

## **The Chinese Wine Market: Vanguard of a Consumption Society**

China overtook France last year as the largest red wine market in the world, at 1.86 billion bottles. Demand for red wine has grown steadily, and today's sales figures represent an increase of 136% over five years.<sup>1</sup> In addition, Christie's auctioned off more than \$39 million worth of wine in its 2012 Hong Kong auctions. However impressive these numbers are, they nevertheless show an immature market driven by a moneyed few. Consumption of non-French wine, white wine, and per capita wine consumption all continue to lag in China, and domestic producers have yet to establish a presence in the fine wine market. Furthermore, under the austerity and anti-corruption drive of President Xi Jinping, Chinese consumption of high-end red wines has declined recently: while imports to China rose 5% by volume last year, their value grew just 0.5%, suggesting a shift toward a new consumption profile.

The Chinese government has been striving to shift China toward becoming a true consumer economy. The success of the wine industry exhibits a few important developments along that path: expanding middle class participation, increasing high-end domestic production and finally, strengthening China-specific distribution networks. These developments have been fostered by major investments from both foreign and domestic industry players: international distributors have played a major role in promoting wine education and training, while local producers and distributors have done their part in promoting wines that cater to Chinese tastes. These changes are positive harbingers that foreign cultural products can do well in China beyond elite status-gifting circles.

### **From Status Gifting to a Unique Wine Palate**

An astonishing 90% of all wine consumed – or bought – in China is red, but the culture around wine has traditionally been one of status gifting. Per capita wine consumption in China is still very low, at just over 1 bottle per year (compared with over 30 in France), suggesting that the Chinese still treat wine as luxury good rather than a lifestyle beverage. ASC Fine Wines, the largest importer of wines to China, first made its mark in the 1990s with a promotion that packaged bottles of wine with men's neckties. Other marketing gimmicks over the years have also found success: Vinexpo chief executive Guillaume Deglise thinks red's status as a lucky color has helped its sales in China, and even Chateau Lafite famously printed the Chinese character for "eight" to promote its 2008 vintage.

Due to such measures, Chinese spending on more expensive wines grew 430% from 2008 to 2012, but the pace is slowing as austerity measures set in and China's palate matures.<sup>2</sup> Deglise notes that countries discovering wine tend to focus on red first and explore other types later. In China, the market is slowly transitioning toward drinking rather than gifting (or investing) as more people discover wine and existing drinkers develop

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<sup>1</sup> <http://www.theguardian.com/world/2014/jan/29/china-appetite-red-wine-market-boom>

<sup>2</sup> <http://www.scmp.com/news/china/article/1470017/china-now-second-biggest-consumer-high-priced-wine>

personal preferences. (There are also mounting suspicions that as much as 50% of status wines in China may be fake.<sup>3</sup>)

Such a phenomenon is not unique to wine – in many other markets, Chinese consumers are pulling back from so-called 土豪 products and gravitating more toward “accessible luxury.”<sup>4</sup> Part of this impetus may be backlash against examples of flamboyant, corrupt wealth, but another explanation is simply that the consumer market is maturing and people feel more confident expressing individuality. In an interview with the Wall Street Journal, Jim Boyce of the popular Chinese wine blog Grape Wall of China predicted that China’s love affair with Bordeaux wines will fade as drinker’s palates become more sophisticated.

When foreign cultural products are introduced to new markets, consumer education is key in order to encourage exploration and refinement of taste. The largest single effort to address this piece of the puzzle has been the 28 million RMB Shanghai “wine residence” built by ASC, the first provider of Wines and Spirits Education Trust (WSET) qualification classes in China. At the grassroots level, retailers such as Pudao Wines are offering rosters of tasting wines and finding that “if given a chance, consumers in China will buy what they like to taste, over labels, image, or heritage.”<sup>5</sup>

New non-French wineries like L’Huguenot, a South African winery that sold 1.5 million bottles in China in 2013, are also helping to uncover new market segments. In 2011, Yao Ming established a winery in California to produce quality wines for Chinese export, with prices starting at 1775 RMB. In the past few months, he has added a lower-priced wine aimed at younger, middle-class Chinese – the so-called 小资. Even internet retailer Amazon.com has begun selling select California wines in China. While currently only about 6% of Chinese wine imports are from America, this figure will no doubt rise.

### **From High End Foreign to High End Domestic Production?**

Though the impressive numbers of the import market have been capturing imaginations for years, in fact more than 80% of the red wine consumed in China is made in China. In the last year alone, Chinese wine production has grown 77%, making China the fifth-largest wine producing country in the world.<sup>6</sup>

An offering from Shanxi Province’s Grace Vineyard famously won a blind tasting against several French Bordeaux in 2011. Some commentators have likened the event to the watershed moment in 1976, when California wines bested French ones in a Paris tasting. Before that pivotal moment, California wines had a difficult time in selling in the US;

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<sup>3</sup> <http://jingdaily.com/chinese-official-claims-half-of-all-chateau-lafite-in-china-is-fake/>

<sup>4</sup> <http://www.forbes.com/sites/michaelzakkour/2014/01/17/the-china-luxury-downturn-is-real-global-luxury-brands-must-adjust/>

<sup>5</sup> <http://www.grapewallofchina.com/2014/04/03/wine-word-ian-ford-of-summergate-on-the-state-of-the-china-market/>

<sup>6</sup> <http://www.ibtimes.com/why-china-surpassed-france-worlds-biggest-red-wine-consumer-1552185>

today, Northern California is recognized as one of world's great wine regions. There should be no reason why Chinese wines cannot also have their moment in the sun: China sits over the 30<sup>th</sup> and 50<sup>th</sup> parallel "sweet spot" where wine grapes thrive. Despite the Grace Vineyard's coup at the tasting, however, some commentators aren't convinced that Chinese wines can yet stand up on the international stage.

French judges pointed out that one requirement for the testing stipulated that all wines fall within the same price range, but steep Chinese import taxes on foreign wine meant that the Bordeaux were actually of a lower tier – cheap by Western standards.<sup>7</sup> Whether or not the Grace Vineyard tasting was fair is somewhat of a moot point – the controversy the event generated suggests that no one is quite ready to think of Chinese wines as true rivals to French ones.

Grace Vineyard is currently being distributed by Torres China, which also represents a few other Chinese wineries. Other international distributors see different collaborative potential with domestic players. ASC Fine Wines came close to purchasing a local winery, Sino-French, a couple of years ago, and are now producing wine in Penglai in partnership with Lafite.<sup>8</sup>

In addition to gaining technical knowledge and prestige through foreign partnerships, Mr. Boyce predicts that domestic vineyards will begin experimenting with flavors and invent varieties that cater to regional tastes. There may even be potential for wines produced specifically for pairing with Chinese food, including bottles that can stand up to the famous heat of Sichuanese or Hunanese cuisine, which overpower delicate Bordeaux. Thus, the next stage of the fine wine industry in China may be one where a uniquely Chinese flavor profile emerges.

### **Exploiting New Distribution Channels**

In an interview with Jim Boyce from 2007, ASC Fine Wines co-founder Don St. Pierre Jr cited focused sales channels and simple messaging as critical aspects to marketing wine in China. "Wine tastings on Nanjing Xi Lu during Chinese New Year with one million people walking by are not a good idea," he said, "and don't compare a wine's taste to saddle leather or black cherries."<sup>9</sup> Given the increasing maturation of the Chinese market, however, new strategies may soon come into play.

In the 1990s, when wine was still a "white space," in China, foreign businesses were the first to take up trade in imported wines. However, as the market becomes increasingly lucrative and competitive, industry experts are beginning to see three trends develop: consolidation as lesser traders drop out, more producers attempting to do their own distribution, and digitized B2C alcohol sales.

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<sup>7</sup> <http://blogs.wsj.com/scene/2011/12/15/ningxia-beats-bordeaux-or-does-it/>

<sup>8</sup> <http://www.grapewallofchina.com/2011/01/21/wine-word-don-st-pierre-jr-ceo-of-china-based-distributor-asc/>

<sup>9</sup> <http://www.grapewallofchina.com/2007/06/28/interview-don-st-pierre-jr-asc-fine-wines/>

After China's ascension to the WTO, tariffs on imported wines fell drastically, creating ripe opportunities for companies like ASC Fine Wines. Chinese import and distribution companies soon followed, adding wine to their existing businesses. St. Pierre believes the government will move to regulate wine imports more in part to addressing the growing problem of fakes and counterfeits, which are largely accounted for by small-scale Chinese companies." Meanwhile, bigger players such as COFCO and Changyu will likely focus on domestic production and distribution rather than landing foreign clients.<sup>10</sup>

Meanwhile, many of those foreign clients – the biggest wine producers in the world – are looking for ways to cut out the middleman altogether. Some well-known producers such as Kendall-Jackson, Georges Duboeuf, and Antinori have tried to build their own brands and markets in China without partnering with a distributor. However, as Ian Ford, founding partner of Summergate points out, the risks of such an endeavor are numerous: "price structure manipulation, trademark violations, poor storage and handling, inappropriate or non-compliant brand communications, regulatory violations, erroneous Chinese back labels, and even counterfeits."<sup>11</sup> Other producers are banding together: Podium Wines, a company formed by five Australian producers, markets directly to Chinese distributors at major wine shows. For smaller buyers especially, being able to access a variety of Australian brands through one representative is a strong selling point, and Podium is able to save its member-producers 25-33% in distribution costs.<sup>12</sup>

Lastly, China's e-commerce juggernaut has not bypassed the wine industry. Jiuxian, a large wine e-tailer that sells everything from red wine to baijiu, recently secured \$69 million in new funding, with top asset management companies such as Sequoia Capital among its investors. Hao Hongfeng, Jiuxian's president, has said he aims to have distribution centers in very provincial capital within the next few years, a sign to look for increased penetration in second and third tier cities.<sup>13</sup>

Though China's mobile internet penetration has been rapidly rising (currently 500 million out of 618 million internet users use their phones to go online), foreign experts had previously dismissed the viability of selling wine online. VINEXPO CEO Robert Beynat predicted that online wine sales will top 8% of global sales at most, yet in China, they reached 27% in 2013. Now, VINEXPO predicts that online wine sales in China will grow by 47% in the next 6 years, eventually leading to the demise of brick and mortar stores.<sup>14</sup>

Though intrepid foreigners riding the WTO wave paved the way for wine in China, the rise of e-tailers such as Jiuxian and its competitors may indicate that the Chinese may soon take control of the market. Chinese people love making purchases online, and in the e-commerce space, Chinese companies have repeatedly beaten back foreign competitors (even Ebay and Amazon). One thing is sure: the shifting consumption, production and

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<sup>10</sup> [http://www.wine-business-international.com/Market\\_Watch\\_The\\_Chinese\\_take\\_interest\\_in\\_their\\_own\\_market.html#](http://www.wine-business-international.com/Market_Watch_The_Chinese_take_interest_in_their_own_market.html#)

<sup>11</sup> <http://www.grapewallofchina.com/2014/04/03/wine-word-ian-ford-of-summergate-on-the-state-of-the-china-market/>

<sup>12</sup> <http://www.grapewallofchina.com/2014/04/30/making-it-in-china-mat-ryan-of-podium-wines/>

<sup>13</sup> <http://www.techinasia.com/china-wine-ecommerce-site-jiuxian-reveals-70-million-dollars-funding/>

<sup>14</sup> <http://jingdaily.com/chinas-gigantic-wine-market-goes-digital/>

distribution patterns of wines in China point to a maturing consumer society and strengthening middle class tastes.