Why should wine continue to receive a differential tax rate compared to other alcohol types? [1]

Key Findings:

- **Domestic wine producers confront unique structural and capital challenges compared to brewers and spirit manufacturers.**
- **Domestic wine producers play a critical role in the socio-economic fabric of regional communities and would be significantly impacted by increases in wine taxation.**
- **The Australian wine industry is already highly taxed by global industry standards.**

Wine should continue to receive differentiated tax treatment compared to other alcohol beverage types. This recognizes the added production risks, economic footprint and industry structure of wine, compared to spirits and beer manufacturing which are very different. Just because they are all products with an alcohol base does not mean that they should be taxed at similar levels. The unique socio-economic contribution made by the wine industry to Australia and in particular our regional communities should also be considered along with the sector's limited capacity to pay even higher taxes during a period of on-going challenges in both domestic and international markets.

Contribution to the national economy

The wine industry contributes the most of all the alcohol sectors to the national economy and this will continue for the foreseeable future:

- The wine industry contributed around $1.77 billion to the national economy in 2013-14 and this is expected to increase at an annualized rate of 4.3% (vs. annualized GDP growth of 2.5%)
- The spirit industry contributed around $130 million to the national economy in 2013-14 and this is expected to increase at an annualized rate of 3.3% (vs. annualized GDP growth of 2.5%)
- The beer industry contributed around $1.17 billion to the national economy in 2013-14 and this is expected to increase at an annualized rate of 0.5% (vs. annualized GDP growth of 2.5%)

The wine industry employs the highest number of people:

- The wine industry directly employs 16,122 in 1,867 businesses
- The spirit industry directly employs 800 in 55 businesses
- The beer industry directly employs 3,918 in 228 businesses

Wine tourism[2]

- International wine visitors (for year ending September 2014):
  - Account for 696,602 visitors to Australia or 11% of the total visitors to Australia
  - Number of wine visitors increased by 1% from last year
  - Winery visitors account for 40 million nights within Australia or 18% of the market. This represents an average annual growth of 1% since the year ending September 2009
  - Contribute $4.9 billion to the overall visitor expenditure to Australia

[1] Unless stated, all facts and figures are based on IBISWorld Industry Reports (Wine Production in Australia, July 2013; Spirit Manufacturing in Australia, September 2013; and Beer Manufacturing in Australia, November 2013)
[2] Figures for year ending September 2014, Tourism Australia

- Domestic Overnight Wine Visitors[3]
    - Account for 3.1 million trips, a 7% increase from last year
    - Contribute 15.7 million visitor nights (5.2% of total)
    - Contribute $3.3 billion in visitor expenditure to the domestic market

The contribution of the wine industry in attracting international tourists vastly outweighs that from the beer and spirits industry. Tourism Australia estimates that beer and spirit manufacturing and tourism attractions such as the Cascade Brewery in Hobart, the Sullivans Cove distillery (producer of the 'world's best single malt whiskey' in 2014), together with Coopers in Adelaide, the Bundaberg Distillery in Queensland and other micro-breweries and micro-distilleries, for example, would only add up to 10% of the total benefits of wine tourism[4].

The competitive disadvantages of wine manufacturing

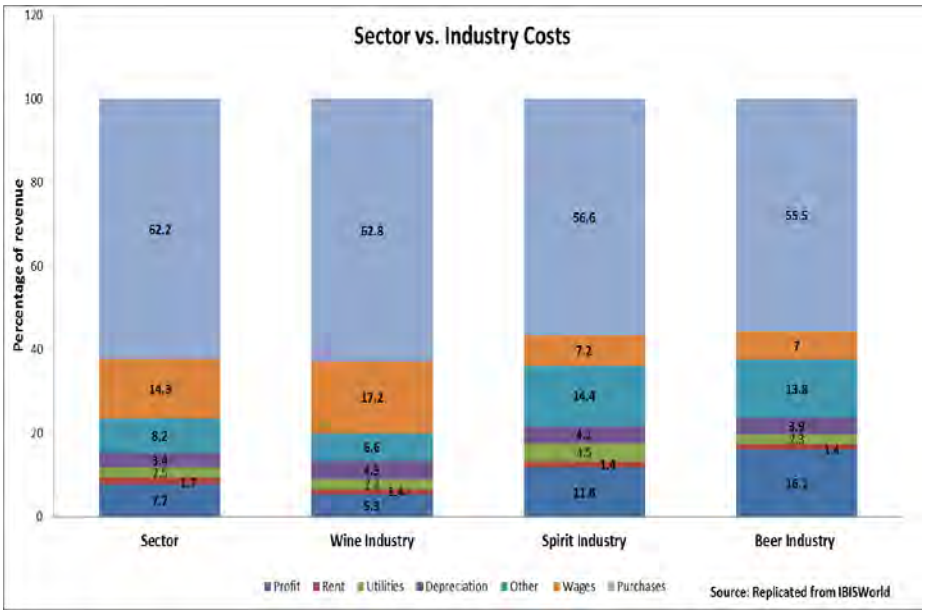
Despite this impressive economic contribution to the Australian economy, there are several commercial and structural factors unique to the winemaking industry which justifies taxing wine at a lower rate when compared to spirits and beer.

Profitability

Of the alcohol manufacturing sectors, wine has the highest cost structures and highest level of revenue volatility, making its profit margins smallest.

- Profits in the wine industry are only 5.3% of total revenue
    - Profits in the spirit industry are 11.8% of total revenue
    - Profits in the beer industry are 16.1% of total revenue and known to be one of the most profitable manufacturing industries in the world
- Wine industry purchases accounted for an estimated 62.8% of revenue, while labour costs account for an estimated 17.2% of revenue. Depreciation is about 4.5% of revenue.
    - Purchases costs include containers and other packaging materials; wine for blending, fortification or distillation; grape juice and grape spirit; sugar; and other purchases. Grape, the most important production input, is predominantly grown and harvested specifically by wineries and grape growers for the purpose of wine production and is subject to significant seasonal volatility in both pricing and supply.
    - Wages in the wine sector are expected to have grown as a proportion of total revenue in 2013-14. This growth was mostly due to falling revenue, but also because of the labour intensiveness of various functions in wine production, such as the upkeep and maintenance of vineyards and manufacturing processes. Analysts believe that wages are expected to fall as a proportion of revenue over the next five years due to increasing investment in modern technologies, thereby making the industry's production process more highly capital intensive.
    - Depreciation in the wine sector remains at about 4.5% of revenue. This is a little higher than other beverage industries such as beer, mainly due to greater costs involved in wine maturation equipment and storage.

[3] Overnight trips In the NVS, overnight trips are defined as trips involving a stay away from home for at least one night, at a place at least 40 kilometres from home. Only those trips where the respondent is away from home for less than 12 months are in scope. The trip is the basic collection unit used in the NVS to obtain information about overnight travel undertaken by Australians.
[4] Socioeconomics benefits of the Australian alcohol industry, Deloitte Access Economics, May 2014

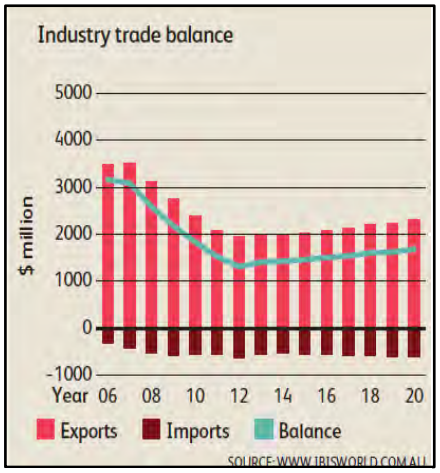


- Purchases are the greatest cost to the spirit industry, accounting for roughly 56.6% of revenue. Labour costs have steadily risen over the past five years, accounting for an average of 7.2% of revenue in 2013-14. Depreciation is estimated at about 4.1%, as the industry is capital intensive. The major purchases are packaging, such as bottles and cans, and full-proof spirits for RTD producers.
- Beer industry purchases represent the largest cost to the industry at 55.5%. Labour costs are equivalent to about 7.0% of revenue.
    - The major purchases of the brewing industry are packaging (glass, aluminium, cardboard and kegs) and malt. The former category accounts for about 60.0% of material costs and the latter for 18.0%. Of the other materials purchased by brewers, the most important are refined sugar (4.0%), hops (2.0%) and water (1.0%).
    - Labour costs are equivalent to about 7.0% of revenue, which is low compared with the average for all food and beverage and reflects the high level of mechanisation. This trend is expected to continue over the coming years, especially as industry operators boost automation.
- The wine industry has the highest revenue volatility. Production and prices are affected by the supply of grapes, which is affected by weather and soil conditions, disease and plagues.
    - Earnings fluctuate due to changing input prices, changes in supply of grapes and restructuring costs.
    - Strong competition within a highly consolidated wine retail market continues to place significant downward pressure on wholesale pricing and margins. The retail price increases of wine has lagged CPI for over five years unlike the above-CPI price rises experienced by beer and spirits.
    - Unpredictable fluctuations in exchange rates also disproportionately impact the wine sector's exposure to imports in comparison to beer and spirits products.
- The spirit and beer industries exhibit far lower levels of revenue volatility. Due to higher profit margins, volatile prices for commodity inputs such as packaging, ethanol, aluminum and barley have only a moderate effect on beer and spirit pricing and revenue.

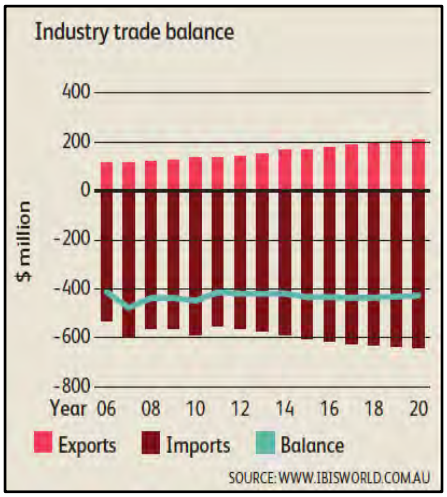
Industry trade balance

The wine industry is a net exporter and therefore more vulnerable to global market issues such as exchange rate fluctuations and global supply/demand imbalance compared to other alcohol manufacturing industries. The spirit industry is a net importer since the majority of the spirits consumed in Australia are imported with no further processing, value-add or transformation. This also implies a lower manufacturing and transportation cost compared to the wine industry.

- Export revenues for the wine industry are $2 billion p.a.
  - Export revenues for the spirit industry are $168.3 million
  - Export revenues for the beer industry are $51.2 million
- Wine exports have fallen sharply over the past 5 years, declining at an annualized rate of 6.5% to account for a 34.5% share of revenue
  - Increased competition in the global wine market and global economic downturn have weighed down industry exports and intensified competition between winemakers on the domestic market.
  - Wine producing countries such as Chile and South Africa have emerged to challenge Australian wine in its key export markets especially in the commercial wine segment.
- The majority of the spirits consumed in Australia are imported, which are estimated to account for 60.1% of domestic demand for spirits in 2013-14.
  - Spirits are usually transported in an over-proof bulk form at 75% alcohol by volume, and are then diluted to 40% alcohol by volume before being bottled domestically and sold. This form of importing applies to an estimated 70% to 80% of spirits imported into Australia, and reduces the cost of transporting the product. The price of over-proofed spirits is largely dependent on exchange rates.
  - Australia is a significant net importer of spirits, and is expected to remain so over the next five years.
- The Australian beer industry has a significant trade deficit due to the low levels of exports of local beer, accounting for only approximately 1.1% of the industry.



Wine Industry trade balance



Spirit Industry trade balance

Competitive Landscape

The wine industry is the least consolidated sector within alcohol manufacturing which reduces its ability to leverage economies of scale and command margin from a highly consolidated wine retail sector.

- The four largest Australian wine producers account for 40.8% of industry revenue.
- The top four players in the spirits industry are estimated to account for about 65% of industry revenue.
- The market share of top two major beer manufacturers is 82.7% of industry revenue

Retailer margins

Retailers generate most margins on wine sales than sales from beer and spirits. Wine sales provide two to three times more margin than beer. This has been confirmed by Woolworths Liquor Group as shown in a presentation slide below. The ability of retailers to extract greater margins from wine can be a reflection of the highly fragmented industry structure and ease of transferring costs to wine producers.

Compulsory levies[5]

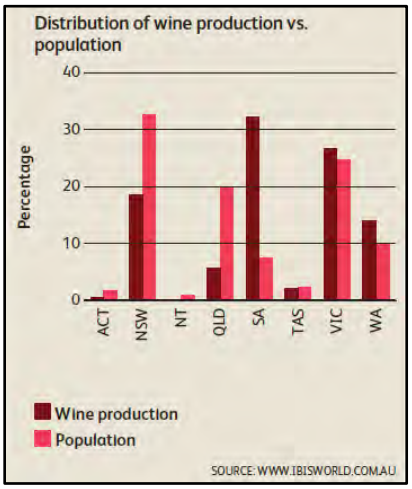
There are currently three levies/charges on wine/grapes. The grape research levy; the wine export charge; and, the wine grapes levy. These industry levies/charges fund marketing, research and development and plant health programs for the grape and wine industry. As of 2012/13, the total levy receipts from the grape research levy, wine grapes levy and wine export charge amounted to $17.12 million. Neither the spirits nor the beer industries are subject to compulsory industry levies/charges such as these.

[5] http://www.agriculture.gov.au/ag-farm-food/levies/categories/winegrapes

Regional benefits

The wine industry contributes the highest value to regional economies by generating employment and economic activity. The Productivity Commission's report in April 2014 on Geographic Labour Mobility highlighted the challenges facing regional growth, and agricultural manufacturing sectors such as wine grape production and winemaking play a vital role in the socio-economic fabric of many non-metropolitan regions. While the industry's proximity to vineyards limits transport costs to source raw materials, the long distances from vineyards to metropolitan areas and distribution centres results in significantly higher transport costs to markets and end-consumers.

The geographic spread of wine production is closely correlated with the distribution of wine grape production.



Wine industry business locations

Wine production facilities are often located at or near vineyards to limit transport costs and ensure the freshest grapes are crushed. Of those employed in the industry, just 29% work in metropolitan areas, with nearly 62% in inland regional areas. This reflects the location of grape growing and wine production facilities.

Capital Intensity

Looking at the snapshot below, it is apparent that wine is more capital intensive than beer in most stages of the supply chain:

- Wine's fermentation equipment/machinery are used two to six cycles a year while beer's fermentation equipment are used 50 cycles a year in a commercial brewery.
- Wine's maturation stage can range from 2.6 months to 16 months while storage of beer can be from one to six weeks (commercially produced typically one to two weeks).
- Between bottling and selling, wine needs to be stored before it gets ready for sale from one to three years in a cool storage, while beer is sold after bottling.
- Wine's supply chain is also less flexible than beer since it only has a once-a-year production that needs to be crushed in six to eight weeks. On the other hand, barley can be stored and converted to malt throughout the year as needed and only takes one week to process.

SNAPSHOT OF CAPITAL INVOLVED IN THE WINE AND BEER INDUSTRIES

WINE

	GRAPE GROWING	CRUSH	FERMENT	MATURE *			BOTTLE	HOLD/STORE	SELL
Description	Grapes are grown and supplied to the winery. The management of a perennial crop like grapevines is more capital intensive than an annual crop.	Wineries crush their entire year's production in 6 to 8 weeks	Equipment/machinery are used 2-6 cycles a year	Short maturation	Long maturation	Total maturation	Wine is bottled once winemaker is satisfied with wine	Depending on the type of wine, it is stored before it gets ready for sale	Wine is sold to on/off premise
Duration	Minimum of 4 years to get a viable crop	6-8 weeks	2-6 weeks per cycle	Common - 1.7mths Premium - 1.6 mths Luxury - 4.2 mths	Common - 0.9mths Premium - 6.8mths Luxury - 11.8mths	Common - 2.6mths Premium - 8.4mths Luxury - 16mths	2 weeks	1-3 years	
Capital involved	cost of trellising	crusher	fermenter	refrigerated stainless steel tanks / non-oak maturation	oak		bottling facilities	cool storage	

*there will be variations depending on type of wine

BEER

	GRAIN PRODUCTION	STORE	BREWING/FERMENT	MATURE	BOTTLE	SELL
Description	Annual barley crops, these require subsequent processing into malt which takes a week.	Malt storage is less costly than wine storage; needs to be weather and insect/rodent proof but no temp control or cover gas needs.	Brewing plant typically does 8 brewing cycles in a 24 hour day. Fermentation equipment/machinery are used 50 cycles a year in a commercial brewery (i.e. weekly turnaround).	Beer needs to sit in storage at 0C for at least a week before subsequent filtration and processing to get it ready for bottling. This provides physical and organoleptic stability. Oxygen must be kept from the product at all cost once fermentation has completed.	Beer is prepared to end product specification and is passed for bottling after organoleptic assessment	Beer is a fresh product and is best consumed fresh. Shelf life out to 12 months, but beer needs cooler (under 25C storage and should be kept away from light.
Duration	Short harvest but need to store the annual grain requirement	Barley is converted to malt throughout the year as needed.	Brewing is typically an 8 hour event and fermentation cycle is one week.	Storage of beer can be from one to six weeks. Commercially typically 1-2 weeks.	typically 24 x 5 production on keg, can and bottle lines all year.	0
Capital involved	farming, growing, harvesting and grain storage costs	maltings plant and grain storage	brewing plant, and stainless steel vessels and line for fermentation and yeast management	Tanks are stainless steel construction, refrigerated and with CO2 cover gas. Use centrifuges to separate yeast from beer, heat exchangers and filtration systems to chill, filter and carbonate to end product specification. Need pressurised tanks for final product pre bottling.	High speed 900bpm bottle and up to 2000 CPM on cans. Most beer pasteurised in package, some will be aseptically filtered and bottled. Coopers products required several weeks controlled temp storage before they can be released to trade due to secondary in bottle fermentation.	Distribution warehouse

Nature of capital[6]

A typical Australian wine producer is likely to have more difficulty accessing capital due to the small scale of operations, lack of diversity and level of risk associated with industry earnings. In general, capital requirements for the wine industry are widely described as being greater, relative to the beer and spirit industries, due to vertically-integrated wine producers requiring the use of vineyards and winemaking facilities. Furthermore, the industry has a longer stockholding period than the beer industry, increasing requirements for working capital. Returns for winemakers on capital have been declining over the past four years, due to the lower levels of profitability and higher levels of capital required.

Access to capital

Access to capital for any business is impacted by a wide range of factors such as:

a) the scale and diversity of the business (geography and product range)
b) age and maturity of the business
c) strength of the brand
d) market share and position
e) distribution channels to market
f) current level of interest bearing debt
g) variability/consistency of return, and
h) management strength and capability.

The scale of a business' operation is a critical factor to the accessibility of debt or equity capital. Larger businesses with a high degree of product and geographic diversification may find accessing capital easier.

Access to capital is a significant challenge for winemakers in Australia as they tend to be small in scale and lack diversity relative to global beer and spirit operations. Smaller, privately held companies may typically source equity capital from private investors (e.g. friends and family) and may source debt financing in the form of small trade loans from banks and financing lease arrangements for plant and machinery.

Wine businesses in the early stage of the lifecycle are likely to be purely equity funded with only the more established businesses able to attract a limited amount of bank debt. This debt would tend to be short term in nature with annually renewable debt most likely, although funding of up to three years is possible for the stronger, more established businesses. This contrasts with a beer and spirits multinational that could potentially access long-dated debt (i.e. 7-10 years). For an Australian winemaker, equity would typically come from private investors and be limited in volume.

Small businesses within the wine industry do not typically lend themselves to being operated as public corporations (which enable easier access to equity capital), and are mainly run as small scale, privately owned businesses for the following reasons:

a) the high capital intensity of the industry
b) the high level of agricultural risk
c) wine producers only have one production opportunity per year which increases risk
d) wine producers have a high inventory holding requirement which requires capital, and
e) the industry has historically generated low returns on invested capital.[7]

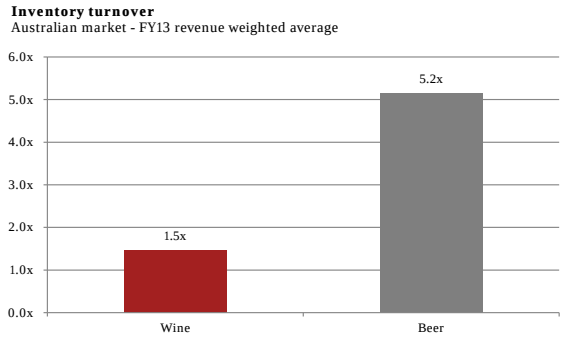
[6] This section on the comparative analysis of the nature of capital in the beer and spirits was provided by PwC.
[7] John Angove, the Managing Director of Angove Family Winemakers, L. Lockshin, Future opportunities and challenges for the South Australian wine industry: An interview with John Angove, Wine Economics and Policy 2 (2013) 50-54, 5 May 2013

Capital requirements

Capital requirements for the wine industry are widely described as being greater, relative to the beer and spirit industries. In general, wine producers are vertically integrated and therefore require the use of vineyards and winemaking facilities.

Furthermore, given the longer holding period of inventory in the wine industry relative to beer and other beverage producers, a higher level of working capital is required. As set out in the chart below, the wine industry in Australia has an inventory turnover of approximately 1.5 times (implying that on average, a business holds enough inventory to satisfy 65% of total sales for the year), whereas the Australian beer industry has an inventory turnover of approximately 5 times (implying on average, 20% of total annual sales could be satisfied with inventory on hand).

Fig. 1. Chart of weighted average inventory turnover across the Australian wine and beer industries



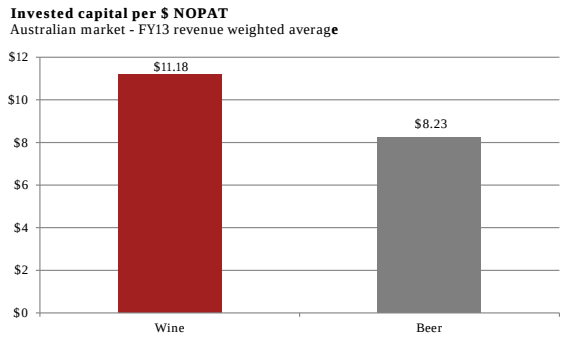
Source: S&P Capital IQ, ASIC, IBIS World, PwC analysis

Note:
1. Inventory turnover is calculated using the formula: cost of goods sold/inventory
2. Based on the average of inventory turnover from financial year 2011 (FY11) to FY13
3. The weighted averages have been calculated based on the FY13 revenue of each company
4. Based on the analysis of 16 Australian wine companies (3 public and 13 private) and 3 Australian beer companies (2 public and 1 private)

Based on available financial data for respective wine and beer companies in Australia, at a high level, the amount of invested capital required to generate a dollar of net operating profit after tax (NOPAT, or profit) appears to be higher in the Australian wine industry than in the Australian beer industry. Over the last three years, the average level of invested capital required to generate a dollar of profit is approximately $11 in the wine industry, whereas the amount of invested capital required to generate a dollar of profit in the beer industry is approximately $8.[8] Given a considerable portion of the smaller brewers across the Australian beer industry are privately held, there is a limited amount of financial information that can be used to draw conclusions. Conclusions and figures presented here should therefore be considered in light of this limitation.

[8] Based on the analysis of 16 Australian wine companies (3 public and 13 private) and 3 Australian beer companies (2 public and 1 private)

Fig. 2. Chart of weighted average invested capital per profit across the Australian wine and beer industries

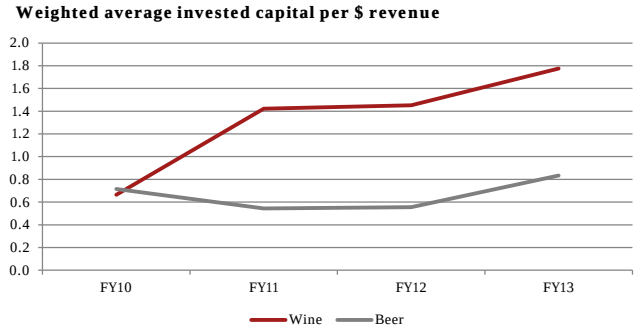


Source: S&P Capital IQ, ASIC, IBIS World, PwC analysis

Note:
1. Invested capital per $ NOPAT is calculated using the formula: Invested capital/NOPAT
2. Invested capital = Long term debt + Equity (Book value of equity for private companies and market capitalisation at the end of each financial year for public companies)
3. NOPAT = EBIT*(1 – Tax). Tax is assumed to be 30%, in line with the Australian statutory company tax rate
4. Based on the average invested capital per NOPAT from FY11 to FY13
5. The weighted averages have been calculated based on the FY13 revenue of each company
6. Companies with negative NOPAT are assumed to have zero invested capital per $ NOPAT
7. Based on the analysis of 16 Australian wine companies (3 public and 13 private) and 3 Australian beer companies (2 public and 1 private)

The level of capital used in the Australian wine industry has increased over the past four years, and by a higher amount than the beer industry. The charts below illustrate the average level of invested capital that was required to generate one dollar of revenue, gross profit and net income respectively. Each chart illustrates the increasing level of required capital to generate a dollar of each metric.

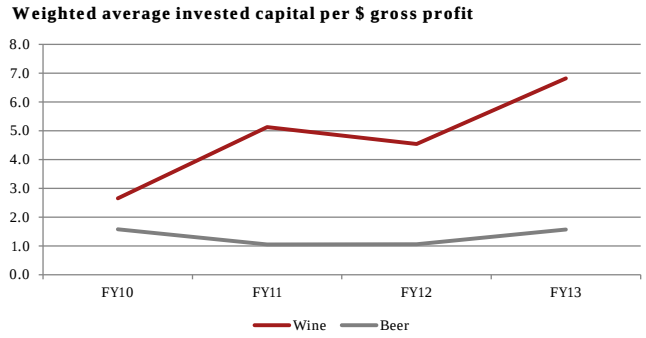
Fig. 3 Weighted average level of invested capital per dollar of revenue generated from FY10 through to FY13, based on a small sample of 14 Australian wine businesses and 3 Australian beer businesses



This chart illustrates that on average, capital invested in Australian wine businesses to generate a dollar of revenue has increased over the past four years from $0.66 in FY10 to $1.78 in FY13 compared to the average beer business, which has increased from $0.72 to $0.83 over the same period.

Source: S&P Capital IQ, ASIC, IBIS World, PwC analysis

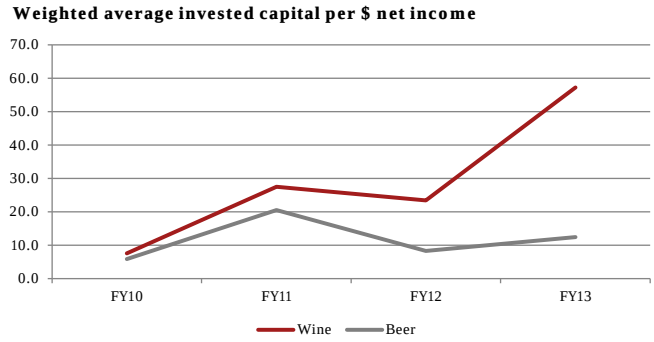
Fig. 4. Weighted average level of invested capital per dollar of gross profit generated from FY10 through to FY13, based on a small sample of 14 Australian wine businesses and 3 Australian beer businesses



On average, the level of capital invested in Australian wine businesses required to generate a dollar of gross profit has increased over the past four years from $2.66 in FY10 to $6.81 in FY13, relative to beer which has remained broadly flat over same time period.

Source: S&P Capital IQ, ASIC, IBIS World, PwC analysis

Fig. 5 Weighted average level of invested capital per dollar of net income generated from FY10 through to FY13, based on a small sample of 14 Australian wine businesses and 3 Australian beer businesses



Over the last four years, the amount of capital invested to generate a dollar of net income for a wine business has increased from $7.56 in FY10 to $57.19 in FY13, relative to a beer business which has increased from $5.88 in FY10 to $12.43 in FY13.

Source: S&P Capital IQ, ASIC, IBIS World, PwC analysis

Note:
1. Companies with negative net income are assumed to have zero invested capital per $ net income for the purpose of this analysis

Return on capital

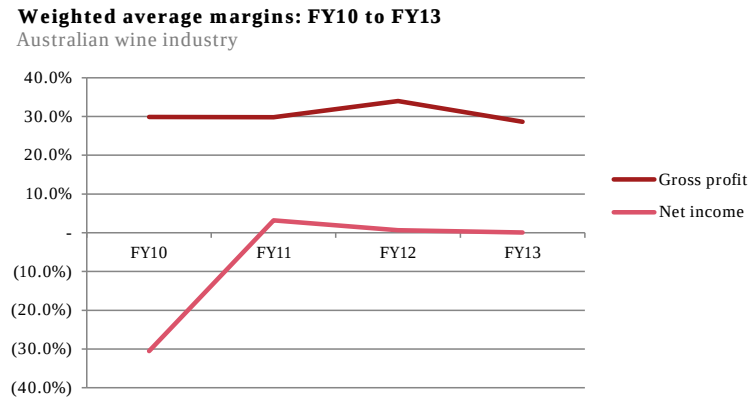
The ability for a business to generate the appropriate level of return (relative to the level of risk) is influenced by specific industry dynamics such as the:

a) level of competition within the market (e.g. level of fragmentation or consolidation)
b) level of supply and demand for the product
c) bargaining power of buyers
d) level of capital intensity.

Each of these factors is likely to contribute to the low level of returns observed in the wine industry today.

As set out in the chart below, profit margins have been falling over the past three years in the Australian wine industry.

Fig. 6. Weighted average profit margins (gross margin and net income margin) from FY10 through to FY13, based on a small sample of 14 Australian wine businesses



Source: S&P Capital IQ, ASIC, PwC analysis

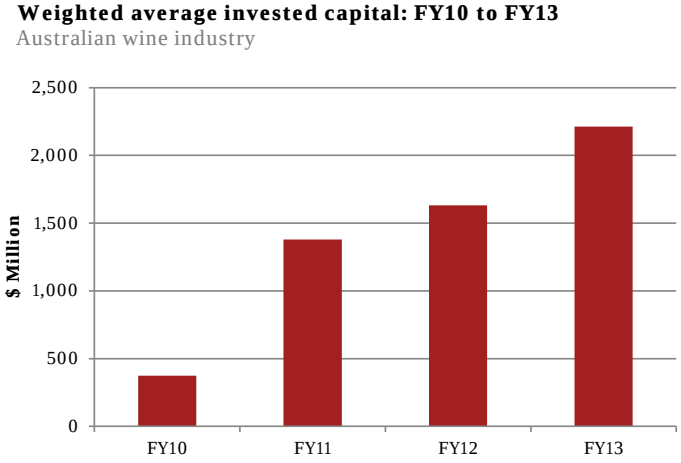
Declining profit margins are in part driven by the domestic oversupply of wine, which has resulted in heavy discounting throughout the supply chain. In addition the profitability of wine producers has been negatively impacted by:

a) the increasing dominance and bargaining power of supermarket retailers
b) the high Australian dollar, reducing the competitiveness of Australian wine in foreign markets[9]
c) fragmentation of the industry leading to difficulties in pricing growth.[10]

Profit margins across the Australian wine industry are expected to be approximately 5.4% in 2014-15, being significantly lower than the average profit margin of the beer and the spirit manufacturing industry of 16.0% and 13% respectively.[11]

In comparison, as set out in the chart below, the average level of capital employed (long-term debt financing, plus equity) has increased over the comparable period.

Fig. 7. Weighted average level of invested capital from FY10 through to FY13, based on a small sample of 14 Australian wine businesses



The average amount of capital invested (debt and equity) in a wine business (based on a small sample of businesses in the wine industry) has increased from $375 million in FY10 to $2,214 million in FY13. However, this chart does not take into consideration the level of productivity or output generated by the increase in invested capital.

Source: S&P Capital IQ, ASIC, PwC analysis

[9] Wine Production in Australia, IBISWorld Industry Report, August 2014
[10] Treasury Wine Estates Limited, UBS Broker Report, 25 June 2014
[11] Wine Production in Australia, IBISWorld Industry Report, August 2014

Given these trends, the declining profit margins and increasing levels of invested capital, returns on capital for the wine industry have been reducing over the past 5 years, as illustrated below.

Fig. 8 Weighted average level of return on invested capital (ROIC) generated from FY10 through to FY13, based on a small sample of 14 Australian wine businesses and 3 Australian beer businesses

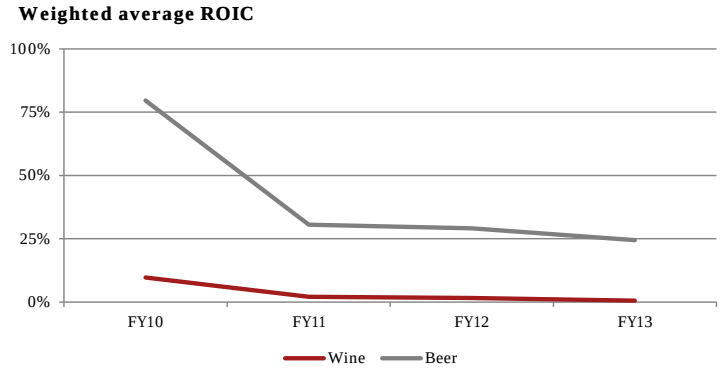
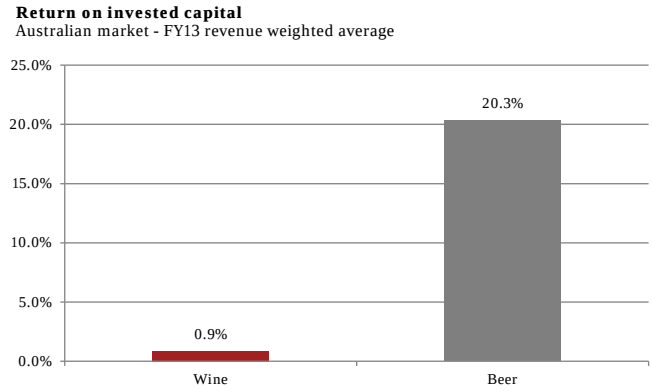


Figure 8 illustrates the average return on capital invested across businesses in wine and beer industries has declined over the last 4 years. Based on the small sample of companies analysed, returns in the beer industry are generally greater than the wine industry. On average, in FY13, the return on invested capital was approximately 25% for beer companies, compared to 0.6% for wine businesses.

Source: S&P Capital IQ, ASIC, PwC analysis

The average return on invested capital (ROIC) in the Australian wine industry is less than 1% which compares to the average ROIC in the Australian beer industry of approximately 20.3%.[12] This implies that for every $100 of capital invested in the wine industry, a wine business (on average) generates $1 of profit (NOPAT), whilst for every $100 of capital invested in the beer industry, approximately $20 of profit is generated. Please note there is limited data available for Australian beer companies and these figures should be considered in light of this limitation.

Fig. 9. Chart of weighted average return on invested capital across the Australian wine and beer industries



Source: S&P Capital IQ, ASIC, IBIS World, PwC analysis

Note:
1. ROIC is calculated using the formula: NOPAT/ Invested capital
2. NOPAT = EBIT*(1 – Tax). Tax is assumed to be 30%, in line with the Australian statutory company tax rate
3. Invested capital = Long term debt + Equity (Book value of equity for private companies and market capitalisation at the end of each financial year for public companies)
4. Based on the average of ROIC from FY11 to FY13
5. The weighted averages have been calculated based on the FY13 revenue of each company
6. Based on the analysis of 16 Australian wine companies (3 public and 13 private) and 3 Australian beer companies (2 public and 1 private)

[12] Based on the analysis of 16 Australian wine companies (3 public and 13 private) and 3 Australian beer companies (2 public and 1 private)

Risk rating[13]

Risk component	Wine	Spirit	Beer
Structural risk (25%)	6.48	4.48	3.25
Growth risk (25%)	5.88	5.37	5.54
Sensitivity risk (50%)	6.37	6.4	6.7
Overall risk	**6.27**	**5.66**	**5.55**

The wine industry has the highest overall risk among alcohol producers at 6.27 (out of 9) which is due to high levels of structural and sensitivity risks. The wine industry's risk rating is higher than the average risk score for all Australian industries and the manufacturing sector. The main structural risk factors for the industry include high level of competition, decreasing exports and a high level of revenue volatility due to changes in grape supply and prices, in addition to the influence of intra-industry competition. Both spirit and beer industries are have low volatility risks due to the ability to mitigate effects of market fluctuations, a steady consumer base and high profit margins.

Global Wine and Alcohol Taxation[14]

Domestic taxation rates on wine are important in ensuring the stability and growth required to develop strong brands and business models that can be confidently taken into the highly competitive and volatile global marketplace. It is critical for local taxation rates to be comparable to global competitors to ensure we continue to grow a globally competitive industry and produce world-renowned wines.

An analysis of how Australia's wine taxes compare internationally however shows that Australia is taxing wine relative to other alcoholic beverages more than most other wine-exporting countries. It is also important to note that wine is taxed lower than other alcohol beverages in the vast majority of wine exporting countries.

The key findings to emerge from this analysis are:

- For commercial premium wines (the sort that would retail at twelve dollars), Australia's 29% WET is one of the highest tax rates among the significant wine-exporting countries: France has 0.8%, Italy 0%, Spain 0%, Argentina 0%, Chile 15%, South Africa 3.8% and the United States 6.6%.

- When expressed in Australian cents per standard drink of alcohol, Australia's wholesale tax for commercial premium wines (22 cents) is marginally lower than New Zealand's 26 cents, but at any higher price point Australia's tax exceeds New Zealand's. That 22 cents tax in

[13] To calculate the overall risk score, IBISWorld assesses the risks pertaining to industry structure (structural risk), expected future performance (growth risk) and economic forces (sensitivity risk). Risk scores are based on a scale of 1 to 9, where 1 represents the lowest risk and 9 the highest. The three types of risk are scored separately, then weighted and combined to derive the overall risk score.

[14] Anderson, K., 2014. Excise Taxes on Wines, Beers and Spirits: An Updated International Comparison, Adelaide: Wine Economics Research Centre Univeristy of Adelaide.

Australia compares with zero in Argentina, 3 cents in South Africa, 5 cents in the United States, and just 1 cent in France and zero in the other Old World wine-exporting countries.

- Analysis also shows when expressed as a percentage of those for other beverages, wines are taxed less than spirits in all but Japan, and are taxed at a similar or lower rate than beer in all but a handful of countries. Again, Australia is taxing wine higher relative to other alcoholic beverages more than most wine-exporting countries, the main exception being Chile where beer is very lightly taxed.

Summary

We have outlined in detail the various commercial and structural challenges facing the wine industry and the numerous ways in which the wine industry is at a competitive disadvantage relative to beer and spirits manufacturing. Globally, Australian wine taxes are already high but our approach of taxing wine less than other forms of alcohol is consistent with our competitors.

Given these findings, WFA submits the wine sector should continue to receive a differentiated tax rate to other alcohol beverages. To introduce tax increases on the sector would jeopardize its recovery and its ability to grow strong brands and businesses that can compete globally.

Recommendation: Wine should continue to receive a differentiated rate to other alcohol types.

The production and capital risks, economic footprint and industry structure of the wine, spirits and beer industries are very different and tax regimes should recognise and reflect these differences. Just because they are all producers of alcohol, this does not mean they should be taxed at similar levels.