Hunter holding all but one of the 150,000 shares. Jane's late husband Ernie started the winery. Hunter's was a pioneer winemaker in the Marlborough area. Its first vintage was in 1982.

In the early stages, the low earning Mueller Thurgau dominated the company's production. Wine was sold through three channels:

- at the winery;
- through normal trade outlets; and
- through a mail order system.[1]

A combination of high interest rates and a depressed local market in mid-eighties forced the company to sell its vineyards. At the same time, the Development Finance Company (DFC) took a minor shareholding in Hunter's Wines.

The company started to develop exports to the UK and Australia through an innovative and risky method of mail orders. Immediately after appearing on the UK scene, Hunter's wines began to win awards, thus it was able to establish itself firmly in the UK market. Hunter's wins in London opened interest to other New Zealand producers in wines such as Sauvignon Blanc.

The company has recovered sufficiently to purchase back the shareholding held by the DFC in 1987. When Jane Hunter took over the company she changed the emphasis to high value-added products at the premium end of the market. Since then, the company has adopted a flexible approach to product choice which has enabled it to increase its production by four fold.

Being a sole shareholder has allowed for a high degree of flexibility and adaptability to market conditions. For example, although Hunter's initially chose to focus on the premium wines, it soon discovered that mid-price wines are essential for entrance into supermarket sales. Consequently, Hunter's has introduced such wine varieties.

Expenditure on research and development primarily goes to improving vine quality. However, the company also seeks to improve the balance between fruit and vine and to make yield predictions early in the season. The company is also working on evaluation of the general canopy management techniques.

Hunter's has appointed a national distributing agency but still depends very much on selling wines by mail orders, at the cellar door, through its own restaurant and in supermarkets. In the UK, the company employs a public relation representative who handles Hunter's exclusively.

Being a small company with virtually no staff turnover, Hunter's is able to communicate changes in work requirements and ethics very easily. ISO 9002 has given staff the opportunity to improve knowledge and skills. All staff are familiar with and abide by the OSH regulations. There are regular training sessions for use of machinery in line with OSH requirements. Due to the small number of staff, the company has no need for formal staff meetings. Rather, employees meet informally to discuss various aspects of business.

Hunter's Wines aims for the top end of the market rather than being volume and price driven. At present, the company is focused on the UK, Australia and the US markets with very important niche markets in Ireland, Switzerland, and Hong Kong.

According to Jane Hunter, now the managing director of Hunter's Wines, the major future challenges of the company include:

- A stagnating domestic market where "everybody wants a bargain" regardless of quality and reputation;
- The need to develop an effective global business strategy; and
- The need to improve marketing techniques and product differentiation to overcome disadvantages of size.

1 A system was rather sophisticated whereby people "owned" a vine in the vineyard and received a free bottle of wine for the first five years.

Jackson Estate Ltd.

Jackson Estate Ltd. is a privately owned company. Its main activities include grape growing, production and marketing of wine. John Stichbury, the majority shareholder, started the company in 1987. Warwick Stichbury provided the capital required for the establishment of a vineyard. A partnership was formed to grow grapes on the full 100 acres of the property. The value of the company is assessed at approximately $6 million. Dave Williams, the Administrative Director, holds approximately 8 percent of shares, as do the other two Directors, Colin Churchouse and Tony Nightingale.

From the outset, a policy was established to grow only the best quality grapes. It was felt that in the event of any downturn in the wine industry, a crop of high quality grapes would be least affected. This policy proved to have dramatic effect on the future development of the vineyard.

When it was realised that grape prices were based more on tonnage yield, and less on the quality of the crop, the company decided to produce wine with its own label. This was largely made possible due to the close proximity of a 'contract' winemaking facility, meaning, it was unnecessary for the company to incur the high capital cost of the plant, equipment, laboratory and storage facilities that are involved in manufacturing.

This move took the company into new areas of activity in making and marketing wine. Consequently, the partners have divided operational tasks into financial and marketing activities and the 'hands-on' role of running the vineyard.

Jackson Estate had good quality grapes and an access to modern winemaking facilities, but lacked the expertise in wine production. As a result, the company formed an association with Martin Shaw, a winemaker of international repute, who established what is today known as 'the flying winemakers'. This association continues to the present time.

A policy of subcontracting enabled the company to concentrate on the growing of grapes, while retaining a high degree of control over other facets of production.

The first significant release of commercial quantity wine was the 1991 Jackson Estate Sauvignon Blanc. It was well received in domestic and British markets. Its continued national and international recognition has helped to ease the burden of marketing. However, the vineyard was hard pressed to cope with demand. Increased production became necessary, and contract growers have been engaged .

The company went through another drastic change in 1996 when one of the partners decided to retire. The company had to borrow money to buy him out. The change resulted in the re-allocation of tasks. John Stichbury is now directly involved in the promotion of the company brand. The viticulturist has increased responsibility, and additional administrative expertise is needed.

The company now operates from one location. Its management structure has changed into a more cohesive unit, with closer relationships between the growing and marketing aspects of the business. Financial reporting structures have also improved.

The company has been profitable since trade in wine commenced in 1991. However, its return on capital investment was marginal for the first few years. With no borrowings there was little pressure on financial performance. Rather, emphasis was placed on development of the vineyard. Re-planting with disease resistant rootstock became necessary from 1994 to 1998, which required additional capital.

The company faces several future challenges.

To secure quality grapes, Jackson Estate has embarked on a cooperative venture to establish and develop another vineyard in close proximity to the present vineyard. Although production will be three to four years away, there is potential to double the present revenue base.

Further expansion may require an on-going association between Jackson Estate and another wine company. This could be in the area of marketing or sales. It could also involve wine production. Such a move could have mutual advantage in the sharing of overhead (wine production and marketing), an increase in productivity to meet market demand, and the development of a secondary brand that would enable entry to another price point.

A policy of bank loan reduction is likely to be a guiding principle for the company during the next few years. Interest rates will be a significant factor in this respect.

The company perceives that future growth will be dependent on successful export marketing. Thus, it is actively searching out other export opportunities.

Future challenges

The New Zealand wine industry has become a successful global player. To attain the position of a dynamic and promising sector, the industry has had to overcome many challenges. However, several future challenges remain.

The wine industry is seeking continued market deregulation in two ways. First, a Sale of Liquor Amendment Bill is to be debated by Parliament. This Amendment is supposed to further deregulate the alcoholic beverages industry and, among other things, to allow for wine sales on Sundays. Second, the industry is encouraging the government to continue to liberalise and deregulate through fiscal policy measures.

Given the pressure to create a surplus, the government has chosen to tax the least elastic products most heavily (tobacco and alcohol). The current policy of inflation indexation applied to excise duties on wine is considered by the industry as an unnecessary cost burden. It adds to the uncertainty in which investors make their choices.

Moreover, representatives from the Wine industry are complaining that government has not provided services to the industry since the Ministry of Health stopped enforcing quality control regulation several years ago. The industry has been left to self-imposed quality controls because only a small number of companies want to invest in obtaining ISO certification.

In other countries that are large agricultural and wine producers, “right to farm” policies have been commonly adopted. However, in New Zealand there is still no national implementation of such a policy. The concern is that the expansion of non-farm activities will raise the costs of farming. The wine industry holds that there would be significant benefits from the nation-wide promulgation of a “right to farm” policy. These include an increased certainty and, in its view, reduced compliance costs for wine producers.

The industry, after some debate, created WINZ. Other agencies and bodies have serviced the industry, such as; the New Zealand Grape Growers Council, Winegrowers of New Zealand, the New Zealand Society for Viticulture and Oenology, New Zealand Wine Guild, and the New Zealand Grape Vine Improvement Groups. A rationalisation of this side of the industry is required in order to provide cheaper and improved information to the grape growers and winemakers.

The number of domestic wine producers has doubled in only the past few years. While this has been beneficial to consumers because they end up with a larger range of wines at lower prices, from the producers’ point of view, it has meant tougher competition. The share of imports in satisfying domestic consumption has risen to almost 40 percent, leaving domestic companies with an even smaller market share.

Not all producers compete in the same price category. Further, domestic producers have abandoned supply of cheap, low price wine. The industry has accepted its position as a global competitor and insists on building up its share of the world market on the basis of supplying premium quality wine to niche markets.

There is still some scope for the New Zealand government to influence the height of non-tariff and technical barriers that are found in foreign, especially European markets. Given that these barriers could be diminished, the New Zealand wine industry might find itself in a very good position if it continues the strategy of premium wine production.