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Who are we

Australian Grape and Wine Incorporated (Australian Grape & Wine) is Australia's national association of winegrape and wine producers. Our activities focus upon the objective of providing leadership, strategy, advocacy, and support that serves Australian wine businesses now and into the future.

We represent the interests of the more than 2,500 winemakers and 6,000 winegrape growers working in Australia. Our role is to help forge a political, social, and regulatory environment - in Australia and overseas - that enables profitable and sustainable Australian wine and winegrape growing businesses. These businesses make a significant contribution to underpinning regional economies by driving growth in jobs, regional exports and food and wine tourism.

Australian Grape & Wine's voluntary membership represents over 75% of the national winegrape crush. We represent small, medium, and large winemakers and winegrape growers from across the country. Policy decisions by the Australian Grape & Wine Board require 80% support, ensuring no single category can dominate the decision-making process and guaranteeing policy is only determined if it provides significant industry benefit. In practice, most decisions are determined by consensus.

Australian Grape & Wine is recognised as a representative organisation for winegrape and wine producers under the Wine Australia Act 2013, and is incorporated under the SA Associations Incorporation Act 1985. We work in partnership with the Australian Government to develop and implement policy that is in the best interests of winegrape growers and winemakers across Australia.

Background and Terms of Reference

On 26 February 2020, The Australian Government's Joint Standing Committee on Trade and Investment Growth sought submissions to the *Inquiry into Diversifying Australia's Trade and Investment Profile*. The Committee sought submissions addressing any or all of the terms of reference for the inquiry. The focus of the Committee's inquiry is to understand whether there is a need for Australia to diversify its trade markets and foreign investment profile including;

- Consider if Australia is too reliant on any one market for exports. If so, what factors are contributing to this dominance;
- The advantages and disadvantages, including in relation to the national interest and national economic risk, to an over reliance on any one market;
- Consider if Australia is too reliant on foreign investment. If so, what factors are contributing to this dominance;
- The advantages and disadvantages, including in relation to the national interest and national economic risk, to an over reliance on foreign investment, especially foreign investment by state-owned enterprises;
- The impact of global crises including trade disputes and political disputes on Australia's relationship with countries we are reliant upon for trade and investment purposes;
- The impact of bilateral trade agreements on Australia's exports and whether they contribute to concentrated export markets;
- The impact of bilateral trade agreements on Australia's domestic market and whether they contribute to an over reliance on foreign investment;
- Analysis of industry and government preparations to diversify its trading partners and secure new markets for Australia's exports, including through further free trade agreements; and
- Analysis of industry and government preparations to ensure the Australian economy is not overly reliant on foreign investment.



The international trading environment

The multilateral trading system has contributed significantly to unprecedented economic development over the last few decades. Greater certainty over trade policies during this time has created predictability, allowing for ideal conditions for long-term business planning and investment. However, a rise in trade-restrictive measures since 2019 — especially between major economies — and the suspension of activities of the WTO's Appellate Body have created new challenges for the multilateral trading system. In addition, the COVID-19 crisis is having a major impact on global supply and demand, leading to disruptions in global supply chains for both goods and services.

Prior to COVID-19, the structure of global trade was already undergoing a substantial shift when some governments imposed more restrictive policies led by trade tensions, sagging growth, and a backlash against globalisation. Global supply chains were also witnessing major shifts driven by technological advances such as 3-D printing, artificial intelligence (AI) and automation. These advances in technology, a renewed focus on ethical and sustainable sourcing, as well as the trade tensions in recent years, have led consumers to reassess from where they source their products.

The Peterson Institute for International Economics¹, has estimated that global trade will drop by 24 per cent year-on-year in 2020, mostly reflecting the compression of supply chains, running down of inventories, and drops in final demand.

Over the next two to three years, we will probably see a rise in protectionist responses, which in turn will limit the rebound in trade once COVID-19 is arrested. Even the one facet of globalisation that may not be so adversely affected of digital flows, e-commerce, and data flows, may also come under pressure as concerns about privacy and data security are raised.

Australia wine trade

The Australian wine sector has been a highly reliant export orientated sector for many years with around 60-65% of our production being exported each year. With supply and demand well balanced in the domestic market there is limited scope for expansion meaning future growth is highly dependent on growing our share in the international marketplace.

Australia's wine exporters have been experiencing extremely positive export growth for some time which has been underpinned largely by, ongoing demand from Chinese consumers, Australia's suite of Free Trade Agreements (FTAs), and the government's investment in the wine Export & Regional Support Packing of \$50 million².

In the past 12 months to March 2020, The Australian wine sector exported around 728 million litres of wine valued at \$2.67 billion. This wine was shipped to 119 different export markets around the world.

While these factors have led to the sectors strong export success and would imply a highly diverse export orientated sector, it does not highlight the full picture. Australia's top five markets in value; China, United States (US), United Kingdom, Canada, and Singapore account for around 82 percent of the total value of these exports at almost \$2.2billion. This means that the remaining \$470million is split amongst the remaining 114 export markets. Further to this point the top two markets of the China and the US account for over half of the total value of all exports at around 55 percent.

As would be expected, much of the focus on resourcing and promotion in recent times has centered on the top

¹ https://www.piie.com/research/economic-issues/coronavirus

² https://www.wineaustralia.com/whats-happening/export-and-regional-wine-support-package



markets to enable the potential in these markets and further capitalise on our strong market position.

All of these factors have left the sector in a strong export market position with significant investment in key markets but it has also left the sector highly reliant on a small number of key markets and therefore potential risks to any adverse trade impacts on those key markets.

Importance of diversification of markets

The global wine market is highly competitive and not all wine businesses enjoy the same level of export success. Indeed, many small wine businesses choose not to explore growth opportunities in export markets because they feel they lack the expertise and knowledge to do so. Enabling small wine businesses to explore these opportunities and take advantage of FTAs is a potential growth opportunity for the sector.

The forecast for export growth over the next five years is relatively strong for China, but much flatter in other markets – including in Australia. While volumes may be contracting in traditional wine markets, the data relating to sales of higher-value Australian wine is more positive. While value growth is forecast to continue in the coming years, several factors could present risks for Australian exporters.

Australia competes against several much larger and often heavily subsidised wine producing nations which have the potential to produce enormous volumes, particularly at the commercial end of the market. The impacts of COVID-19 also further complicate wines global supply and demand during 2020 and beyond. Despite this, Australia remains in a strong export position in 2020 and the impacts of COVID-19 may even present some opportunities for Australian wine exporters to capture market share. However, given the subsidies provided to many producers in these countries, and the availability of cheaper inputs (including labour and water), it is becoming more difficult for Australian wine businesses to compete at lower price-points.

Secondly, trade and strategic tensions between the United States, Europe and China, Brexit and the increasing levels of global geopolitical instability all present a level of uncertainty for global exporters. Given the importance of the China, United States and United Kingdom wine markets, this is potentially a very significant risk. Further to this, trust in key international institutions like the World Trade Organization (WTO) is decreasing, and in some instances, world leaders are actively seeking to diminish the WTO's importance. This has the potential to erode the rules of the global trading system which has enabled the more level playing field from which we have all benefited.

This trade uncertainty is centered upon Australia's key wine export markets, highlighting the need to not only capture the export opportunities that exist today, but to plan for and manage the potential for shocks to export markets in the future. Diversifying Australia's export footprint in a strategic and considered way will be a critical part of this future planning.

Diversification is important aspect of trade and it is clear there is a need for sector to spread its risk and consider a broad range of markets that suit their needs in both traditional and non-traditional markets for wine. While non-traditional markets can be challenging in terms of compliance requirements and establishment, they also offer opportunities for lower competition and first mover advantage in gaining and then growing market share. We have had clear warnings for some time that relying too heavily on a single market with limited ability to shift is a highly risky strategy for business in the current trade environment which can see countries close or slow trade overnight. A flexible diverse array of market options would prove a more sustainable option. While none of these markets are without their challenges there are a number which show a lot of potential as future high value or high demand wine markets, including India, Mexico, Russia, parts of South-East Asian and a number of the African nations. While there is significant potential for future growth in many of these markets it will require sustained effort and investment, and an improved trading environment (E.g. FTAs and improved regulatory arrangements) before this potential can be realised.



Foreign investment in the Australia wine sector.

Australia's world-class food and wine tourism offering is part of what makes Australia attractive as a destination for people, investment and ideas, and each bottle of Australian wine sold internationally can tell a story, providing a unique perspective of Australia. Increasing the number of tourist visitors to Australia enables us to harness our natural assets, our culture and our people, to shape positive perceptions of Australia which are brought back to their countries and shared. Foreign investment has a role to play in enabling better links between Australian, international business people and their markets.

Australian wine has shown that there can be advantages to foreign investment which support the development of export markets and growing demand. It can drive investment in the sector and can also play a role in developing export markets both directly and indirectly. For example, in Australian Wine, there is some investment in Australian based wine businesses by locally based and foreigner Chinese nationals. These businesses have provided a key link in driving part of the Australian wine sectors success in China as an export market. They have supported business linkage to the China market which in turn aids in the promotion and business relationships which have contributed significantly to the cultural and business understanding of wine between Australia and China.

Trade negotiation impacts

Australian Grape & Wine is a strong advocate for Australia's aggressive free trade agenda as it seeks to harmonise trade and improve market access. Much of the sectors success in several export markets has been made off the back of Australia's existing meaningful and comprehensive trade agreements. Australia's bilateral trade agreements present no risks to our well-established domestic market as a well-established mature wine market. In fact, they are a key pillar which supports diversification of export markets which the sector is highly reliant on and would seek further investment.



Policy responses

Diversification of market and investment in Australian wine is of great importance but can only be driven by greater investment in growing demand and enhancing our unique, world leading Australian wine proposition.

Building on previous investment.

The \$50 million package had a very strong focus on marketing and promotion in export markets, assisting existing exporters and developing capabilities for new exporters in China and/or other free trade agreement (FTA) markets. This funding is vital in assisting industry's SMEs to capitalise on their existing export success or enter the export market. However, the \$50 million package and the investment into the United States is also likely to see an increasing dependence on the three key markets of China, United States, and the United Kingdom. The uncertain geo-political environment demonstrates the need to further diversify our markets to future proof against the sovereign risk provide by market specialisation.

The \$50 million package has helped build demand in the key markets of China and the United States. However, without additional investment, we risk falling short of capitalizing on this growth and capturing the immense opportunity before us.

We can do this in two ways:

First, investment in marketing and brand building activities in new and emerging markets. The \$50 million package has shown us how this can be achieved, and a further investment within these markets would build on this, providing the opportunity for the sector to gain a permanent foothold in the key economic-growth regions of Asia and Africa. A further investment will enable the sector to replicate our China growth in these new markets, diversifying risk.

The second element to grow demand is to lower trade barriers and improve market access for exports through a network of international trade negotiations and sustained efforts to reduce non-tariff barriers. At a time when farmers around the country are in a crippling drought, free trade agreements give hope for a long-term sustainable future and recognise the importance of agriculture, and more importantly, exports of agricultural produce as vital to Australia's economic well-being and rural and regional Australia's prosperity. We will address these issues later in the document, but these are critical to market diversification risk mitigation and export growth.

Demand growth through enhanced marketing

A continued annual investment of \$25 million in global marketing funding (i.e. an additional \$17 million per annum, over and above the recurrent industry funding of \$8 million from existing levies and user-pays funding) would conservatively see wine exports reach around \$3.2 billion by 2024–25 (see table 1). When combined with the other elements of the wine sectors future-proofing strategy, a more realistic estimate is \$4–5 billion. There are three key elements to growing demand.

First, this additional investment would focus on cementing and building our recent extraordinary growth in China, by strategically targeting the anticipated 750 million people who will make up China's middle-class by 2022. Ongoing investment will allow us to educate these consumers about Australian wine by improving Australia's social media presence in current and new channels, and driving our engagement in e-commerce channels. It will also enable the continued and expanded delivery of our ambitious education program to Chinese consumers. We must recognise that as growth inevitably slows in China, we must take every opportunity to cement our position as the top exporter of premium wine into the market.

Second, we continue to see tremendous opportunity to re-capture market share in the United States. Australian wine has underperformed since the Global Financial Crisis, when Australia lost significant ground in the premium



wine segment to competitors based on factors including the exchange rate, consumer perceptions and falling demand. Additional investment in the United States would unlock our potential in this market, returning sales growth to \$1 billion per annum. The United States market is one of the few traditional wine markets which is still growing, with the expectation that by 2023, an extra 23 million cases of premium wine will be required to meet demand. Australia is well placed to capture this opportunity, but we need to overcome current consumer-perception barriers. Our proposed investment would focus on re-capturing shelf-space with major retailers and continuing to engage with influential wine figures in the United States, including critics and leading sommeliers, to ensure Australia's talented winemakers get the recognition they deserve. Doubling current sales of Australian premium wines in the United States only requires an extra million cases worth US\$100+ million in retail value. We can do so much more. We expect additional investment would unlock growth of half a billion dollars over the next five years.

Third, the increasing dependence on the three key markets of China, United States and the United Kingdom mean we need to diversify our markets. South-East Asia will continue to be a major source of growth, but the forthcoming Free Trade Agreement with the European Union and the UK may also provide a stimulus in these important markets. More long-term prospects include East Africa and India. We must start to invest in all these markets to provide a platform for growth.

Industry will play its part in funding these programs, but it will require the development of partnership arrangements between industry and State and Federal governments to capture the opportunities before us. Innovative and collaborative export programs will involve co-investment from all stakeholders.

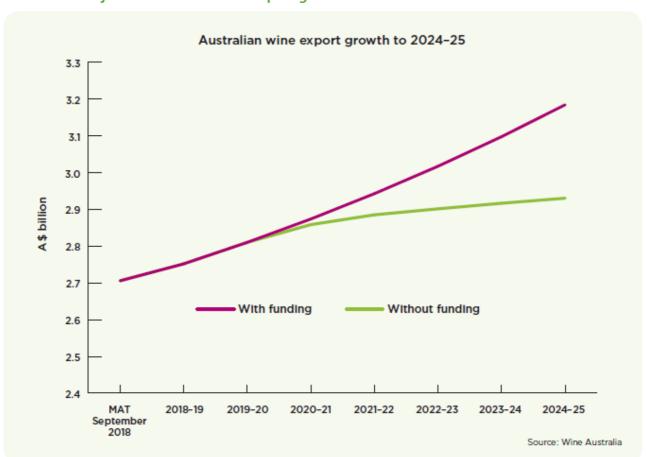


Table 1: Projected Australian wine export growth - with and without additional investment.



The average export price and average grape price are closely linked. The export growth generated by the \$50 million package is underpinning by higher prices for grapes in Australia, delivering growth along the value chain. During the 2020 vintage, the average purchase price of grapes in Australia was \$694 per tonne, a 5 per cent increase compared to 2019 and the highest average price since 2008. An investment in building demand will pay dividends along the supply chain.

Increasing wine tourism

Tourism remains an important vehicle for driving growth in rural and regional economies and enhancing understanding of Australia's wine offering. The \$50 million package was designed to complement and contribute to the objectives of the Australian Government's Tourism 2020 strategy, which is focused on building the resilience and competitiveness of Australia's tourism industry and growing its contribution to the Australian economy. The more than \$8 million investment in international wine tourism grants and 'Growing Wine Tourism' training has stimulated development of wine tourism products and services and built the capability and capacity of wine businesses to leverage the increased marketing activity funded by the \$50 million package. Additional investment will maintain this momentum over the long-term, enabling continuing accruing benefits in rural and regional economies.

COVID-19 has increased the importance of tourism to diversify our offering to market. On-premise sales remains arguably the best channel for interaction of brands and categories with consumers, as both off-premise and e-commerce channels having limitations in this regard. We need a deeper understanding of how Australian wine companies can leverage the growing importance of the online channel to grow their brands.

The viability and structure of the on-premise in most markets is under review. While there may be a combination of government assistance and beverage alcohol industry support schemes, at least in some countries, the survival especially of Small and Medium Enterprises in this sector is crucial. Their survival will, naturally, be impacted by any extension of restrictions. Second waves of the pandemic in some markets, including Australia, are seeing the on-premise shutdown again.

However, the recent school holidays, coinciding with social distancing requirements, have demonstrated that the premiumisation of cellar door offerings with paid tastings and sit-down tastings has had strong consumer demand. This high demand during this period has accelerated the adoption of these strategies and helped profitability for those able to open cellar doors. Consumers, at least in the short term, have shown a real desire to explore domestic tourism opportunities. This raises the pertinent questions:

- Can domestic tourism compensate for the demand deficit from international tourism and restrictions on on-premise in the short to medium term? For example, Tourism Australia has pivoted very rapidly to the domestic market out of necessity, and while international borders are closed, interstate and intrastate tourism should take up this gap.
- International tourism as a driver cannot provide the catalyst required (or anticipated) in the short term (24–36 months). What placeholder do we need to revive this when the time is right?
- Can the current tourism experience and follow-up to maintain a connection to the brand and region translate into follow-up sales /visitations?

We project that an additional annual spend of \$3 million would see 400,000 to 450,000 more domestic and international tourists visit wineries over five years, (refer to table 2) on top of Tourism Research Australia's National Forecast, firmly placing Australia as a source of outstanding wine-based tourism experiences over the long-term, and building demand for high-quality Australian wines when tourists return home.



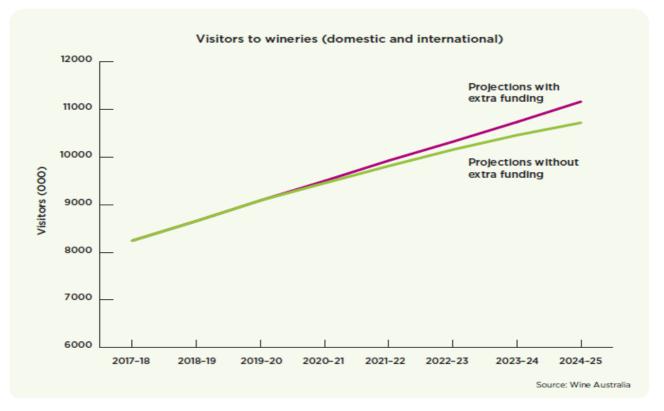


Table 2: Visitors to Australian wineries.

Harnessing innovation

Innovation is a critical driver of productivity, increasing quality and improving sustainability in the Australian wine sector, and in the agricultural sector more broadly. While we are confident the current model of industry and government investment in Wine Australia's Research & Development (R&D) investments is well placed to drive the sector into the future, there is one piece of ageing infrastructure preventing the sector from unlocking the full potential of our world class R&D.

The University of Adelaide's <u>Hickinbotham Roseworthy Wine Sciences Laboratory</u> at the Waite campus was established in 1998 and plays an integral role in research, education and service to the wine industry. State-of-the-art at the time, the winery is now too small and dated to provide our researchers with the infrastructure required to provide the innovation we need. A new winery is urgently needed to ensure our researchers are on par with our competitors in the US, Europe and South Africa who have invested in new facilities.

These research facilities are critical to the entire sector, but are particularly important to the future productivity of small and medium-sized wine businesses that do not have the capacity to engage in their own large-scale R&D activities. In addition, the winery acts as a major piece of infrastructure to attract new Australian and international students, strengthening the pool of highly trained oenologists entering the industry, and contributing further to Australia's educational export earnings. This understanding that research capability is part of the diversification of the sector, and not just an input to the grape and wine production sector, is vital to achieving our future success.



Conclusion

The wine sector faces unprecedented change over coming decades, presenting both opportunities and threats to its future prosperity. The Australian wine sector will need to respond to these challenges and opportunities and will look markedly different by 2050.

Responding to the short-term challenges of the COVID-19 pandemic will result in much pain and potentially significant structural changes to the sector. These will deliver more rapid change then otherwise would have occurred, with digitalisation, new products, new routes to market and innovative consumer engagement driving growth.

Exports are key to the profitability of the sector. While the largest markets of China, North America and the United Kingdom will remain highly important customers, a diversified markets strategy will provide growth opportunities in Europe, India, South East Asia, and Africa. Promotional strategies position Australia's wine to be sought-after globally, with a target of an annual growth rate in unit value of three per cent. A relatively small amount of government investment will build on the grape and wine sectors strong and sustainable foundation to springboard growth as we emerge from the COVID-19 pandemic. This inquiry has never come at a better time, as trade and investment diversification are critical to Australia's economic success.



Contact

For further information, please contact

Tony Battaglene

Chief Executive

14-16 Brisbane Avenue Barton, ACT 2600

Tel +61 2 6239 8304

Email tony@agw.org.au

Damien Griffante

Manager, Policy and Market Access

National Wine Centre, Botanic Road, Adelaide, SA 5000 PO Box 2414, Kent Town SA 5071

Tel: +61 8 8133 4308

Email: damien@agw.org.au