THE GLOBAL WINE INDUSTRY

How small Chilean wineries should compete

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CHILEAN WINE REGIONS

Foreword

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Table of Contents

1. Introduction

Since the late 1970s the world wine market has witnessed some important shifts. The so-called New World has acquired a substantial share of the market, mainly under influence of branded wines from Australia and the US, but countries such as Chile, New Zealand, Argentina and South Africa have also increased their market share. This has threatened the age old comfortable positions held by the established wine producing nations of the so-called Old World; France, Italy, Spain, Germany, and to a lesser extent Portugal.

The rise of the New World has caused a few important changes, beginning with an increasing level of production leading to a much wider range of different wines on offer, which in turn has led to consumer confusion. Consumption levels have been substantially below production levels, causing excess supply and increased competition among producers. Because of, or perhaps in part due to the above, New World nations -especially Australia and the US- have rightfully recognized the importance of marketing and branding. However, increased competition has also strengthened the position of –ever larger- distributors, importers and supermarkets vis-à-vis producers.

Although Chile is part of this group of New World countries, it is very different from some of the other New World producers. Where the New World nations are generally renowned for their use of marketing and branding, this is not the case for Chile. The country's major problem is considered to be its lack of *country image*; not only considering wine, but for every product it exports[1]. Furthermore, Chile's wine industry has a strong competitive position compared to other major wine exporting nations, with certain distinct advantages and disadvantages.

Within this environment, -both the world market and within the Chilean industry setting- there are a number of smaller Chilean wineries which are mainly focused on higher quality exports for their survival. Many of these are struggling however, and the aim of this paper is therefore to investigate why they are struggling, how this might be connected to the lack of country image, or *Brand Chile*, and how these companies could become more successful. The central question of this thesis is:

What are the effects of country image on the performance of smaller Chilean Wineries and what strategies could these wineries pursue in order to become more successful on the export market?

[1] Except perhaps copper, Chile's number 1 export product.

This paper is divided into four parts. First of all, a macro view of the world wine market and its main players shall be given, especially in relation to Chile. Then, the Chilean wine sector shall be thoroughly discussed, including its main advantages and disadvantages versus other important exporting nations. The findings of these shall be applied to a theoretical chapter on business strategy, marketing and branding aimed at the wine business. The final part of the paper will look at the case of the small Chilean wineries and their position in both the Chilean wine industry, as well as on the world wine market. Through the use of interviews and questionnaires I hope to have sufficiently identified the main threats to, and weaknesses of these wineries, as well as offer some possibilities to improve their strategies in order to become more successful, especially in relation to a country image.

2. The World Wine Market

This chapter aims to analyse the world wine market. The first paragraph offers a short description of the product wine, followed by a paragraph consisting of a thorough investigation of the global wine industry, including its main players in terms of production, exports and consumption, and their relation to Chile.

2.1. The Art of Making Wine

The art of making wine is estimated to be over 6000 years old. It is unclear where wine making was first discovered, but the most probable locations are thought to be Mesopotamia, the Middle East or the Caucasus. Wine was then introduced to Egypt, Greece, Spain (by 2500 B.C.), Southern Italy and Sicily by the seafaring Greeks and Phoenicians. The Romans brought wine to France around 600 B.C., from which it spread further north in the first and second century B.C (Anderson et al, 2003). It should be noted that the wine drunk in those days was in no way comparable to what is considered wine nowadays. It wasn't until the end of the 18th century, when the glass bottle was introduced, that wine could be properly preserved (Terheijden, 2005).

The process of making wine can be divided into two important parts: *viticulture* and *vinification.* Basically, viticulture means everything that goes on in the vineyard and vinification is what goes on in the wine cellar (Dominé, 2003). An important aspect of making wine is called *terroir.* Terroir does not only mean the type of soil, but also the amount of minerals the soil contains, the quantity of sun the vines receive (the vineyards location and altitude) and the micro-climate (temperature, humidity, wind, etc). Apart from terroir, there are other aspects of the *viticulture* process that influence the quality of the wine. The way vines are planted, kept and watered plays an important part, as well as the quantity of planted grapes per hectare. The lower the quantity planted, the better the quality of the wine. Other important factors are the date of harvest and the grape variety. The *vinification* process also affects the wine, including the fermentation process, and whether –and for how long- the wine is ripened in stainless-steel tanks (either with or without added oak chips) or in oak barrels. If the goal is to make a blended wine, then it should be decided which grape varieties should be used and in what quantities. A wine made of a single grape variety is called a *varietal* or *single variety wine* (Terheijden, 2005).

Red wines are made from blue (dark) grapes. Both skins and pulp are used in the fermentation process for red wines. White wines on the other hand can be made from both white and blue grapes, but the juice should be separated from the skins before fermentation. Rosés or pink wines are made the same way as white wines, but the juice is coloured from short contact with dark skins before fermentation (Robinson, 2003).

Although there are many grape varieties in the world used to produce wine, the following table shows the most widely used, along with the countries most famous for producing them.

Table 1: Important Grape Varieties and Country

Grape Variety	**Red/White**	**Country**
Cabernet Sauvignon	R	Australia, *Chile*, France, US, South-Africa
Carmenère	*R*	*Chile*
Chardonnay	W	Australia, *Chile*, France, Italy, US, South-Africa
Chenin Blanc	W	France, South-Africa
Colombard	W	Australia, France, US
Malbec	R	Argentina
Merlot	R	France, Italy, New World
Pinotage	R	South-Africa
Pinot Blanc	W	Germany, France
Pinot Noir	R	Germany, France, US
Riesling	W	Germany, France, Austria
Sangiovese	R	Italy
Sauvignon Blanc	W	Australia, *Chile*, France, New-Zealand, US, South-Africa
Sémillon	W	Australia, France, US
Syrah	R	Australia, France
Tempranillo	R	Portugal, Spain
Zinfandel	R	US

Source: Productschap wijn, 2007

2.2. The World Wine Industry

The World Wine Industry is highly fragmented compared to the beer and spirits industries; wine is produced by a large number of individual wine companies that each aim to realise maximum returns. Nevertheless, when numerous companies in one country fail to make the timely adjustments required by the market, the entire country is set to lose market share. It appears that the particular environment within a country can either serve as a stimulant or a barrier for companies to change in order to adjust to a changing market environment. The industry has consequently been faced with major shifts in competitiveness among its supplying countries (Heijbroek, 2007). At the same time major distributors have increased their bargaining power. Although this seems bad news for exporting wineries, exports have been increasing year over year. In the Chilean case the focus on exports is even greater, due to its relatively small domestic market.

The Industry has undergone some important changes the past decades. First of all, the ascendancy of the New World Producers, -Australia, New Zealand, The US, Chile, Argentina and South Africa-, has been considerable, threatening the comfortable positions held by the Old World Wine producers -France, Spain, Italy, Germany, and Portugal-. This has meant an increase in competition. Furthermore, production levels have been considerably higher than consumption levels the past few years, leading to a global over-supply of wine putting downward pressure on prices, especially in the (popular) premium segments. This means that Chilean producers will have to move to higher market segments (Visser and de Langen, 2006). Consumer demand has also shifted towards higher price segments. In short, both demand and supply have clearly changed tremendously.

Furthermore, the 1990s saw a transition from traditional supply-driven production to market-orientated types of wine and business models. The suppliers who were first to recognise these changes, in particular certain New World countries such as the US and Australia, enjoyed excellent growth opportunities (Heijbroek, 2007).

2.2.1. Production

Table 2 shows production levels and percentage change between 2005 production and the average production for the period 1996-2000 for the 15 largest wine producers. As can be seen from this table, Chile’s production increased 55.76% between 2005 and the average production level of 1996-2000. Only Russia and Australia did better with 59.25% and 89.71% respectively.

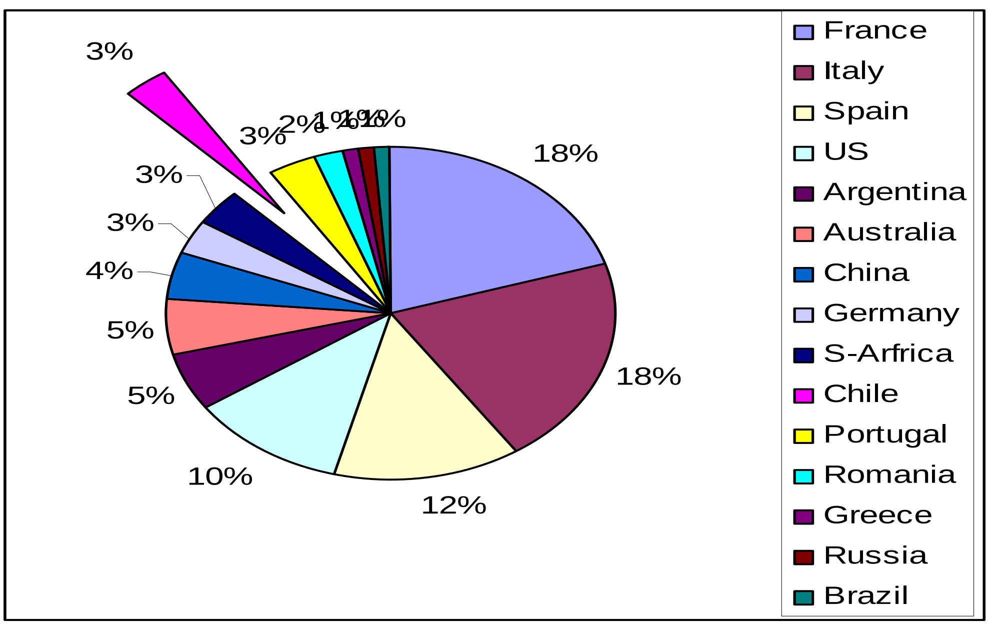
Table 2: World Wine Production of top 15 Producers (in hectolitres * 000)

Country	**96-00**	**2001**	**2002**	**2003**	**2004**	**2005**	**% change 2005/ (96-00)**
France	56,271	53,389	50,353	46,360	57,386	52,004	(7.58%)
Italy	54,386	52,293	44,604	44,086	53,000	50,566	(7.04%)
Spain	34,162	30,500	33,478	41,843	42,988	34,750	1.72%
US	21,381	23,944	24,648	24,156	24,947	28,692	34.19%
Argentina	13,456	15,835	12,695	13,225	15,460	15,222	13.13%
Australia	7,380	10,347	11,509	10,194	13,810	14,000	89.71%
China	9,581	10,800	11,200	11,600	11,799	12,366	29.06%
Germany	9,989	8,891	9,885	8,191	10,047	9,100	(8.90%)
S-Africa	7,837	6,471	7,189	8,853	9,280	8,410	7.31%
Chile	*5,066*	*5,658*	*5,623*	*6,682*	*6,300*	*7,890*	*55.76%*
Portugal	6,828	7,789	6,677	7,340	7,481	7,254	6.24%
Romania	6,173	5,090	5,461	5,555	5,500	5,600	(9.28%)
Greece	3,382	3,477	3,085	3,799	4,295	4,093	6,81%
Russia	2,512	3,430	4,060	4,530	4,000	4,000	59.25%
Brazil	2,920	2,968	3,212	2,620	3,930	3,200	9.59%
World Total	**270,826**	**269,719**	**260,508**	**267,441**	**301,933**	**286,175**	**5,67%**

Source: The Wine Institute (2007)

Figure 1 shows the 2005 production level of the same countries as a percentage of total world production in 2005:

Figure 1: Production percentage of top 15 Producers (2005)



Source: The Wine Institute (2007)

The main producers are France and Italy (both 18%), followed by Spain (12%) and the US (10%). Chile accounted for 3% of the world's total wine production in 2005, occupying a 10 Th or 11th position.

As said, a distinction is often made between New World and Old World wine countries. Old world wine countries are essentially the biggest European producers (and exporters): France, Italy, Spain, Germany and Portugal. The New World consists of all wine producing countries which are not part of the Old World. The most important proponents of the New World are Australia, New-Zealand, South-Africa, Argentina, Chile and the US (California). Although China is the fourth largest producer, it is often not considered to be among the most important New World players on the World market because of its low export percentage (less than 1% of production). The term New World does not necessarily mean that these countries have recently begun to produce wine, as wine has been produced in Chile since the 16th century, in South-Africa since the 17th, and in Australia and New-Zealand since the 18th and beginning of the 19th century respectively. The most important New World countries are not only former colonies of European nations, but the term refers mainly to their fairly recent success on the world export market. This process started in the late 1970s when a legal change made it possible for the first time to sell wines in British supermarkets (one of the most attractive export markets), a possibility which was seized immediately by Australian wine producers. Later other wine producing countries followed suit and other importing countries opened up their (super) markets as well (Terheijden, 2005).

As can be seen from table 2, worldwide production of wine has grown only a little over 5% between 2005 and the average for 1996-2000. However, it is clear that most Old World countries, except Spain, have produced less, whereas New World countries have been increasing their production, especially Australia and South Africa. Table 3 shows that between 2001 and 2005 the Old World countries saw their share of production decrease from 57% to 54%, whereas the New World share of production increased from 23% to 28% without even counting New Zealand.

Table 3: % Share of World Production per Country

	2001	2002	2003	2004	2005
France	19.8	19.3	17.3	19	18
Italy	19.4	17.1	16.5	17.6	18
Spain	11.3	12.9	15.6	14.2	12
Germany	3.3	3.8	3.1	3.3	3
Portugal	2.9	2.6	2.7	2.5	3
Total Old World	**56.7**	**55.7**	**55.2**	**56.6**	**54**
Australia	3.8	4.4	3.8	4.6	5
US	8.9	9.5	9	8.3	10
S-Africa	2.4	2.8	3.3	3.1	5
Chile	*2.1*	*2.2*	*2.5*	*2.1*	*3*
Argentina	5.9	4.9	4.9	5.1	5
Total New World	**23.1**	**23.8**	**23.5**	**23.2**	**28**
Total N W + O W	**79.8**	**79.5**	**78.7**	**79.8**	**82**

Source: The Wine Institute (2007)

Another way of looking at wine production is by looking at acreage planted. Table 4 shows the acreage changes of the most important Old and New World countries, as well as China.

Table 4: World Wine Acreage (acres x 1000) of Old and New World Countries

Country	**96-00**	**2001**	**2002**	**2003**	**2004**	**2005**	**% change 2005/(96-00)**
France	2,262	2,224	2,219	2,191	2,162	2,134	(5.65%)
Italy	2,246	2,204	2,155	2,145	2,120	2,110	(6.05%)
Spain	2,925	2,992	2,969	2,982	2,990	2,990	2.22%
Germany	258	255	252	252	252	252	(2.39%)
Portugal	636	613	615	616	615	615	(3.23%)
Australia	263	366	392	389	400	440	67.44%
US	930	1,052	1,026	951	933	935	0.52%
S-Africa	276	311	319	326	320	320	16.09%
Chile	*363*	*447*	*455*	*457*	*465*	*465*	*28.33%*
Argentina	514	506	513	520	520	520	1.23%
NZealand	26	38	42	48	50	55	90.49%
China	538	887	1,040	1,119	1,100	1,150	113.76%
Total	**18,942**	**19,397**	**19,473**	**19,409**	**19,391**	**19,462**	**2.12%**

Source: The Wine Institute (2007)

Here we see the same trend: The Old World has diminished its acreage (except for Spain), whereas the New World, especially Australia and New Zealand, have increased their acreage substantially. China has increased its acreage more than any other country in the world and is now in 4^{th} position concerning total acreage, trailing the Old World nations of France, Italy and Spain, but still produces large quantities of low quality wine aimed almost entirely at local consumption. Considering acreage increase, Chile scores a fourth position with an acreage growth of 28.33% between 2005 and the average of 1996-2000, just behind Australia (67.44%), New Zealand (90.49%) and China (113.76%).

It should be mentioned however, that part of the European acreage and production stagnation can be explained by EU policy. Under the EU's wine regime, the planting of vines is strictly regulated and controlled in terms of acreage and allowed varieties. Controls remain in place to encourage the production of quality wines while discouraging the production of those of poor quality. New plantings of wine grapes are prohibited until July 21, 2010, except under certain circumstances -for example, in some areas old grape varieties are being taken out and new, more marketable vines are being planted- (USDA, 2006). This policy is expected to increase the quality level of European wines, as well as diminish excess supply of mainly lower quality wines, hopefully leading to a lower level of competition in the lower market segments. According to Heijbroek (2007) oversupply is expected to last at least through 2009. The uprooting policy of the EU will theoretically bear fruit after 2009 and reduce global supply. However, other EU and New World companies will seek opportunities for growth. It seems very unlikely that global supply will genuinely decline as a consequence.

2.2.2. Consumption

After a surge in wine consumption in the 1970s, consumption has been decreasing an average of 2% per capita per year since 1980, although consumption levels have been rising slightly again between 2001 and 2005. However, since the mid 1990s World wine consumption has been consistently below World wine production, and floats around 220 to 240 million hectolitres, signalling an ever larger oversupply of wine, causing competition between producers to increase. Table 5 shows the world's fifteen largest wine consuming countries and their consumption levels between 2001 and 2005.

Table 5: Top 15 Wine Consuming Countries in Volume (hectolitres 000)

	2001	2002	2003	2004	2005	% change 2005/2001
France	33,919	34,820	33,340	34,000	34,000	0.24%
Italy	30,150	27,709	29,343	28,000	28,000	(7.13%)
US	23,570	23,650	24,363	25,114	25,929	10.01%
Germany	20,044	20,272	20,150	20,200	20.200	0.78%
Spain	14,238	13,960	13,798	14,000	14,000	(1.67%)
China	11,054	11,470	11,586	11,500	12,000	8.56%
Argentina	12,036	11,988	12,338	10,150	11,500	(4.45%)
UK	9,794	9,916	10,622	11,500	11,500	17.42%
Russia	6,067	6,404	8,682	8,500	8,500	40.09%
Romania	4,705	4,964	5,050	6,000	6,000	27.52%
Australia	3,976	4,007	4,196	4,850	5,000	25.75%
Portugal	4,697	4,650	5,290	4,950	4,950	5.39%
S-Africa	3,972	3,884	3,487	3,700	3,700	(6.85%)
Netherlands	3,330	3,330	3,563	3,500	3,500	5.11%
Canada	2,800	2,884	3,440	3,450	3,470	23.92%
World	**229,409**	**230,072**	**235,458**	**236,515**	**239,877**	**4.56%**

Source: The Wine Institute (2007)

Although consumption growth has been highest in Romania and Russia, in terms of value other markets are still more interesting. Especially the US, Canada, UK, and other European nations such as The Netherlands and the Scandinavian countries have been very attractive markets for exporters. In the near future demand from Asian nations is assumed to rise significantly.

Chile occupies a 20th position on the list of major Wine consuming countries. Chilean consumption has increased 11.11% between 2001 and 2005, from 2.25 million hectolitres to 2.5 million hectolitres. With a population of 16 million, per capita consumption was around 15.6 litres in 2005 and 15 in 2006. As a comparison, French consumers drank an average of 54 litres per capita in 2006, followed by Italy with 48, Spain with 34, Argentina with 28 and Australia with 20 litres per capita (CVV, 2007). Although Chilean wine consumption increased the past five years, per capita consumption has decreased considerably over the past decades, which used to be as high as 53 litres in the sixties.

2.2.3. Exports

Although, or perhaps because of the fact that, consumption has been on the decrease and steadily under world wine production, an increasing amount of the world's wine production is being exported. As can be seen from table 5, consumption has gone down in some traditional wine producing nations, both Old World and New World, whereas consumption has been expanding in non-producing countries, mainly in Europe and East-Asia, signalling that wine is becoming much more of an internationally traded product (Anderson et al, 2003). In the beginning of the 90s only 15% of world production volume was exported, which increased to an estimated 25% around 2005. If measured in value instead of volume around 40% of world production was aimed at exports in 2003 (Anderson et al, 2003). This increase in (high value) exports can be largely attributed to the New World. Terheijden (2005) revealed six (general) critical success factors that explain the success of the New World Wine countries versus the Old World on the world export market: *organised national marketing, better price-quality ratio, a differentiated product, better use of branding, better understanding of its possibilities, and a limiting structure of the Old World Wine industry*. However, as we shall see, there are some important differences between New World producers as well.

Table 6 shows the export market shares in 2001 and 2005 (according to volume) for the major countries of both the New and Old World. The Old World's most important countries, France and Italy, have lost some market share whereas Spain, Germany and Portugal have gained market share on the export market. In total the Old World has lost market share however. The New World countries have all increased their market share on the export market, led by Australia.

Table 6: Market share Top Ten Exporters according to volume

	2001	**2005**
France	23.2%	18%
Italy	23.5%	21%
Spain	15.2%	18%
Germany	3.7%	4%
Portugal	2.6%	3%
Total Old World	**68.2%**	**64%**
Australia	5.7%	9%
US	4.4%	5%
S-Africa	2.7%	4%
Chile	*4.7%*	*5%*
Argentina	1.4%	3%
Total New World	**18.9%**	**26%**

Source: Terheijden, (2005) and USDA (2006)

Table 7 shows Old World versus New World Market shares on the export markets for 1992, 2000 and 2005 (according to volume). Again, it is clear that the New World is increasing its market share on the export market. Still, almost 60% of all the wine bottles exported in the world are from France, Italy and Spain (Ter Heijden, 2005).

Table 7: New World versus Old World Market share on Export Market according to volume

	1992	**2000**	**2005**
Old World	77%	71%	64%
New World	8%	20%	26%[2]
Rest of World	15%	9%	10%

Source: Terheijden (2005) and USDA (2006)

[2] Does not include New-Zealand

Table 8 shows both production as well as export market shares for 2005 according to the ten major Old and New World countries.

Table 8: World Production and Export Market Shares Top Ten countries (2005)

	PRODUCTION	**EXPORT (volume)**
France	18%	18%
Italy	18%	21%
Spain	12%	18%
Germany	3%	4%
Portugal	3%	3%
Total Old World	**54%**	**64%**
Australia	5%	9%
US	10%	5%
S-Africa	5%	4%
Chile	*3%*	*5%*
Argentina	5%	3%
Total New World	**28%**	**26%**
Total New W + Old W	**82%**	**90%**

Source: Terheijden (2005) and USDA (2006)

From table 3 and 6 we may infer that The Old World's share of world production decreased almost 3% (from 56.7% to 54%) between 2001 and 2005 and its export market share decreased over 4% (from 68,2% to 64%) during the same period. The New World's production share increased over almost 5% (from 23.1% to 28%) whereas its export share rose by 7.1%, from 18.9% to 26%. Chile increased its production market share by 0.9% and its export market share increased 0.3% over the same period. Although positive figures, they are both below New World average and it might be considered a problem that Chile increased its share of world production more than its share of exports, as the Chilean wine industry's main focus is the export market. At the same time, Chile's share of the export market in 2005 was 5%, still above its share of world production (3%).

A study conducted by Castaldi et al (2006) listed the competitive advantage positions of the most important exporting nations, both Old World and New World. Although we have seen that the New World's ascendancy at the expense of the Old World could be explained by six general critical success factors, Castaldi et al demonstrate that there are some major differences in competitive advantage between the New World countries themselves as well. As can be seen from the next figure, Chile scores highly on its overall competitive advantage. Although its domestic market is not considered very attractive, and is not expected to become more attractive in the near future, Chile does have a production cost advantage over other countries. Also, it scores highly on adaptability to industry change, which in the Chilean case means the willingness and ability of producers to experiment with cost saving production methods. Lastly, the country's low production costs, low country risk and perfect *terroir* make the Chilean wine industry attractive to foreign investors. These and other advantages and disadvantages of Chile will be discussed more thoroughly in the coming paragraphs.

Figure 2: Competitive Advantage Position by Nation

	Existing Domestic Market position	Domestic Market Growth Potential	Econ of Scale/Cost structure benefits	Adaptability to Industry Change	Potential to attract Foreign Investment	Overall Competitive Advantage
NW						
USA	Strong	Strong	Moderate	Strong	Strong	**Strong**
Australia	Weak	Weak	Strong	Strong	Strong	**Strong**
Chile	*Weak*	*Weak*	*Strong*	*Strong*	*Strong*	***Strong***
Argentina	Moderate	Moderate	Moderate	Strong	Moderate	**Moderate**
S – Africa	Weak	Weak	Moderate	Strong	Moderate	**Moderate**
OW						
Italy	Strong	Weak	Weak	Moderate	Moderate	**Moderate**
Spain	Moderate	Weak	Weak	Moderate	Moderate	**Moderate**
France	Strong	Weak	Weak	Weak	Moderate	**Weak**
Germany	Strong	Moderate	Weak	Weak	Weak	**Weak**

Source: Castaldi, Cholette, Hussain (2006)

2.2.4. Australia

As figure 2 demonstrates, Chile's main competitors among the New World Countries are the US and Australia. The US has a very large domestic market, whereas Australia is more focussed on exports, like Chile. As can be observed from tables 2, 4, 5 and 6 Australia has increased its production, planted acreage, domestic consumption and exports enormously over the past decades. Although the country lacks some (natural) and cost advantages enjoyed by Chile; it is considered by many among the Chilean experts as a benchmark, especially concerning the use of marketing and branding and the issue of country image.

First of all, Australia has large market shares in the world's most attractive and also Chile's biggest export markets: The UK, where Australia is market leader with 22.5% of market share (against 6.9% for Chile), and the US. Secondly, as was discussed, Australia's domestic consumption, production, planted acreage and exports have shown impressive growth rates the past years. Australian exports are above those of Chile and it also serves the higher price segments better, which translates into a higher average price per litre of exported wine. Thirdly, the Australian wine business makes better use of marketing and branding.

Australia's success can be explained mainly by the structure of the Australian wine industry, the high level of cooperation between wineries and government support. The Australian wine business is based on a clear separation between production and marketing. There is a strong will to cooperate and conduct generic R&D and market research (Australia has some fine research institutions, such as universities and research centres) which is shared freely among the wineries, leading to a more marketing and customer oriented industry than its Chilean counterpart. Lastly, the Australian government is more inclined to support the wineries, both financially and otherwise.

The country has been especially successful in branding by promoting *Brand Australia* in the wine industry through an industry-wide marketing vision and strategy (Australia 2025). The *branded wines* that have been introduced are lifting upon the image of *Brand Australia.* Australia is supposed to convey feelings of a nice life, beautiful nature and upbeat people (Terheijden, 2005). As a consequence, the Australian industry was able to build brand equity through strong positive qualitative associations (Atkinson, 1999). Another advantage of well functioning national wine promotion bureaus is that they can reach parts of the market, such as sommeliers, restaurants and even end-consumers, which are often unreachable for individual wine producers.

Other features that have characterised Australia's success are rapid technological innovation and interregional blending to produce a wider variety of well-liked wines. Because of increased competition the Australians are now trying to establish a system of geographically delimited *points of difference.* In 2005 the Australians started a campaign to educate worldwide consumers on the 65 Australian wine regions and grape varieties (Terheijden, 2005).

Through its enormous marketing and innovation capacity the Australian wine industry is not only capable of satisfying consumer needs, but has even created and satisfied *new (future)* consumer needs ((Moguillansky, Salas and Cares, 2006). This is one of the key concepts of successful marketing, which shall be discussed shortly.

2.3. Conclusion

The World Wine industry has witnessed some major competitive shifts among supplier countries since the 1970s. The New World has impressively gained market share at the expense of the Old World producers. This has led to increased production, which has been significantly above consumption levels, signalling an oversupply of wine and increased competition among wine producers worldwide, especially in the lower price segments. At the same time, the industry is still highly fragmented compared to other alcoholic beverage industries and market power of distributors has increased. Furthermore, a result of decreasing consumption in Old World producing nations combined with an increase in demand from non producing nations, has led to an increase of exports.

Within this environment, Chile has shown some impressive growth rates concerning production, planted acreage, and exports. In 2005, Chile's market share in world production was 3%, occupying a 10th position. Concerning acreage planted Chile occupied an 8th position in 2005 and the country's share of the export market was 5%, translating into a 5th position. Chile's domestic market is less attractive, which translates into low domestic consumption levels of around 15 litres per capita. This is equal to a 20th position worldwide. Nevertheless, when compared to its main competitors Chile has a strong competitive advantage position. Some key facts and figures and the strengths and weaknesses of the Chilean Wine industry will be discussed in the next chapter.

3. The Chilean Wine Industry

This chapter aims to give an overview of the Chilean Wine Industry, beginning with its history and covering its current planted acreage, production, consumption and export levels. Also, the Chilean wine industry's regional structure, the role of technology and innovation, and industry structure will be discussed. The final paragraph discusses the Chilean Wine Industry's main advantages and disadvantages.

3.1 History and Foreign Investment

Alonso Moreno is said to have been the first to ever produce wine in Chile, in 1550[3]. However, Rodrigo de Araya was the first to produce wine on a larger scale. His first production was dated March 8th, 1555. This has consequently been recognised as the official date of birth of Chile's wine industry. Grapes were harvested from the gardens of the first settlers, close to modern day Santiago and the vineyards were irrigated with water from the Mapocho River. Later, grape vines and vineyards spread south to the Maipo Valley. The grape varieties used in this period were mostly Spanish.

Chile became such an important wine producer the following centuries under Spanish rule that a decree was issued in 1654 to curtail Chilean wine expansion, as the country became too much of a threat to the Motherland. Chilean wine had quickly developed a name of being low priced and of reasonably good quality, an image still in sway today. In 1678 the Chilean governor recommended that the ban be lifted and that vineyards should be actively encouraged to establish more haciendas (Robinson, 2006). In the 18th century wine growing became an important industry –despite another production curtailing decree issued by Spain in 1767- with over 15.000 hectares planted, mostly close to the major cities.

After Chilean independence in 1850, a new period of expansion commenced and France became the new example, not only in terms of culture and architecture, but also concerning vineyards. This meant a shift from Spanish to French grapes. In 1851 Silvestre Ochagavía Echazarreta imported, along with a French winemaker, a range of vine varieties regarded today as the most classic and internationally respected (Robinson, 2006). Some of the most famous Chilean wine houses were also established in this period, which started using predominantly French grape varieties: Viña Linderos (1865), Viña Errázuriz (1870), Viña Tarapacá (1874), Viña Santa Carolina (1877), Viña Santa Elena -later named

[3] Cited from Van Casteren (2006). *Paradiso. De Nieuwe Wijnen van Chili.*

Valdivieso- (1879), Santa Rita (1880), Concha y Toro (1883) and Viña Undurraga (1885). In 1875 Chile had over 40,000 hectares planted and already produced 50 million litres of wine (Ilufiz and Venegas, 2005). Luckily, Chile started to develop its own collection of European grape varieties as early as the 1830s. While the rest of the world would be hit by *phylloxera vastatrix* in 1863*,* a parasite which wreaked havoc in many wine producing countries, especially in the Old World, Chile was spared because of its isolated position: the Atacama Desert in the north, the Andes in the east, Antarctica in the south and the Pacific Ocean, with its cold Humboldt Current, and the Coastal mountain range in the west. The outbreak of phylloxera stimulated the export of quality wines from Chile. However, when a solution was found for phylloxera –planting vines on grafted rootstock-, Chile's luxury position on the export market changed. Many Chilean wineries started to focus more on the local market, producing ever larger quantities of wine, but of lower quality. Nonetheless, to this day Chile is still considered a phytosanitary paradise where diseases and pests are almost non-existent, a major advantage.

Between the 1930s and 1970s a moratorium on new plantations was imposed, and during the inter-bellum period an embargo on imports was established. This led to technological stagnation and a further decrease in quality (for instance, wine couldn't be ripened on French oak any more). Import substitution policies did not favour exports and winemakers had no choice but to depend on a small domestic market (Visser, 2004). These problems ultimately resulted in social unrest and redistribution of land under the Socialist governments of the late sixties and early seventies. The military coup of 1973 under General Augusto Pinochet caused a liberalisation of the wine market, but this led to an immediate saturation of the local market, at the same time that exports stagnated. Local consumption decreased and the country also suffered from an overall economic crisis between 1982 and 1985. These setbacks resulted in a decrease of almost 50% of total wine production acreage.

In these difficult times, the Chilean wine industry would be transformed by foreign investment. In 1978 Miguel Torres, from the famous wine region of Penedès, in Catalonia, Spain, came to Chile. Torres introduced the latest technology (temperature driven stainless steel tanks for instance) and started making modern, fresh and fruity wines focused on exports, a novelty in Chile. Many Chilean wineries copied this example and in the late 1980s exports increased again and other foreign investors followed in Miguel Torres' footsteps, especially the French. A few interesting examples: Les Domaines Barons Rothschild (Lafite) entered Chile in 1988, and in 1994 Casa Lapostolle was established through a joint-venture between two famous French and Chilean wine families. Casa Lapostolle is currently famous for its acclaimed *Clos Apalta* carmenère, which might be considered one of Chile's few *Icon* wines. Another famous French-Chilean joint venture is the 1997 joint-venture between

Concha y Toro's Giulisati family with the Baroness Philippine de Rothschild, leading to the production of *Almaviva* wine, another one of Chile's top wines. Further projects involve the cooperation between Château Dassault and Chilean giant San Pedro, leading to *Altaïr*. The US has also found its way to Chile. In 1995 Robert Mondavi, the well-known Napa Valley wine producer, established the famous *Seña* wine brand with Eduardo Chadwick from Viña Errázuriz, and Veramonte is working together with wine giants Constellation Wines (Van Casteren, 2006). Between 1974 (one year after the official liberation of Chile's wine market) and 1989 investment in joint-ventures amounted to US 5$ million (Visser and de Langen, 2006). Decreasing domestic demand and the arrest of Pinochet in 1989, making exports possible again, led to an increase in exports in the beginning of the nineties. Between 1990 and 1994 investment in joint ventures increased to US$ 8 million, and to US$ 38 million between 1995 and 1998 (Visser and de Langen, 2006). Wine acreage doubled; and foreign investment and the increased focus on exports led to a change in mentality among Chilean producers: more emphasis was given to lower yields (which means higher quality production), better irrigation, more attention to the vines, and a more careful assessment of possible sites for future vineyards (Van Casteren, 2006). This led to a very important increase in the quality level of the wines produced. In total, between 1974 and 1998 foreign investment (not only in joint ventures, but also in foreign companies' own vineyards in Chile) amounted to US$ 101 million, of which over 50% came from US investors (Agosin, Pastén and Vergara, 2000).

Apart from an increasing focus on quality and benefiting from technical and marketing expertise from foreign investors, the Chilean Wine industry has also benefited from foreign investors' market knowledge, brand names, and economies of scale (in distribution costs, for example) (Visser and de Langen, 2006). According to these same authors, wineries with a foreign investment were the first to sell to a wide range of export markets, setting an example for local, smaller wineries, thereby further promoting the internationalisation of the Chilean wine industry (Visser and de Langen, 2006).

3.2. Geography and Climate

Chile has a somewhat peculiar topography. The country is only 180 km wide on average, but stretches out in north-south direction for over 4,000 kilometres (even 5,000 km according to some sources). This has led people to comment that the country is virtually impossible to defend in case of war. At the same time however, Chile might be considered very sheltered and protected, by Antarctica in the South, the Andes in the East, and the Coastal mountains plus the ocean and its Humboldt Current in the west. To the north Chile consists of desert;

the Atacama. This natural diversity also means the country has a lot of different climates and temperatures ideal for vine growing. Both the Andes and Pacific cool the air and the snow from the Andes also serves as a steady supply of crystal clear water used to irrigate the vineyards. Its sheltered nature has also earned Chile the name of being a phytosanitary paradise, as the bacteria *phylloxera,* which wreaked havoc in vineyards almost everywhere else in the world, never hit the country and pests are rare. Because of this Chilean vineyards are still planted with ungrafted rootstock. Chile's ideal climatic conditions and position as a phytosanitary paradise are often cited as two of the most important (natural) advantages of the Chilean wine industry. This natural advantage is one of the main reasons for the attraction of the Chilean wine industry to foreign investors. The various wine regions of the country will be discussed shortly.

3.3. Planted Surface

To compensate for the domestic consumption slump –as well as for the decrease in exports- Chile's planted surface of vines almost halved between 1970 and 1986 (Van Casteren, 2006). This negative trend continued until 1995, after which acreage started to increase again. Together with the influx of foreign investment and an increased focus on exports, the surface planted with vines almost doubled between 1996 and 2000 (Visser, 2004). And as can be seen from Table 7, the planted surface has continued to increase since. Between 2001 and 2005 planted acreage increased from 447,000 to 465,000 acres. In 2005, Chile's vines made up 2.4% of the world's total planted surface. Chile currently has an estimated 8,000 producers of wine grapes (USDA, 2007). Good prices obtained by grape farmers during the last few years resulted in additional plantings of vineyards and existing operations expanded or replanted to varieties in higher demand. Industry sources believe that once the new areas come into production, wineries will have to invest in new processing and storage facilities to absorb the annual additional output. As a result the Ministry of Agriculture's new estimate of total planted area of vines for wine is now 117,000 hectares. Out of the total planted area, around 76 percent are red varieties (20 red varieties, of which almost half are Cabernet Sauvignon). Also, close to 75 percent of all planted area is irrigated. As a result, Chile's total volume of exportable wine is expected to continue to expand in the coming years (USDA, 2007). This will likely increase competitive pressure on exporting wineries.

Red wines are still the industry's main focus. The most important grape varieties are *Cabernet Sauvignon*, *Merlot*, *Carmenère* and *Syrah*. In 2007, Cabernet Sauvignon accounted for 42.4% of production, Merlot for 14.3%, Carmenère for 8% and Syrah for 3.8%

(SAG, 2007). It wasn't until 1994 that it was officially discovered that a lot of the merlot planted in Chile was actually carmenère, a variety thought to have disappeared because of phylloxera. It seems odd that this was never noticed before as the varieties are very different. It is possible that many Chilean wine producers did not want to admit that their merlot wasn't actually merlot, as it was the most sought after Chilean wine at the time. Now that Carmenère is accepted it is identified as being Chilean, in the same way *Zinfandel* belongs to California, *Malbec* to Argentina and *Pinotage* to South Africa. Thus, focusing on Carmenère (as single variety, or used in blends) could offer Chilean wine producers a way of differentiating themselves from foreign competitors on the export market. However, in other countries carmenère has been recently re-discovered as well, such as Northern-Italy, Napa Valley and Washington State (Van Casteren, 2006).

Although Chile's image as wine country is based primarily on red wines, it also produces and exports white wines. *Sauvignon Blanc* is the most important white wine, followed by *Chardonnay*. In 2007, Sauvignon Blanc accounted for 13.2% of production and Chardonnay for 9.1%, occupying a third and fourth position respectively, still in front of carmenère and syrah (SAG, 2007).

Chilean wines exported are mainly characterised as extremely fruity and clean. Yields are still relatively high although more low-yield and/or more wines matured in barrels are being exported (Robinson, 2006). Lower yields and older vines signal an increase in wine quality.

3.4. Production

As a consequence of the continuing increase of planted vines since 1995, wine production also increased. Table 9 shows Chilean production between 1997 and 2007. In 2007, 73.5% of production consisted of red wine, and 26.5% of white wine (SAG, 2007). The 6 most important grape varieties (mentioned above) were responsible for 91% of production.

Table 9 Chilean Production 1997-2007 in Hectolitres

Year	Wine with D.O[4].	Wine without D.O.	Table Wine	Total
1997	2.489.287	1.330.057	490.905	4.310.249
1998	2.996.983	1.443.082	825.438	5.265.503
1999	2.395.729	1.318.548	565.874	4.280.151
2000	3.748.213	1.956.098	715.063	6.419.374
2001	4.460.397	583.290	408.098	5.451.785
2002	4.430.500	834.463	358.267	5.623.230
2003	5.460.865	947.611	273.745	6.682.221
2004	5.474.888	577.173	248.675	6.300.736
2005	6.303.212	1.047.796	534.503	7.885.511
2006	7.163.042	861.365	424.370	8.448.777
2007	7.038.873	879.062	359.525	8.277.460

Source: SAG (2007), Chilean Ministry of Agriculture

During 2001 and 2005 Chile increased its share of world production from 2.1% to 3%, as can be observed from table 3. This put Chile in 11th (and last) place among the major Old and New World Countries (not counting China and New Zealand). The current production growth is closely linked with increasing foreign demand for Chilean wines. According to Visser (2004) this must have gone hand in hand with changes in technology, production, marketing and distribution so as to supply a coherent product, matching prevailing trends in retailing and consumer demand in importing countries. Part of this can be explained by the influx of foreign investment and international joint ventures to Chile, which were described before. However, table 9 also shows that total Chilean production decreased with 2% from 2006 to 2007, from 8,448,777 hectolitres to 8,277,460. This can be seen in light of the current world-wide oversupply of wine, which forces Chile (and others) to cut down production and increase quality, meaning a shift from bulk to bottled wine, and also an increase in the quality of (exported) bottled wine. Many of the successful smaller Chilean wineries focus their exports accordingly, as they produce relatively small quantities of high quality wines from well known grape varieties. Similarly, a study by Foster et al (2002) concluded that the Chilean Wine Industry's top priorities are the production of high quality wine to meet final consumer demand and the reliability of their supply to meet distributors demand, directly followed by product price and production costs. However, the same study also found that the industry has an orientation and focus towards the product rather than a market orientation.

[4] D.O. = Denominación de Origen

3.5. Consumption

As was mentioned before, Chilean consumption has fallen from 53 litres per capita in the sixties to around 15 litres per capita since the 1990s. A partial explanation is that in the same period Chilean beer consumption doubled. Also, changes in lifestyle have made it more difficult to consume wine on a daily basis (Terheijden, 2005). Thirdly, the wine drunk between the 60s-mid 80s was of inferior quality, mostly drunk by lower income families. With the increase in living standards, consumption of this type of wine diminished over the years. The wine produced nowadays is of higher quality, although Chile still produces a large quantity of lower quality bulk wine. Between 2001 and 2005, per capita consumption increased again from 14 to 16 litres, as total consumption increased from 2.25 million hectolitres in 2001 to 2.5 million hectolitres in 2005, an 11.11% increase. Still, Chile's consumption level is the lowest of all major wine producers and exporters (USDA, 2007). Furthermore, the growth potential of domestic consumption is low, as the Chilean population is smaller than in most other wine producing and exporting countries. Lastly, a lot of the wine consumed locally is still low priced. As a consequence, Chile's domestic market is not considered very attractive, as was already observed in figure 2. Many Chilean wineries - especially the ones who are or would like to target higher price segments- are therefore dependent on exports for their survival, which in large part explains the high level of internationalisation of the Chilean wine industry, as shall be discussed next. To increase domestic wine consumption, the Wines of Chile business association has conducted a promotional programme during the last 10 years. Their annual budget is approximately $700,000 to $1 million dollars. The main activity of this programme is called "Wine Show and Tasting". This activity takes place in different parts of the country. It consists of seminars and wine tasting in Malls, at Art centres and special wine tasting events (USDA, 2007).

3.6. Exports

Chile has been steadily increasing its market share of total wine exports over the past decades. Chile's increased orientation towards exports can be seen by the fact that the country ranked 13th concerning global wine exports in terms of volume in 1986, with a market share of 0.5%. In 2000, however, Chile had advanced to a 5th position. In 2005 Chile still ranked 5th but already accounted for 5% of total world exports in volume. As mentioned before, Chile ranks only 11th in terms of production volume, thus signalling a high degree of internationalisation of its wine industry: in 2006 over 60 percent of Chile's total yearly production volume was exported, supplying more than 100 countries. In 1994 only around 30% of production was aimed at exports. Over the same period (1994-2006), export volume increased 4.7 times and export value increased 6.7 times, showing an increase in average export price per litre from US$ 1.29 to US$ 1.86 (see table 10 below). At the same time it has to be remembered that Chile has a relatively weak domestic market both in terms of current consumption (it ranks 20th in terms of domestic consumption volume), as well as possible future growth because of its relatively small population. Therefore, success on the export market is crucial to the Chilean wine industry. It is estimated that there are over 175 Chilean wineries, of which around a 100 are more or less dependent on exports (Van Casteren, 2006). The next table shows Chile's wine exports according to volume and value. These figures include both bottled as well as bulk exports, of all types of wine. In 2006 Chile's wine exports amounted to US$ 965 million, where its total exports amounted to almost US$ 59 billion, or around 1.5% of total Chilean exports.

Table 10: Chilean Exports in Volume (Million Litres) and Value (Million US$)

	1992	**1994**	**1996**	**1998**	**2000**	**2002**	**2004**	**2005**	**2006**	**2007**[5]
VOLUME	74	111	185	251	276	356	474	421	520	598
VALUE	119	143	294	540	585	610	845	885	965	1,110
AV.PRICE	1.61	1.29	1.59	2.15	2.12	1.71	1.78	2.10	1.86	1.86

Source: USDA GAIN Report CI7015. World Wine 2007 (2007)

After many years of expansion, Chile's wine exports in volume fell for the first time in 2005. Due to a fall in operational margins as a result of the revaluation of the peso against the dollar, most wineries had to increase the prices of their export wines. This price increase lowered the competitivity of Chilean wines against other producers (countries), thus reducing demand (USDA, 2006). Industry sources believe the increase in the average export price reflects an improvement in the quality of the wine being exported (USDA, 2007). In 2006 and 2007 the average export price slumped again however. It should be remembered however that table 10 shows all wine exports, including bulk wine. A fall in average wine price does not necessarily mean a decrease in price or quality of (higher quality) bottled wines, which shall be demonstrated shortly.

Other major gainers in export market share have been the US and especially Australia. Also, the other New World countries (Argentina, South Africa and New Zealand) have increased market share, as was shown in Table 6. Argentina's exports are growing especially fast, a fact that causes some unease among Chilean wineries. For instance,

[5] Forecasted

Argentina's exports to the United States are growing much faster than those of Chile. Furthermore, Argentina's production level is already far higher than Chile's and its land and labour costs are comparable to those of Chile. Lastly, Argentina has a better defined country image which wineries may profit from. Some major disadvantages of Argentina are its lack of trade agreements and high inflation levels. The Chilean wine industry's attitude towards its larger neighbour is somewhat ambivalent. On the one hand it is seen as a sleeping giant; a potential threat to the Chilean wine industry. On the other hand, Chilean wineries have also started to invest in Argentina since the mid nineties, tempted by lower land costs across the Andes (Robinson, 2006).

As has been said, Chile traditionally exports both bottled and bulk wine. An increasing number of wineries are making a big effort to increase premium-bottled wine exports; as a result bottled wine grew faster than bulk wine in 2006 (USDA, 2007). However, Chile still has a long way to go to be able to compete in the higher bottled wine segments with its principal competitor Australia. As short ago as 2003, 45% of Chile's exports consisted of bulk wine and a large part of bottled wine exports was destined for the lower price segments, leading to an average bottled wine price of US$ 2.1 per litre, compared to an average export price of US$ 3 for Australian bottled wines (Moguillansky, Salas and Cares, 2006). The following table shows the percentage of Chilean and Australian exports destined to the different price segments for 2003. It is clear that Chile is underperforming in the higher, more attractive segments, where competition is less cutthroat and profits higher. There is evidence that wineries putting a greater emphasis on product quality indeed receive higher average prices. There is, however, less support for the idea that an emphasis on product quality translates into improved export growth performance (Foster et al, 2002).

Table 11: Spread of Chilean and Australian Exports according to Price Segment (2003)

	Av. price in US$ p Ltr	**Australia**	**Chile**
Basic wine	Less than 2$	17%	44%
Table Wine/Premium	2$ - 3.5$	45%	47%
Super&Ultra Premium, Icon	More than 3.5$	38%	9%

Moguillansky, Salas and Cares, (2006)

Considering the Chilean exports of fine wines (higher quality bottled wines) between January and September 2007, Cabernet Sauvignon was the most important exported variety (33%), followed by Merlot and Sauvignon Blanc (both 14%), Chardonnay (12%), Carmenère (6%) and Syrah (3%) (ODEPA, 2007).

Apart from an increase in export market share and an increase in average quality (and price) of the exported wines, Chile has also wisely diversified its wine exports geographically. In 1980, almost 88% of Chilean wine exports were destined to other Latin American countries. This figure dropped to less than 8% in 2002 (Visser, 2004). Throughout the 1980s the USA, Canada and Mexico became Chile's main export destinations, at the expense of Latin America. However, since 1990 sales to the NAFTA countries decreased and Western Europe became the number one destination, importing over 50% of Chilean wine exports in 2002. More recently, Asian countries have been increasing their share from 3% in 1995 to 12% in 2002 (Visser, 2004). This figure dropped to around 10% since then (USDA, 2007). Still, many exporting wineries are turning their attention to Asian countries such as China and Japan, as well as Russia. Other markets which might be considered of increasing importance in the future are India and other Asian nations such as Vietnam, Indonesia, Malaysia and Thailand. The total number of buyer countries increased from 34 in 1984 to over a 100 in 2007. Table 12 demonstrates Chile's most important wine export destinations, both in terms of volume and value.

Table 12: Chilean Wine Exports by Country of Destination

	Quantity (1000 Hectolitres)		**Value (1000 US$)**	
Country	**2005**	**2006**	**2005**	**2006**
UK	787.1	1,018.1	153,210	163,303
US	561.1	535.5	147,456	149,721
Canada	262.3	449.6	53,378	56,150
Germany	465.7	399.7	64,525	53,167
China	66.3	393.0	9,107	21,119
Denmark	293.5	256.8	49,921	42,429
Russia	73.0	236.8	16,718	26,069
Netherlands	151.0	177.4	36,397	42,106
France	187.8	164.4	19,499	20,131
Venezuela	92.0	153.6	17,744	25,252
Brazil	116.3	143.5	27,868	37,028
Others	1,221.2	1,276.2	288,870	331,551
TOTAL	**4,745.8**	**5,204.6**	**884,643**	**968,026**

Source: USDA GAIN Report CI7015. World Wine 2007 (2007)

In 2006, the top ten importers in terms of *value* of Chilean wine accounted for almost 64% of total Chilean wine exports. The Top Ten includes four non western countries: China, Venezuela, Brazil and Russia. Within the top 11 (top ten plus France), the European countries accounted for over 33% of imports (in value) and North America for 21%.

According to *volume* exported the figures are similar: the top ten accounted for almost 73% of exports, of which Europe accounted for 39% and North America for 19%. The next table shows the percentage of Chile's Wine exports (expressed in volume and value) according to country of destination.

Table 13: Chilean Wine Export Percentages by Country of Destination in 2006

Country	Volume	Value
UK	19.6%	16.9%
US	10.3%	15.5%
Canada	8.6%	5.8%
Germany	7.7%	5.5%
China	7.5%	2.2%
Denmark	4.9%	4.4%
Russia	4.5%	2.7%
Netherlands	3.4%	4.3%
France	3.2%	2.1%
Venezuela	3%	2.6%
Brazil	2.8%	3.8%

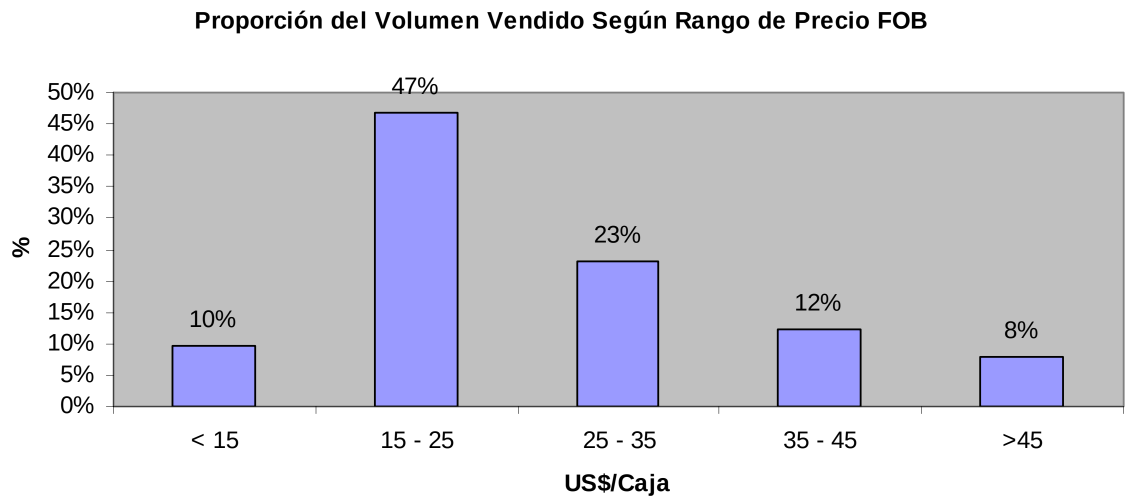
Source: USDA GAIN Report CI7015. World Wine 2007 (2007)

As table 13 shows, Chile's most important export markets, both in terms of volume and value, are the U.S. and the U.K. It is interesting to see that only in Brazil, the Netherlands and the US the value of Chilean wine imports exceeds the volume percentage. It seems these countries are importing quality over quantity, especially in the case of the US, where the value of Chilean wine imports exceeds the volume by over 5%.

Bottled wine exports over the first six months of 2007 (January-August) reached 232 million litres and US$ 690 million, an increase of 27% and 33.4% respectively. This translates into an average price per case (12 bottles of 0.75 litres, or 9 litres) of US$ 26.76 (or almost US3$ per litre), an increase of around 5% against the same period last year. However, this is on par with the level Australia had already reached in 2003, as was shown in table 14. Similarly, between January and September 2007 Chile exported 230 million litres of Wine with *Denominación de Origen*, worth US$ 715.6 million, an increase in volume of 23% and in value of 30% over the same period in 2006, leading to an average price of US$ 3.11 per litre of exported D.O. wine. This proves again that Chile has not just increased export volume, but also the quality of the exported wines, leading to higher prices (ODEPA, 2007). The next table shows bottled wine exports (US$ FOB) over the first nine months of

2007 (Jan-Sep) according to Price Range (expressed per case, or 12 bottles or 9 litres of wine):

Table 14: Export Volume per Price Range FOB

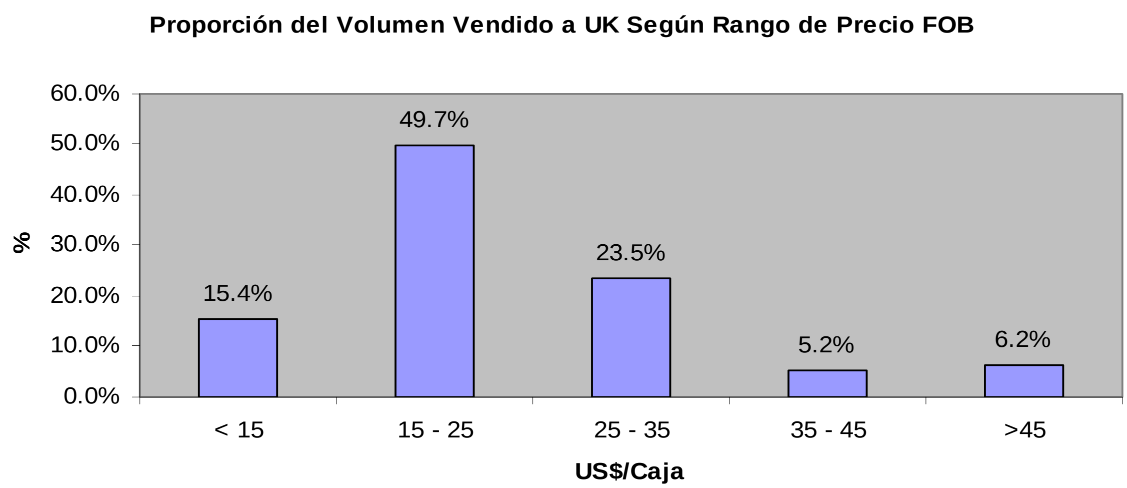


Source: ProChile (2008)

The table demonstrates that a lot of Chilean wine exported is still in the lower price segments, the majority between US$ 15-25 per case, or US$ 1.25-2.08 per bottle. Only around 8% of Chilean wine bottles are exported for over US$ 45 a case, or a price of around US$ 3.75 per bottle.

The UK 's imports of Chilean wine over the first six months of 2007 increased 37.9% in volume and 51.7% in value, to 6.2 million cases worth US$ 140 million compared to the same period in 2006. The average price per case was US$ 22.6 -or around US$ 2.5 per litre- (Viñas de Chile, 2007). Between June 2003 and June 2007 Chile's UK market share increased from 5.9% to 6.9%, a percentage putting Chile in 6th position, overtaking Spain. Over the same period average consumer price increased from 3.71 to 3.82 GBP per bottle. Sales of Chilean wine in the £5 to £10 sector—generally considered to be Chile's greatest strength—grew by an impressive 26% over the last 12 months to June 2007, and Chile now sells 14% more wine priced above £5 than South Africa. However, Australia is still by far the biggest exporter on the UK market with a share of 22.5% in June 2007 (Wines of Chile, 2007). Considering Chile's position on the UK market, Wines of Chile's UK Director Michael Cox said: *"Chile is making steady and sustained progress across the board in both volume and value, and this is testimony to the hard work being done by the wineries, and the* *growing awareness of Chile's naturally diverse styles of quality wines"* (Wines of Chile, 2007). The following table shows Chilean exports to the UK over the first nine months of 2007 according to Price Range:

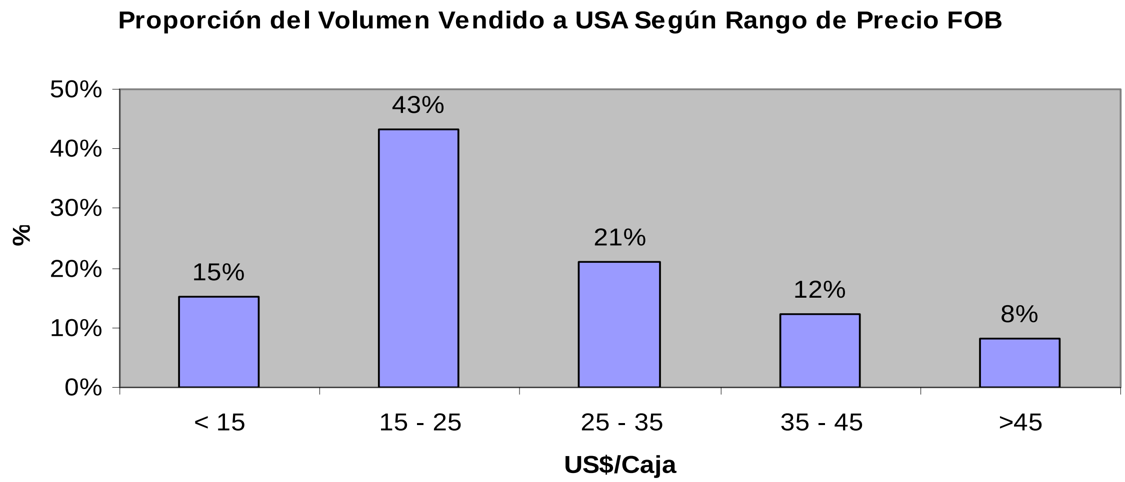
Table 15: Export Volume to the UK per Price Range FOB



Source: ProChile (2008)

In the US imports increased 11.7% in volume and 23% in value, leading to 4.2 million cases and US$ 115 million over the first six months of 2007 compared to the same period in 2006. Average price per case was US$ 27.4, or a little over US$ 3 per litre (Viñas de Chile, 2007). Chilean wines ranked 4th concerning imported wines in the US in 2003, behind Italian, Australian and French wines (Heijbroek and Rubio, 2003). Still, in 2006 Chilean wines only accounted for 2% of the US market, which is dominated by local wines (Reuters, 2007). The following table shows exports per price range to the US.

Table 16: Export Volume to the US per Price Range FOB

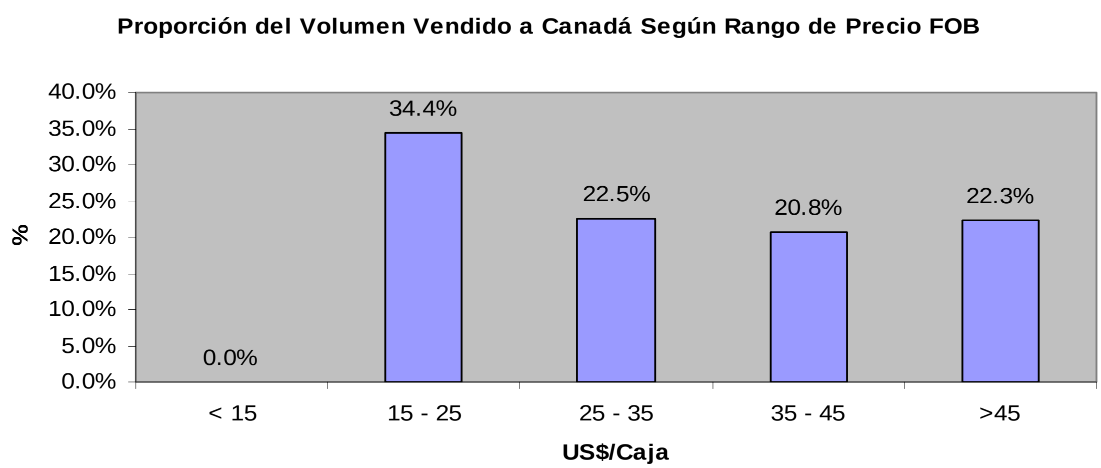


Source: ProChile (2008)

The US shows almost the same spread according to price range as table 14.

Chile's third biggest export market, Canada, also showed some impressive growth figures: imported volume increased by 22.8% to 1.074 million cases and import value increased by 25.7% to US$ 39 million between January-August 2007 versus the same period in 2006. Average price per case increased over 4% to US$ 36.3, the equivalent of over US$ 4 per litre. (Viñas de Chile, 2007). If we look at exports per price range over the first nine months of 2007 we see that Canada seems to be increasingly importing more bottled wine of the higher price categories

Table 17: Export Volume to Canada per Price Range FOB



Source: ProChile (2008)

The above shows that both in total exports, as well as in Chile's three most important export markets, value grew more than volume, increasing the average price per case (or per litre). In conclusion, it might be safely assumed that Chilean wineries are indeed increasing the average quality of their exported wines, as average prices in all its most important export markets have been on the increase.

3.7. Technology and Innovation

Modern technology was first introduced into the Chilean wine industry when Miguel Torres entered Chile in 1978. In the late 1980s this process was accelerated by foreign investment and by the democratic transition that took place in the country in 1990. These outside investors assisted the influx of both equipment (such as stainless steel tanks, pneumatic presses, oak barrels, modern filters and cool storage facilities) and expertise (Robinson, 2006). In this period, Chile's wine industry was to be highly influenced by Australian vinification techniques and the import of European machinery and equipment (Gwynne, 2005). Nowadays the Chilean wine industry uses the latest technology and machinery, on par with other major wine producing countries. However, technological advances still mostly take place outside of Chile and most machinery is still imported from and produced by European competitors such as France, Italy, and Germany (Visser, 2004). This presumably leads to a certain laps of time before the latest technology is incorporated into Chilean wineries. However, experts point out that this situation is fairly similar for other major producers and exporters. Currently, over 46 percent of wine storage containers at Chilean wineries are made of stainless steel, which shows a high technological development standard for the industry. Additionally, 39 percent of the wineries use oak barrels, French or American, for an average of 3 to 5 years. Over 70 percent of Chilean wine makers believe that they have sufficient (cool) storage capacity for their production; while only 12 percent believe they need to expand (USDA, 2007). Technological advances in machinery and equipment haven't been as dynamic as the latest changes in agronomic and oenological practices. This has led to a continuing increase in quality and consistency of Chilean wines. Other advances which need to be addressed are the use of IT for monitoring and control, as well as logistics (JIT) and organisational approaches (ISO 9001) (Visser, 2004).

Chilean wineries are very interested in innovation, not only in light of competition with the country's major New World competitors such as Australia, but also its Old World competitors who are fighting back to regain lost market share, such as Spain and Italy. Also, both consumers and large supermarket chains have become more demanding. To be able to export a differentiated offering, continuing innovation (seen as new products, processes, business models and management methods to create value) is considered very important by Chilean exporting wineries (Moguillansky, Salas and Cares, 2006). There are some problems however. First of all, a lot of smaller companies suffer from a lack of management and innovation capabilities and both smaller and larger companies alone do not have the financial nor human resources to conduct generic market or other research, so a form of association or cooperation between wineries is necessary. In Australia, vineyards of all sizes are represented by an industry wide organisation, and receive state funds to promote their product. However, in Chile a lack of trust impedes this to a great extent, even considering market research which might be considered equally beneficial to all. An often heard explanation is that Chileans have a very entrepreneurial attitude and are not used to cooperate, although relationships among wineries are said to be fairly good. Secondly, there is a need for the different business associations and (public) support organisations (to be discussed next) to cooperate, not just financially, but to devise the infrastructure and support programmes to educate and inform wineries; for instance to develop management capacity, so that knowledge and best practices are not dispersed but shared evenly among the majority of interested wineries. Another important problem facing the Chilean wine industry in terms of innovation is that University research is often basic, of technical nature (instead of commercial), not always of interest to the wineries, and lastly, not always coordinated so risking duplication. These problems cause Chile to remain largely dependent on foreign technology and know-how (Moguillansky, Salas and Cares, 2006).

Lastly, apart from government support and public (financial) resources, Chile’s wine industry also lacks its own financial resources. For instance in 2000 US wineries together spent US$ 6 million and Australia spent a total of US$ 9 million on R&D, half of which paid by the state and the other half by Australian wineries, against a mere US$ 400.000 by Chile (Moguillansky, Salas and Cares, 2006). A lack of capital is thus also often cited as a problem impeding innovation, especially concerning marketing and branding.

3.8. Government Support and Business Associations

The Chilean government does not interfere directly with the wine industry by subsidizing wine production or exports directly. However, through its policy of singing bilateral trade agreements (Chile has the highest number of bilateral free trade agreements in the world, currently over 40) it does contribute to the success of Chilean wine on the export market.

Also, there are some state-supported organisations that play an important role in the wine business: SAG (Servicio Agricola y Ganadero, part of the Ministry of Agriculture) deals with legislative issues for wineries. For example, wine production and exports are regulated and certified by the SAG. All wine produced in Chile for both the domestic and export market is periodically sampled by SAG and SAG also issues the export certificates that include the wine's origin and quality. It is in the entire wine industry's best interest that this quality control takes place; if one deficient wine brand would slip through, this would adversely affect the name of all Chilean wines and perhaps all Chilean export products. A second organisation, ProChile, promotes exports of Chilean products –including wine- all over the world, and lastly, CORFO (*Corporación de Fomento de la Producción*) is a public fund aimed at private enterprises. In the wine sector it supports the *Rutas del Vino* and some technology projects through the *Corporación Chilena del Vino* (CVV) (Visser, 2004). Other organisations include: *Oficina de Estudios y Políticas Agricolas* (ODEPA) and *Fundación para la Inovación Agraria* (FIA).

There are three major wine business associations in Chile; Viñas de Chile, ChileVid and Corporación Chilena del Vino (CCV).

Viñas de Chile was founded in 1949 and is Chile's oldest wine business association, uniting Chile's biggest wineries, such as Concha y Toro, Santa Rita, San Pedro and others, with successful medium-sized firms exporting high-quality wines, such as Montes and Casa Lapostolle. It currently tries to lobby the government for export market access, devises training programmes for fieldworkers, and education programmes for exporters. It is also committed to work with universities to stimulate research and technology development and works closely together with ChileVid to promote the image of Chile and Chilean wines abroad.

ChileVid, or *associación de productores de vinos finos para la exportación*, was founded in 1993. Its members are mostly younger and smaller companies primarily aimed at exports of higher quality wines. ChileVid focuses on helping to develop the business of their members, by lobbying for financial resources and providing information and advice on technical, legislative, and commercial aspects of wine exports, the organisation of trade fairs abroad, and the development of relationships with wine journalists.

Recently, ChileVid and Viñas de Chile decided to cooperate by establishing Vinos de Chile (Wines of Chile) to devise a *Brand Chile* to promote Chilean wines in its most important export markets. Wines of Chile has offices in Chile, London and the US and organises promotional campaigns, wine promotion fairs and competitions, to build an image of Chile in consumers' minds. At the moment the organisation is mainly active in the US, UK, Canada and Germany. The Wines of Chile campaign is funded mainly by ChileVid and Viñas de

Chile and has an annual budget of $6 million, which is less than 1 percent of the total value of Chile's bottled wine exports last year. The marketing funds are used for generic promotion. The Government contributes 15 percent of the total amount, through its export promotion agency ProChile (USDA, 2007). Wines of Chile's mission is to strengthen the image of Chile in the marketplace. Wines of Chile hope to boost worldwide exports to $1.2 billion by 2010, with most of the growth coming from higher prices (Economist, 2007). A lot is expected of Vinos de Chile, as it is the only campaign that comes close to being a national wine promoting agency such as the ones that exist in other wine producing countries, such as The Australian Wine Bureau and Wines of South Africa (WOSA). The lack of such an organisation is often seen as the biggest problem facing the Chilean wine industry today. ChileVid and Viñas de Chile are said to represent around 95 wineries and 95% of the total exported wine. The main Wines of Chile activity is called the "Tastes of Chile" campaign to promote Chilean fruits and wine. The images used build on the natural beauty of Chile and the quality of its products. Another promotional programme is the activity called "Wine Show and Tasting", or *muestra y cata*. This activity takes place normally once a year. It consists of seminars and wine tasting. ProChile contributes with logistics and market information and the wineries pay the costs. With this strategy the wine industry is promoting wines in markets like Russia, The Netherlands, Denmark, Sweden, The Czech Republic, Brazil, Mexico, Venezuela, Taiwan and Hong Kong (USDA, 2007).

The last organisation is called *La Corporación Chilena del Vino* (CCV). CVV consists not only of wineries, but also grape producers and their suppliers. Activities of the CVV include the diffusion of technical and market information through special publications, the organisation of training courses, and representing members in negotiations on new policies, treaties and regulations. Secondly, it acts as an intermediary for CORFO, a public support fund for the private sector (Visser, 2004).

3.9. Regional Structure

Chile is divided into 12 administrative regions, regions I to XI plus the Metropolitan Area of Santiago (R.M., or *Región Metropolitana*). This administrative division was created in 1980 by the former Pinochet government (Visser, 2004). The division follows a north to south direction; region 1 is the Northern tip of the country, and region 11 lies in the south (Antarctica). Grape growing and wine production takes place in a territory covering about one third of the entire nation. The major wine producers are found in the Metropolitan Region of Santiago, the 6^{th} region (Bernardo O'Higgins) and 7^{th} region (Maule). The Maule region is the single largest wine producing region of Chile, accounting for 48.9% of total production (SAG, 2007). Together these three regions (R.M., 6th and 7th) accounted for 93.3% of Chilean wine production in 2007 (SAG, 2007).

Table 18: Chilean Production (in Hectolitres) according to Administrative Region

Region	**2006**	**2007**
III	291	260
IV	162,036	184,329
V	244,882	167,453
R.M.	1,127,760	939,624
VI	2,713,894	2,730,498
VII	4,003,295	4,049,640
VIII	196,619	205,656
Total	**8,448,777**	**8,277,460**

Source: SAG (2007), Chilean Ministry of Agriculture

Considering wine production, Chile is more commonly divided into wine producing valleys, instead of administrative regions. Form North to South these valleys include: *Elqui, Limari, Aconcagua, Casablanca, San Antonio, Maipo, Cachapoal, Colchagua, Curicó, Maule, Itata, Bio Bio and Malleco* (Van Casteren, 2006). Colchagua and Cachapoal valleys together constitute an official *denominación de origen* (DO): the Rapel Valley. The Maipo valley also has a D.O. In Chile, only 75% of the grapes have to come from a limited zone, sub-region, or region to be able to use the term D.O. Furthermore, the Maipo, Rapel, Curicó and Maule valleys are often referred to as Valle Central, or Central Valley, the centre of Chilean wine production, although new areas are being planted increasingly. Although many valleys have been only recently "discovered" there is still an enormous potential of undiscovered, very promising valleys. New vineyards are not only appearing in north-south direction, but also increasingly in an east-west direction, to the Pacific and the Andes, in search of cool climatic conditions, new soils and sub soils. The search for new *terroirs* is proof of Chile's focus on increasing the quality of its wines. There is a conviction that increasing quality can only be done by fine-tuning specific grape varieties with specific areas. This has its effect on labels, which are increasingly stating specific valleys: Cachapoal or Colchagua instead of Rapel, or might be even more specific, stating sub-valleys such as Apalta, in Colchagua (Van Casteren, 2006).

Santiago is the administrative headquarters of most (larger) wineries and also business associations, which shall be discussed in the next paragraph. For a more elaborate description of some of Chile’s most important valleys and sub-valleys I refer to Robinson (2006).

3.10. Industry Structure

The Chilean wine industry is more concentrated than its European counterparts, but less so than in other new world producers (Visser and de Langen, 2006). However, the global wine industry is dominated by French, German, US and Australian firms. Although Concha y Toro is the largest Chilean winery, it ranked only 30th in the world on the global list of leading wine companies in 2003 (Heijbroek and Rubio, 2003). The Chilean wine industry may be considered a global niche player without any really strong brands, which makes it more difficult to find the right distribution channels. The global wine industry as a whole is rather small and much more fragmented compared to other major alcoholic beverage industries, such as the beer and spirit industries.

Before investment in export-oriented wineries in the 1990s, the Chilean wine industry was dominated by a small number of “brand” companies that exported small quantities but whose main focus was still the national market (such as Concha y Toro and Cousiño Macul). Most other wineries were fully focused on the domestic market. Export growth in the 1990s diversified the Chilean wine industry structure (Gwynne, 2005). According to Gwynne (2005) at least four types of wine enterprises can now be identified (apart from small exporting wineries):

1. The large domestic firms with a long “brand” history, such as Concha y Toro, Santa Rita, and San Pedro. Some of these have also developed joint ventures with foreign firms, as was discussed before.
2. Subsidiaries of large foreign-owned wineries, both wholly-owned (Miguel Torres-Spain, Marnier/Casa Lapostolle-France) or joint ventures with large Chilean firms (for example, Concha y Toro and Rothschild, producing the *Almaviva* wine brand)
3. Some medium-sized companies attempting to target niche export markets. These can have various backgrounds, such as wine consultants moving into wine making as was the case with Montgras in 1994. Another theme of enterprise development in this category is that of traditional, small wineries investing heavily in new techniques and upgrading their production, such as in the case of the La Rosa winery
4. Large co-operatives that have managed to upgrade and supply international markets, such as the Cooperativa Vitivinícola de Curicó, producing under the brand name Los Robles.

Nowadays, Chile's three major wineries in terms of production volume are Concha y Toro, Santa Rita and San Pedro. In 2006, these three controlled 73% of Chile's domestic market in terms of sales volume and over 65% in terms of sales value. Concha y Toro had a volume market share of 28%, Santa Rita accounted for 25% and San Pedro for the remaining 19%. In 2001, the big three controlled only 56% of the market in terms of sales volume, and 55% in terms of value, signalling an increase in their domestic market power over the past few years, threatening the existence of some smaller wineries. That concentration levels are lower in terms of value than volume might be explained by the fact that technology and machinery available to smaller wineries acts less as a barrier to increase the quality of wine production, as it does to increase volume (Urquieta and Rojas, 2006). In other words, because technology levels are now equally high at most wineries, it is easier and cheaper for smaller wineries to increase the quality of their wines than it is to invest in significantly increasing production capacity. Table 19 demonstrates that even within the top 20 (out of an estimated 175 wineries in total), most wineries –apart from the big three- have very low market shares in terms of volume; all below 3%. The same holds for domestic market share expressed in value (table 19), with market shares all below 6%. Or put differently, around 172 wineries are left with around 25% of the Chilean market in terms of volume and almost 35% in terms of value. Furthermore, the Chilean domestic market may still be considered as not very attractive. This leaves many smaller wineries with a simple option: increase quality and focus primarily on exports. Indeed, Urquieta and Rojas (2006) conclude that the smaller wineries are capable of withstanding competition from the big three mainly based on product differentiation, adding value to both their wines and their brands, so they can focus mainly on the export market with high quality wines.

Table 19: Top 20 Chilean Wineries in domestic Volume %

Winery	**2001**	**2006**
Concha y Toro	21,4	28,3
Santa Rita	21,2	24,6
San Pedro	14,2	19,7
Santa Carolina	4,4	3,0
Tarapacá	1,5	2,8
Canepa	2,6	2,3
Fco. De Aguirre	3,1	1,7
Viña Ventisquero	0,0	1,4
Viña El Aromo	1,2	1,3
Undurraga	2,4	1,2

Covica	3,1	1,2
C. Agricola Curicó	0,9	1,0
S. Ema	1,5	0,8
C. Macul	0,3	0,4
C. Silva	0,1	0,3
A.F. Arco Iris	0,0	0,2
Macaya	0,1	0,2
Errázuriz	0,2	0,2
Torres	0,1	0,1
Viña Mar	0,0	0,1

Source: Urquieta and Rojas, 2006

Table 20: Top 20 Chilean Wineries in domestic Value %

Winery	**2001**	**2006**
Concha y Toro	21,4	25,8
Santa Rita	21,6	23,7
San Pedro	12,1	15,8
Tarapaca	3,1	5,4
Santa Carolina	5,2	4,4
Undurraga	4,8	2,5
Canepa	2,8	2,2
Viña Ventisquero	0,0	1,9
Fco. De Aguirre	2,4	1,2
C. Macul	1,2	1,1
S. Ema	1,4	1,1
C. Agricola Curicó	1,0	1,0
Covica	2,0	0,9
Viña el Aromo	0,9	0,9
Montes	0,2	0,7
Errázuriz	0,9	0,7
C. Silva	0,3	0,7
M. Torres	0,5	0,6
A.F. Arco Iris	0,1	0,5
Caliterra	0,4	0,3

Source: Urquieta and Rojas, 2006

However, in terms of exports the big three also led the Chilean wine industry, albeit to a far lesser extent. In 2006, Concha y Toro's bottled wine exports reached US$ 175.6 million; San

Pedro exported worth US$ 44.5 and Santa Rita for US$ 40.2 million. Total Chilean wine exports amounted to US$ 965 million, leading to an export market share of 18% for Concha y Toro, 4.6% for San Pedro and 4.2% for Santa Rita, or a total of almost 27% of Chilean wine export value for the Big Three taken together. In 2001 the big three still accounted for 29% of wine export value: Concha y Toro (14.2%), San Pedro (10.7%) and Santa Rita (4.7%) (Heijbroek and Rubio, 2003). The top ten exporters considering sales value (US$ FOB) of bottled wine over the first nine months of 2007 are shown in the next table:

Table 21: Top Ten bottled wine Exporters considering US$ FOB Jan-Sep 2007

Company	**Cases (12 bottles)**	**US$ FOB**	**Average Price US$**
Concha y Toro	7.328.288	174.999.957	23,88
Cono Sur	1.853.117	41.000.335	22,13
San Pedro	1.864.192	39.904.871	21,41
Santa Rita	934.694	35.677.260	38,17
Montes	444.009	23.882.376	53,79
Errázuriz	410.217	20.712.544	50,49
Santa Carolina	868.308	20.501.757	23,61
Tarapaca	627.548	18.355.886	29,25
Ventisquero	613.674	16.701.987	27,22
Santa Helena	755.821	15.702.833	20,78

Source: ProChile (2008), Wines of Chile (2008)

Interestingly, Cono Sur has surpassed Santa Rita both in export volume as well as value, and San Pedro in terms of export value. In this thesis the distinction between small and large wineries shall from now on be made based on *export value* as this is deemed the best measure to express success on the export market in general and the higher segments in particular. The best measure of success in the highest price segments however would be average export price (US$ FOB) per case.

Many Chilean wineries, especially the bigger ones, have various vineyards in different valleys, or might source grapes from different valleys. For instance, Concha y Toro has vineyards in Casablanca, Rapel, Maipo, Maule and Curicó, as well as offices in Santiago. Santiago appears to agglomerate marketing, administrative and strategic decision-making functions in the Chilean wine industry (Visser, 2004). Santiago is the preferred headquarters for national wine associations, university wine research institutes and public agencies involved in the wine industry.

The not so attractive home market and high level of domestic market power of the three biggest wineries, together with the higher prices to be obtained on the export market, leave many smaller wineries focussing on the export of high quality wines. However, although the larger companies have an advantage in their economies of scale and large production volumes, this does not mean that they do not produce high quality (low yield) wines as well. Obviously, they produce an array of different wines at different quality levels and prices, including top quality wines. Furthermore, as was discussed, competition abroad is also fierce. This has led many to believe that the only way to be successful on the export market is either by being really big or really small (in terms of production volume aimed at exports). Being big means economies of scale in marketing, production and distribution, and thus placing power. Also, it is attractive to large distributors which demand a variety of different types of wine in different price ranges. Being smaller offers a winery the opportunity to specialise in the highest quality boutique wines, although there aren't that many Chilean icon wines yet. An often cited example of a very successful medium-sized (smaller if expressed in production volume) winery, aimed at the export of high quality wines, is Montes.

3.11. Advantages of Chile

The next two paragraphs will discuss Chile's main advantages and disadvantages as a wine exporting nation. These have been drawn from both the literature as well as from the interviews held with some experts on the Chilean wine industry. These interviews may be found in the appendixes.

As was discussed before, Chile has a relatively strong competitive advantage position compared to other major wine exporters. First of all, its natural resources stand out. Chile is a phytosanitary paradise, where phylloxera never occurred, and where pests and other threats are virtually non-existent. This also means that Chilean producers can work in a more biological manner than competitors and have the opportunity to stress their environmentally-friendly grape growing methods or might consider producing organic wine so as to differentiate their offerings from competitors. Furthermore, the country is ideal for grape growing, because of its unique *terroir*, including optimal climatic and soil conditions, as well as a wide variety of micro-climates. This may lead to increasingly higher quality wines, as well as exciting new blends which might appeal to the consumer. Another interesting option to differentiate itself from other countries is to stress the "Chilean" nature of the carmenère grape, originally a French variety which was wiped out in Europe by phylloxera and deemed to have been lost for ever. Lastly, as Chile is still considered mainly for its red wines (although Sauvignon Blanc and Chardonnay are the 3rd and 4th most export Chilean varieties) it might be possible to stress the health benefits of drinking red wine in moderation, perhaps in combination with one of the above mentioned niche strategies.

Secondly, capital, land and labour costs are –still- relatively low compared to most competitors, which keep production costs down. Additionally, there is a strong focus on cost saving production methods throughout the industry. At the same time, the level of technology and know-how is more or less equal to other wine exporting countries, leading to consistent and good quality wines. Thus, Chilean wines are famous for their price-quality ratio, which might be considered a relatively long-term competitive advantage. The quality of Chilean wines is being increased on a continual basis and it is hoped that the average price might also be raised accordingly. The past few years this indeed seems to have been the case, although there is still a lot of room to improve. Chile's natural comparative advantages, together with its attractive cost structure, also attract foreign investment and expertise, reinforcing the process of increasing the quality of Chilean wines.

Another often cited advantage is Chile's commitment to a stable, free, transparent and export-oriented economy, as can be seen form its numerous bilateral free-trade agreements and its treatment of foreign investment. Chile ranks 22nd on Transparency International's Corruption Perception Index 2007, making it by far the least corrupt country of Latin-America (Argentina ranks 105th in the world for instance). The Economist Intelligence Unit ranked Chile as the No. 1 Latin American country in which to do business for the period 2005-2009 (ProChile, 2008). Secondly, Chilean entrepreneurism is often cited as another advantage of the Chilean Wine industry on world markets. Furthermore, Chile is a stable and secure country in the sense that it hasn't recently suffered from social unrest or economic crises such as some of its neighbours, signalling a low country risk. This also attracts foreign investment.

3.12. Disadvantages of Chile

Chile's major problem is considered by most to be the lack of Country Image. A clear *Brand Chile* does not exist yet. Generic promotion through Wines of Chile and ProChile is as of yet aimed at only a few important markets. The country is largely unknown to consumers around the world. To many consumers the first things that come to mind when thinking about Chile are the Andes and Pinochet. Chile lacks a national symbol such as the Australian kangaroo, or the Argentinean tango (the Chilean national dance, *cueca* is virtually unknown internationally and not nearly as appealing to use as an attribute to build an image on). The only thing that Chile has on offer, and should promote, is its nature; the country offers adventure. Indeed, according to Heijbroek and Rubio (2003) Chile is considered an adventurous, young, passionate, successful and energetic country. But even the image of “adventurous, beautiful” Patagonia is more or less “taken” by Argentina, which also scores higher as a country of “passion” and perhaps “energy” (so does Spain for that matter, the best Old World representative of generic wine promotion). Furthermore, Chile is not a very popular holiday destination, not even among adventure seeking tourists, unlike for example Australia which is a famous back-pack destination. A well developed tourist-destination image can be very helpful in promoting a country image based on natural beauty and adventure, which is deemed beneficial to wine exports. However, instead of benefiting from a country image, wine has –paradoxically- *created* Chile’s image, which might be considered harmful to the industry: that of Chile as a cheap wine producer (Van Casteren, 2006). The goal of Vinos de Chile therefore is to devise a global country image which (with state support in the form of ProChile) would ideally be used not only by the wine sector, but by all export products, current and future.

In line with the lack of image, the Chilean wine industry lacks the will and to cooperate and focus on marketing and branding. The industry is largely production driven, wine is a *push product*. Because of the reasonably high level of fragmentation of the industry, not even some of the larger companies are really capable of going at it alone. There is not enough critical mass to make marketing efforts profitable, so a certain form of cooperation (Vinos de Chile) and even government support (ProChile) is vital. The orientation towards a high quality product at a competitive price is a priority of all Chilean wine companies; it does not matter if we are talking about small, medium or large wineries. Industry coordination is therefore critical to positioning these concepts in international markets (Foster et al, 2002). What is needed to promote Chilean wines is industry-wide cooperation through public-private partnerships. Public-Private Partnerships can contribute to the realisation of projects that increase welfare for society at large, but that are not financially viable for the private sector alone (Van Dijck and Den Haak, 2006). A country image beneficial to all export products could generate positive externalities for society at large and might therefore be considered a collective good. Thus, the Chilean government’s hands-off policy might be considered a disadvantage as well in this respect, although some experts feel this is not a decisive disadvantage as other wine exporting nations also function without government support. The same entrepreneurial spirit cited as an advantage is often seen as a major obstacle for cooperation. In line with the above is a need to develop more consumer- and market know-how. There is a lack of innovation and of high level investigation institutes, such as exist in other countries like France and Australia. Although organisations such as Viñas de Chile are working closely together with universities, these studies focus more commonly on production and technological issues and, as was stated before, are often of little interest to many wineries.

Chilean wines in a sense are too low priced compared to their quality (Chile is over-delivering), and because price is often seen by consumers as the most important indicator of quality, Chile has developed the name of being a low end producer of reasonably good quality wines, which is commonly seen as one of Chile's major advantages. However, considering the current situation of global oversupply and increased competition, especially in the basic and premium sectors, -where large importers and supermarket chains have increased their negotiating power and consumers show a low-level of involvement- Chile's image of a low-cost producer entails a risk of getting stuck in these segments. This would make the Chilean wine industry vulnerable to a high level of competition and price volatility (Moguillansky, Salas and Cares, 2006). In this respect, this image might also be considered a disadvantage instead of an advantage. It is important for Chileans to keep increasing the quality of their wines to be able to enter higher segments (super and ultra premium, where competition is less fierce), and command higher prices, perhaps even more so for smaller wineries. This is a very difficult process however, especially for the same smaller wineries which presumably often lack a variety of skills and capital. One expert pointed out that *within* the higher price, higher quality segment however, it might become an advantage again being seen as the cheaper alternative (good value for money), as long as the quality of the Chilean offerings is seen to be equal or even better than those of competitors. But the difficulty is how to get to that higher segment. Currently Chilean wine is still not perceived as having competitive quality at all price points. Additional problems for Chile's wine exports include the low dollar exchange rate, which translates into lower profit levels in Chilean Pesos, and high electricity prices, increasing production costs and putting pressure on producers' margins.

Apart from moving up segments, it is also important to keep on targeting new markets to reduce risk. Although Chilean wineries export to over 100 countries nowadays, around 30% of exports (both in volume and value) are destined to the US and UK. Two markets in which competition is fierce, and where Australia also commands high market shares. Furthermore, 54% of export value and 58% of export volume goes to North-Western Europe and North America. Gaining sufficient market share in (relatively) new markets also offers a first-mover advantage, perhaps making it easier to position Chilean wines as high quality, ultra premium wines, or in whichever way is deemed most desirable.

We may conclude that the Chilean wine industry has to deal with an almost paradoxical challenge: consolidating its position as an exporter of good quality wines at competitive prices, whilst at the same time entering higher price segments. To be able to achieve this goal, quality levels need to be increased and consumer perceptions of Chilean wine as good and affordable, perhaps even cheap, need to change as well. Ideally a consumer should no longer think of Chilean wine as “cheap and good” but as “good quality”, and willing to pay a premium for that quality. In this respect, it might be considered a problem that many Chilean wineries are still operating in the lower segments. Furthermore, Chile’s two most famous wine brands, Concha y Toro’s *Casillero del Diablo* and San Pedro’s *Gato Negro*, are both lower priced brands. Although other countries face the same challenge to increase quality and obtain higher prices, it is more complicated for Chile, because of a lack of country image, or at least the “wrong” country image. A well developed country image would contribute to successfully influencing consumer perceptions.

3.13. Conclusion

As was shown in the previous chapter, Chile’s wine industry has a strong competitive advantage position compared to other major producers, both Old World and New World. Planted acreage, production and export levels have shown impressive growth rates; only domestic consumption has lagged behind. Exports have increased in volume as well as value, and are increasingly diversified geographically, although the US and UK are still the most important markets. The country’s main strengths concerning wine production are its natural resources and low costs, whereas technology levels are more or less equal to most other exporting nations. Chile’s wines are therefore famous for their good price-quality ratio and Chile’s wine sector is an attractive FDI target. At the same time, Chilean wineries are committed to continually increase the quality of exported wines to be able to enter higher, more attractive price segments. It is considered a challenge to enter higher price segments whilst being famous for lower priced wines. However, once such a higher segment is successfully reached it might be very beneficial again to be considered as the lower priced, equal quality alternative.

The wine industry is relatively fragmented, which also holds true for Chile, although less so than Europe. However, Chile’s biggest wineries are relatively small compared to other international wineries. Individual wineries in general lack the ability and resources to invest in and establish elaborate marketing and branding strategies. A form of cooperation among wineries is therefore deemed necessary. The establishment of Wines of Chile, a collaboration between ChileVid and Viñas de Chile (Chile’s two major wine business associations, uniting small and large exporting wineries) is therefore considered an important feat. At present there is still a lack of country image for Chilean wineries to profit from however. This impedes the industry’s aim of entering higher price segments, as consumers do not perceive Chilean wines as being expensive and high quality. Furthermore, it is argued that a country image should be established beneficial to all export products. This means it could be considered a collective good and might be developed through a public-private partnership between wineries, business associations and government agencies, such as ProChile.

Small Chilean wineries are even more focused on higher quality exports than their larger competitors, as the domestic market is dominated by the big three and is not considered very attractive in any case. Furthermore, it is easier for smaller wineries to increase the quality of their wine than to invest in substantially increasing production capacity. Smaller wineries are equally considered to be even more dependent on industry cooperation and the development of a beneficial country image, as they arguably have even less resources to invest in marketing and branding to influence consumer perceptions and purchasing decisions.

The next chapter revises three strands of business literature (business strategy, marketing and branding) deemed essential to understand the opportunities and threats facing the Chilean wine industry, the small wineries in particular.

4. Theoretical Basis

This chapter will discuss three major strands of business literature (strategy, marketing and branding) thought to be of importance to the success of any enterprise, regardless of the industry it operates in. However, although theoretical and general, an effort will be made to aim these strands of literature on the wine business, and on small Chilean wineries in particular. First business or competitive strategy shall be discussed, followed by marketing and branding. The specific order of first strategy followed by marketing and branding has been made under the assumption that a company's branding strategy is part of its marketing strategy, which in its turn should be based on the company's overall business strategy.

4.1 Strategy

In order to be successful, at least in the longer term, every enterprise should operate with a certain strategy in mind. Although the literature on *Strategic Management* is diverse, undecided, often paradoxical and mostly aimed at Multinationals (MNC's) operating in an international or even global context, it is considered a useful exercise to use this strand of literature to gain insight into the strategies pursued by (small) wineries which commonly operate indirectly in various countries through exports.

According to Johnson and Scholes (2002) *Strategy* might be defined as:

The direction and scope of an organization over the long-term, which achieves advantages for the organization through its configuration of resources within a changing environment and to fulfil stakeholder expectations

One of the problems of Strategic Management is the various theories and ways of looking at Strategy which have been developed. For instance, by analyzing the literature, Mintzberg et al (1998) have identified 10 "Schools of Strategic Management": The *design, planning, positioning, entrepreneurial, cognitive, learning, power, cultural,* and *environmental* and *configuration* schools.

Table 22: The 10 Strategy Schools and their view on Strategy Formation

Strategy School	Strategy formation as a:
Design	Conception Process
Planning	Formal Process
Positioning	Analytical Process
Entrepreneurial	Visionary Process
Cognitive	Mental Process
Learning	Emergent Process
Power	Negotiation Process
Cultural	Collective Process
Environmental	Reactive Process
Configuration	Transformation Process

Source: Mintzberg et al (1998)

These schools are often divided into two different approaches, which are more or less opposite to each other: the *Outside-In approach* (Positioning School) versus the *Inside-Out approach* (schools concerned more with the company's competences). This translates into a distinction between two views which can be defined as the Deterministic view, which takes the industry and the company's strategic fit to its environment as a starting point to develop strategy, versus the Voluntarism view, which stresses the importance of the firm and its strategic stretch as a basis for developing a competitive business strategy. This distinction is primarily theoretical in nature. In practice firms operate and make decisions, either consciously or unconsciously, based on a combination of internal strengths and weaknesses as well as –perceived- external opportunities and threats.

4.1.1 The Outside-In approach to Strategy

The positioning school is somewhat similar to the planning school and is primarily concerned with analyzing the industry the company competes in (the Outside-In approach) to be able to choose a certain type of generic strategy to defend a market position. In this view Strategy is seen as a way to "fit" the firm to the environment. Strategic Fit can be defined as: *developing Strategy by identifying opportunities in the business environment and adapting resources and competences so as to take advantage of these* (Johnson and Scholes, 2002).

The generic strategies that have either been devised or further developed under the influence of the Positioning School philosophy include the famous Low Cost, Differentiation and Focus (Niche) strategies (Porter, 1980), as well as Innovation and Entry strategies (or Barriers to Entry strategies).

A Low Cost strategy is considered as more than one strategy as it involves implementing five different driving forces: no frills product/service, product design, production and operations design, scale economies and experience curve (Aaker, 1998). Firms that have achieved cost leadership have the lowest production and distribution costs. They must be good at purchasing, manufacturing and physical distribution, but need less skill in marketing (Kotler, 2000). The danger of this strategy is that it is easily copied and will likely not lead to a sustainable competitive advantage (SCA). In the Wine industry this strategy is used by producers in the so called Basic segments, producing and exporting wine in bulk. Certain countries such as Chile and perhaps Argentina also have a cost advantage over other wine exporting nations such as the US and France, because of lower land and labour costs leading to lower production costs. In general one might assume larger exporting wineries have a cost advantage over smaller ones because of economies of scale, although it is believed that all Chilean wineries are said to actively pursue cost saving production methods. Keeping costs down is one of the few strategies individual Chilean wineries have a direct influence on. However, a study by Visser and de Langen (2006) found that Chilean wine experts interviewed do not consider a low-cost strategy alone sufficient to increase competitiveness on the export market. Other important factors are an increase in variety and quality of the wines produced, as well as investment in branding. As has been mentioned before, the Chilean wine Industry has rightfully recognised the importance of increasing the quality of the wine produced so as to be able to target higher price segments, where competition is less and margins higher.

A Differentiation strategy is defined by Johnson and Scholes (2002) as a strategy that seeks to provide products or services unique or different from those of competitors in terms of dimensions widely valued by buyers. Differentiated marketing may be defined as a strategy in which a company operates in several market segments and designs different programmes for each segment. A company’s market offering can be differentiated along five dimensions: product, services, personnel, channel, and image. Product Design is the factor that will often give a company its competitive advantage (Kotler, 2000). Product design and differentiation is related to the topic of branding, which shall be discussed shortly. According to Visser and de Langen (2006), innovation in the Chilean wine industry is considered the second most important problem that should be resolved to increase competitiveness, especially the need to differentiate the product. Differentiation in this case means increasing product variety while maintaining or improving the quality and consistency of wines. Again, it might be assumed larger wineries are better able to differentiate their product in the sense that they can more readily produce a larger variety of wines, although we have seen before that smaller wineries are capable of withstanding competition from the big three mainly based on product differentiation, adding value to both their wines and their brands, so they can focus mainly on the export market with high quality wines (Urquieta and Rojas, 2006). Furthermore, the Chilean Wine industry as a whole differentiates itself from other wine producing nations through its geographic characteristics (terroir, etc) and viticultural advantages, such as a clean environment, foothills, drip irrigation, clone selection, etc. This enables Chilean wineries to produce high quality, differentiated wines appealing to consumers.

A Focus Strategy, or niche strategy, is a strategy in which the business focuses on one or more narrow market segments. Within this target segment the firm can either pursue a cost leadership or differentiation strategy (Porter, 1980). A Focus Strategy does not necessarily have to be based on a certain narrow customer segment, as a company can also focus on a certain product line or a certain limited geographic market (Aaker, 1998). Almost all Chilean wineries follow a niche strategy, especially the smaller firms. Even a general strategy of targeting higher price segments with a variety of higher quality wines is considered a niche strategy, as these higher price segments are still considered a niche market. As was already mentioned before, a weakness of the Chilean wine industry is that it is a global niche player without strong brands, making it difficult to find the right distribution channels.

A Continuous Innovation Strategy means being a leader in developing new products, customer services, distribution effectiveness and cost cutting. An Innovation refers to any good, service, or idea that is perceived by someone as new (Kotler, 2000). Innovations are necessary to increase world wide wine consumption, which is below production levels. Considering wine innovation may be aimed at the product, the label and the packaging. As was just mentioned, in the Chilean wine industry innovation is often seen as a key way to differentiate the product, which should ultimately lead to increased competitiveness. Firm size doesn't seem to matter to successfully pursue an innovation strategy. Product innovation (for example increasing quality) through viticultural and/or vinification innovations does not depend completely on firm size, although it might be argued that larger firms might have more resources and therefore might be able to attract the best winemakers, buy the best machinery and grapes, invest in innovative labelling and packaging. However, this is a generalisation as many smaller wineries might have the resources and knowledge to do the same.

An Entry Strategy refers to the various ways a firm may enter a certain market or market segment. In a global or international context these include exporting (both direct and indirect), licensing, franchising, contract manufacturing and a direct entry strategy, perhaps through a joint-venture or direct investment. Most Chilean wineries actively look for distributors and importers in various foreign markets.

Furthermore, the Outside-In approach/Positioning School has led to a few of the most widely used strategic analysis tools such as Porter's five forces and value-chain models, as well as Abell and Hammond's Learning Curve, Ansoff's Product-Market Matrix and the BCG Group's Product Portfolio Matrix. Although the Positioning school came to the fore in the 1980s and has met considerable critique since, many of the above mentioned strategies and analytical tools/matrices are still widely studied and used today, but mostly aimed at large Multinational Companies (MNCs).

4.1.2. The Inside-Out approach to Strategy

The Inside-Out approach takes the firm as starting point instead of the industry/environment. This approach is based more on an entrepreneurial philosophy and might even be traced back to the design school. It was devised at the end of the 1980s and beginning of the 90s as a counterweight to the previously mentioned view. It sees strategy primarily as the choice of a unique set or certain combination of a company's (core) competences and (unique) resources, which are used to create an advantage over competitors. This is often called strategy as stretch. Strategy as stretch is the opposite of strategy as fit. The strategy as fit philosophy takes the industry/environment as a given, in which the firm should try and apply a strategy that best fits to this environment. Strategy as stretch is a philosophy that starts with the firm and looks at the firm's specific resources and competences, which it should use to devise a specific strategy, regardless of what the environment it operates in looks like. Johnson and Scholes (2002) define Stretch as: *the leverage of the resources and competences of an organisation to provide competitive advantage and/or yield new opportunities*. Core competences are those competences that underpin the organisation's ability to outperform competition by meeting the critical success factors better than competitors (Johnson and Scholes, 2002). A core competence provides potential access to a wide variety of markets, it should make a significant contribution to the perceived customer benefits of the end product and finally, a core competence should be difficult for competitors to imitate (Hamel and Prahalad, 1990). Critical Success Factors of a firm are those product features that are particularly valued by a group of customers (Hamel and Prahalad, 1990). Critical Success Factors may also be identified at a national or industry level, as we have seen before. The way a business articulates and actions its critical success factors is a major determinant of sustainability and success (Demediuk, 2003).

Aaker (1998) defines two other possible strategies which are based more on the inside-out approach (apart from the Low Cost, Differentiation and Focus Strategies mentioned under the outside-in approach). First of all there is the Pre-emptive Move Strategy; a strategy which is new in its segment and should be based on a competence which is not easily copied by competitors due to technological leadership. In the case of the Chilean wineries, there are no real technological leader firms. Most firms have a reasonably high level of technology at their disposal and so are able to produce fairly high quality wines. This is not only the Chilean reality, as the situation is similar in many wine producing and exporting nations. The large firms however do have an advantage over smaller firms in that they have a larger production capacity and therefore can benefit from economies of scale and scope. This enables the large firms to produce in higher quantities, as well as more varieties of wine than smaller wineries.

The second strategy is a so called Synergy Strategy which is based on the relative advantage that can be achieved through cooperation among various departments or Business Units within an organisation. It is assumed that bundling competences makes them more unique and so more difficult to imitate by competitors. Synergy is supposed to enhance consumer benefits and reduce operational costs and investments. Again, this strategy seems more likely to be pursued by a large MNC, consisting of various (international) business units or subsidiaries. Some larger wineries do however have smaller subsidiaries which might behave more or less independently from one and other in terms of production, but benefit from a united marketing and sales strategy. A lack of cooperation, both between wineries as well as between wineries and public organisations, is often cited as a constraint to the success of Chilean wineries, both concerning large and small firms.

4.1.3 Other views on Strategy

The newer Schools of Thought (the cognitive, learning, power, cultural, environmental and configuration schools) are diverse, yet unified in the criticism of the above mentioned schools for being too rational and therefore too limited and static (Mintzberg et al, 1998). Limited in the sense that they do not account for the role that factors such as culture and politics might play. And too static in the sense that strategy might also be considered as an intuitive or incremental learning and/or creative process. As such, the accent has changed from prescriptive philosophies on strategy to a more descriptive focus. At present there seems to be a strong focus on (strategic) networks and cooperation between external and internal partners, as well as identity (culture) and (core) competences. Also, more attention is being given to innovation, leadership, knowledge and Human Resources (Mintzberg et al, 1998).

Cooperation between firms, or networks, seems a logical option for small exporting wineries, since Global Wine Market competition is expected to increase because of a worldwide oversupply of wine. Also, because of the increasing negotiating power of distributors and large supermarket chains, it is assumed that smaller wineries could strike better deals with these parties by cooperating. Strategic networks can be beneficial if the firms involved can profit and learn from the other firms' competences (Hamel, Prahalad and Doz, 1989). Cooperating with the competition is increasingly interesting when market shares of the participating firms are small, which is the case for small Chilean wineries. However, if most companies have the same strengths (in the case of Chilean wineries: low costs, good quality production) and weaknesses (lack of marketing and branding skills), it might be considered difficult to create a mutual basis for cooperation. Still, it has been noted that the success of the Chilean Wine Industry in world markets is currently stimulating increased cooperation between firms and other actors in other areas where the industry needs to improve: marketing and promotion, internationalisation, and innovation and training (Visser, 2004). In the case of the Chilean Wine industry strategy formulation, cooperation and cluster governance skills are important and will determine whether collective upgrading efforts succeed, export growth continues, or decline sets in (Visser and De Langen, 2006). Smaller Chilean wineries sometimes join forces by forming a cooperative organisation, pooling sales and/or marketing resources, although a lack of trust and free-riding often leads to dysfunctional cooperatives. Also, larger firms might join forces with smaller firms. According to Visser and de Langen (2006) some larger Chilean wineries entering new export markets still need smaller firms to supply a larger variety of products. The smaller firms also profit because the larger firms mitigate typical constraints (financial and human resources) suffered by the smaller wineries interested in exporting to the same new markets. However, in general it is argued that there is still a lack of cooperation among wineries, but also between wineries and public support organisations.

As was mentioned at the start of this chapter, a lot of the literature in the field of Strategic Management is aimed at MNCs. Strategic Management in a small business context is not as widely covered, but a few generalisations might be made (Barrow, Brown and Clarke, 1995): Small businesses are likely to operate in a more limited number of markets with a more limited range of products and services. The scope of the operation is therefore likely to be less of a strategic issue than it is in larger operations. In smaller firms the values and views of the executives (often also the owners) are likely to be very important. Indeed, in a study on critical success factors at a small (profitable) Australian boutique winery, Demediuk (2003) concludes: *in common with other small businesses, the owner/manager in smaller wineries is typically involved in every aspect of running the business. Such a hands-on approach has some redeeming features, but immersion in short-term problem-solving is also a threat to competitiveness and growth. Owners typically focus solving immediate problems, and consequently their work and that of employees is not always focused in a* *balanced-way on activities that contribute to essential longer term goals*. It is also likely that the small company will be exposed to significant competitive pressures so competitive strategy is very important. Small firms are often privately owned which affects their ability to raise capital. Furthermore, their size will often prevent them from having large market research departments, impairing their ability to devise elaborate marketing and branding strategies. All of these generalisations seem to apply to the average small Chilean winery. However, this paragraph doesn't show any absolute advantage that larger exporting Chilean wineries might enjoy over their smaller counterparts in pursuing any of the mentioned generic strategies, apart from economies of scale and scope in terms of production, which might be an advantage in finding larger distributors. Also, it is assumed that in general larger wineries have more resources to their disposal.

4.2 Marketing

The Old World wine industry, especially France, is still rooted in traditions and largely based on production-oriented export growth (Atkinson, 1999). Although things are rapidly changing, mainly due to the New World's (and increasingly Spain's) attention to and better use of marketing and branding, it has been argued that there is still a lack of marketing orientation throughout the wine industry. Several authors have highlighted this from different perspectives (for a summary I refer to Bruwer, Li and Reid, 2002): Howely and Young (1992) and Lockshin (1999) concluded that there is "*a lack of marketing skills in the wine industry*"; Sharp (1991) stated that "*marketing is not relevant for smaller wineries*"; and Hall and Winchester (1999) felt that "*wine will market itself*". Spawton (1991) stated that the wine industry is *sales rather than marketing oriented*. Various authors have also been critical of the wine industry's mass marketing approach. However, the wine industry is suffering from a global oversupply, growth is expected to flatten and competition to intensify, especially in the (lower) premium price segments. Also, consumers now require a higher degree of novelty and clarity (Visser and de Langen, 2006). This means that even small wineries will have to adopt a marketing orientation to be able to stand out and influence consumers' purchase decisions. Apart from these mentioned production, selling and marketing concepts or orientations, companies or industries may also have a product or societal marketing orientation (Kotler, 2000).

The Production Concept holds that consumers will prefer products that are widely available and inexpensive. This means a firm focuses on low cost, high production efficiency and mass distribution.

The Product Concept states that consumers will favour those products that offer the most quality, performance or innovative features.

According to the Selling Concept the organisation needs aggressive selling and promotion activity to sell its products. The aim of selling-oriented firms is to sell what they make rather than make what the market really wants. This indeed seems to be the case for many (small) Chilean wineries, although perhaps without the aggressive promotion activity due to a lack of capital and customer knowledge.

The Marketing Concept holds that the key to achieving its organisational goals consists of the company being more effective than competitors in creating, delivering, and communicating customer value to its chosen target market.

The latest concept is the Societal Marketing Concept which states that the organisation's task is to determine the needs, wants and interests of target markets and deliver the desired satisfactions more effectively and efficiently than competitors in a way that preserves or enhances the consumer's *and* society's well-being. This includes current trends to market a product or company as being concerned with the environment, or with social equality. As was previously discussed, a marketing concept that not only benefits the company or private sector as a whole, but also society's well-being might be considered a collective good and therefore merits public support, as is the case in developing a generic promotion strategy (country image) for Chile's export products. In the wine business, it is currently becoming popular to produce and sell organic wines, or wines made from grapes grown in an environment friendly manner.

It seems that, in general, the Wine industry is still very much operating according to a product, production and/or selling orientation, although marketing (and branding) have become more popular the past decade, especially due to the ascendance of Australian branded wines in the 90s.

In light of the above concepts, Kotler (2000) defines Marketing as:

A societal process by which individuals and groups obtain what they need and want through creating, offering and freely exchanging products and services of value with others.

Marketing Management may be defined as:

The process of planning and executing the conception, pricing, promotion and distribution of ideas, goods, services to create exchanges that satisfy individual and organisational goals.

Kotabe and Helsen (2004) add to this definition that marketing is also about anticipating and creating *future* customer needs at a profit. In the context of the wine industry, anticipating and creating future customer needs might be considered producing new blends, or devising different winemaking methods to create differentiated and new wines. It may also involve educating consumers, for instance about grape varieties or different grape producing valleys, through marketing communication strategies. Especially Australia has proven to be very successful at all of the above.

Of course there are a multitude of possible marketing strategies a company may pursue, but any strategy needs to fit with the overall strategy and (international) development phase of the firm. Ideally, corporate strategy (or competitive strategy in the case of smaller companies) should drive a firm's marketing strategy (White and Griffith, 1997). In turn, a branding strategy is part of a firm's marketing strategy.

Considering a firm's stage of development Kotler (2000) defines entrepreneurial marketing (for a very small company, usually owned by one individual), formulated marketing (increasing a mid-sized company's name recognition through a more formulated strategy and perhaps research department) and entrepreneurial marketing where formulated marketing should become more consumer oriented and firms devise strategies to add value to their customers' lives. Small wineries, which do not cooperate or do not yet have a coherent national marketing programme to adhere to (the Chilean case), are still very much stuck in entrepreneurial and perhaps formulated marketing phases, although they are often more export than domestically oriented.

When becoming more internationally oriented, a company should generally adjust its marketing strategy, or even devise different marketing strategies, according to its degree of experience and nature of operations in international markets. These different possible strategies according to the level of internationalisation are: domestic marketing, export marketing (indirect and direct), international marketing (when companies begin to manufacture locally and may even set up foreign subsidiaries, a polycentric approach), multinational marketing (when a company might realise some economies of scale by consolidating some activities on a regional basis, a regiocentric approach), and global marketing (which emphasizes standardisation efforts, coordination across markets and global integration) (Kotabe and Helsen, 2004). Companies operating on an international basis have three general options: a Global Strategy that sees the world as a single market, a

Multinational Strategy that treats the world as a portfolio of markets and a Glocal Strategy that standardizes certain elements and localizes others (Kotler, 2000). Most small Chilean wineries are exporting, normally through a number of importers and distributors, to a variety of countries and they generally do not have a manufacturing base abroad. Often, they do not have an elaborate business or marketing strategy and see the world as one single market, or as a portfolio of markets.

Another important distinction between marketing strategies, especially relevant to the Global Wine Business, is explained by who the firm's marketing activities are directed to: the end consumer (a pull strategy) or retailers/wholesalers, who in turn use their marketing skills to attract consumers to buy the product (a push strategy). In general, a push strategy is appropriate where there is low brand loyalty in a category, brand choice is made in the shop, the product is an impulse item, and product benefits are well understood. A Pull strategy is appropriate when there is high brand loyalty and high involvement in the category, people perceive differences between the brands and people choose the brand before they go to the shop (Kotler, 2000). It seems that small wineries, which (individually) often do not have the marketing skills, consumer knowledge or the financial clout to promote their products to the end consumer in various countries, would follow a push strategy. Especially firms operating in the popular premium and premium (supermarket) segments, where brand loyalty does not seem to be very high (yet) and where most customers are considered to be low-involvement consumers. However, also firms operating in higher price segments, targeting high level restaurants and specialty stores, often aim their marketing and promotion efforts towards their importers, distributors, sommeliers and wine journalists instead of the end consumer. Again, an industry-wide national promotion organisation may be considered better equipped to target these agents than individual wineries, as well as having a better chance to directly influence final consumers. The different price segments of wine will be discussed later. In the Chilean case, by my knowledge only Concha y Toro, Chile's biggest wine producer, directly tries to influence consumer buying behaviour by advertising it's most famous brand, Casillero Del Diablo, on international television channels such as CNN.

4.2.1. Market Segmentation

An important process within marketing is Target Marketing, or the STP process, which stands for Segmentation, Targeting and Positioning.

According to Kotler (2000), The STP process starts with identifying and profiling a distinct group of customers, who might require separate products or marketing mixes (Market Segmentation). Then, one or more segments are chosen to enter or serve; the Target

Market(s). Lastly, the product's key distinctive benefits should be established and communicated to the target market; Market Positioning.

Segmenting and positioning are intertwined processes. Decisions about positioning affect the choices of a firm's marketing segmentation and segmentation decisions influence the way in which the firm positions a brand or product (Hassan and Craft, 2005). There are numerous bases for Segmentation of consumer markets, which are often divided into two distinct groups. The first group are the Macro-Level bases which include Demographic, Geographic, Political, Economic, Industrial Structure, Cultural, and Technological variables. The second group consists of Micro-Level bases, such as lifestyle, consumer responses to marketing, attitudes, tastes, predispositions and cultural traits (Hassan, Craft, Kortam, 2003). Micro-level segmentation bases are suggested for firms seeking differential positioning strategies, but both micro and macro variables should be used in order to leverage similar strategic positioning across global markets (Hassan and Craft, 2005). Micro level bases may be simplified into lifestyle and behavioural variables, or lifestyle and psychographic variables (Kotler, 2000). Lifestyle variables are increasingly used in studies on wine market segmentation. These micro-level segmentation variables are often based on cultural and social anthropology instead of pure demographic or socio-economic classifications.

Baalbaki and Malhotra (2001) discern two different, yet similar bases for international market segmentation: Environmental Bases (geographic, political, economic, cultural) and Market Management Bases (product, promotion, price and distribution related variables; which together form the company's marketing mix).

Another often used distinction is between Intermarket and Intramarket Segmentation. Intermarket Segmentation involves the detection of segments that exist across regional/national borders which can lead to a certain standardization of marketing strategy and the marketing mix across countries/segments. This is considered the simplest way to extend into international markets (Hassan and Craft, 2005). Intramarket Segmentation involves segmenting each country's markets from zero.

As a subject, Market Segmentation has a long and debated history in marketing literature. Its application in the Wine Industry seems to be in its infancy and needing careful assessment (Thomas and Pickering, 2003). However, it is considered very important. A study by Foster et al (2002) found that those firms identifying select groups of consumers receive a higher price and this relationship apparently holds regardless of winery size.

Bruwer, Li and Reid (2002) reviewed various wine market segmentation studies and found that essentially nine different segmentation variables have been used to study wine markets: *quality, risk-reduction, consumption, occasion based, and cross-cultural,* *behavioural, involvement, geographical and wine-related lifestyle.* A few of these market segmentation studies using the wine industry as subject might be worth mentioning:

Mc Kinna (1986) was among the first to undertake a market segmentation study based on wine. He identified four wine customer segments: *connoisseurs*, *aspirational drinkers*, *beverage wine consumers* and *new wine drinkers*.

Edwards and Spawton (1990) refer to three of the same segments, but change *beverage wine consumers* into *bag-in-box wine drinkers*.

Hall and Winchester (2000) found support for three of the four clusters mentioned before, but not for the *new wine drinkers* segment. They proposed to include an *enjoyment-oriented segment*: young people out to have a good time and who may be new to wine as a beverage.

It has been argued that a deeper understanding of the wine consumer is offered by examining usage *occasions* and therefore the use of *occasion-based* segmentation over *user-based* segmentation might be better (Dubow, 1992). As an example, high price becomes more important when a consumer (regardless what type of consumer) is purchasing wine in order to impress someone or to celebrate something special. Low price has been demonstrated to be important when the situation is to relax at home by oneself, or when throwing an informal party. Different consumption situations amplified or muted the importance of different wine attributes (Hall and Lockshin, 2000).

Bruwer, Li and Reid (2002) identified wine as increasingly becoming a *lifestyle beverage* and found evidence of five wine-related lifestyle segments in the Australian Domestic Wine Market: *purposeful inconspicuous premium wine drinkers, ritual oriented conspicuous wine enthusiasts, enjoyment seeking social wine drinkers, fashion/image oriented wine drinkers,* and *basic wine drinkers*. These social stratifications based on lifestyle actually exceed pure economic theory.

In a study examining wine retail choices of two samples from two different countries (France and Australia), Lockshin, Quester and Spawton (2001) examined the respective contribution of *involvement* and *nationality* (culture) as segmentation variables. The results suggested that although French wine shoppers differ somewhat from the Australians, retail strategies aimed at identifying high-involvement wine consumers may be more successful on a global scale (indicating that standardisation/globalisation might be more effective than (g)localisation/adaptation of certain strategies according to country). In other words, involvement was a better predictor of wine choice behaviour than the nationality of the wine consumers.

So the level of consumer involvement can also be seen as an important segmentation basis. *Low involvement* consumers generally shop in supermarkets (where wines are increasingly stocked according to country of origin and grape variety), whereas *high involvement* consumers normally tend to shop in specialty wine stores. High involvement consumers utilise more information and are interested in learning more, while low involvement consumers tend to simplify their choices and use *risk reduction* strategies. To reduce risk, low involvement consumers use price and award to a greater degree than high involvement consumers. A gold medal increases the choice probability the most, but mainly at the lower and middle price points, and a well known wine region amplifies the desirability of small brands more than large brands (Lockshin et al, 2005).

Thomas and Pickering (2003) review the above mentioned segmentation studies and add another: behavioural segmentation based on bottles purchased. They conclude that a number of significant differences exist between light, medium and heavy wine purchasers, at least in New Zealand.

Interestingly, most Wine-related marketing literature and research seem to stem from Australia, New Zealand and the United States, all New World producers famous for their use of marketing and branding.

4.2.2. The Marketing Mix

After the firm concludes the STP process it has to devise a set of tools to attain its goals. Kotler (2000) defines the Marketing Mix as the set of marketing tools a firm uses to pursue its marketing objectives in the target market(s). These marketing tools are grouped together into the famous 4Ps of Marketing: Product, Price, Promotion and Place (Distribution) (Mc McCarthy, 1996).

A Product is often seen as consisting of various layers. Kotler (2000) identified five: core benefit, basic (generic) product, expected product, augmented product and potential product. The core benefit is the fundamental service or benefit the consumer is buying. The basic product enables the core benefits. The expected product consists of the attributes and conditions buyers would normally expect when buying the product. The augmented product are the benefits that actually exceed customer expectations, they are often not tangible. The potential product entails all the possible augmentations and transformations the product might undergo in the future. The augmented and potential product attributes and benefits is where companies not only satisfy, but surprise and delight consumers. This is where their offering should be distinguished from other offerings. The Product Mix, or assortment, is the set of all products and items that a firm offers for sale.

Price is often seen as critical within the Marketing Mix as it is the only P that actually generates revenue instead of costs. A Pricing Policy encompasses the following six steps (Kotler, 2000): Selecting the Pricing Objective; Determining Demand; Estimating Costs;

Analyzing Competitors' costs, prices and offers; Selecting Pricing Method; Selecting the Final Price. In general, price may be based on competitors, customers/buyers or on the firm's own costs or (financial) targets. Possible Pricing Objectives include: survival, maximum profit, and maximum market share, maximum market skimming or product-quality leadership. The influence of the other Marketing Mix elements should also be taken into account in deciding on the final price. Also, different market segments often lead to adaptations in price. A few well-known Price-Adaptation Strategies include: geographical pricing, price discounts, promotional pricing, discriminatory pricing (when a company sells a product at different prices to different segments), and product-mix pricing. An increasingly popular pricing method, Perceived Value Pricing, is based on the customer's perceived value. This concept is closely related to Branding and plays an important role in the Wine Industry. A strong Brand implies a strong ability to differentiate from competitors and so a firm with a strong brand can command a price premium.

The Consumer Wine Market is often segmented into six distinct segments according to *price* and *features*:

Table 23: Consumer Segments in the Wine Industry according to Price

Category	Consumer Price p. Bottle	Features
Icon	> 150 €	Long term image, high scores, complexity, prestige
Ultra-Premium	14 -150 €	*Varietal* or *blend*, reasonably high scores, character, origin, image
Super-Premium	7-14€	Brand, recognizable, origin, structure, *varietal* or *blend*
Premium	5-7€	Brand, origin, recognizable, accessibility
Popular-Premium	3-5€	*Varietal,* fruity, accessibility, brand
Basic	<3€	Low price and traditional, often bulk

Source: Heijbroek (2003)

In purchasing wine, price is often seen as a way to overcome perceived consumer risk (Spawton, 1991). The risk that concerns consumers most is the taste of wine, according to Mitchell and Greatorex (1988). This means that a wine which is very low-priced is often seen as being of inferior quality and thus would taste bad. As was said before, it is predominantly the low involvement consumer who is concerned with risk reduction strategies. In the basic segment price is the most important attribute influencing consumer buying behaviour. The majority of wineries operating in this segment follow a cost leadership strategy. The popular premium and premium sectors is where the majority of branded wines, especially from New World countries, are to be found, although a relatively low price is still a decisive factor in purchasing decisions. In the super and ultra premium sectors branded wines still exist, but in general more expensive wines are more dependent on their quality image than their brand associations (Terheijden, 2005).

Currently, the Chilean Wine industry has been aiming to target higher price segments where margins are higher. Especially the US$ 15-25 price range (consumer price per bottle) is considered attractive because of a relative lack of competitors. In general, the Old World nations' wineries are either focussed on low price/high volume or high price/low volume segments. The Californian Wine industry produces similar or perhaps slightly higher quality wines than Chile, but at significantly higher costs. Australia is famous for its fairly low priced, easy to drink branded wines, but also produces a few high quality wines at high prices. However, within the US$ 15-25 segment Australian wineries are said to be fairly absent.

The Promotion Mix may consist of sales promotion, advertising, sales force, public relations, direct mail, telemarketing and the Internet. The choice for a specific Promotion Strategy is of course dependent on various factors such as the other Marketing Mix elements, the company's customer knowledge, its resources, the chosen segment(s), etc. Also, whether a firm is pursuing a previously mentioned pull or push strategy holds consequences for the chosen promotional activities. Some countries, such as Australia and South Africa, employ well-functioning national wine bureaus to promote the country's wine business as a whole (generic marketing), as well as reaching not only consumers, but also retail buyers, bartenders, restaurateurs, wine distributors, wine journalists, connoisseurs, and others who play an important role in influencing consumer decisions and thus ultimately an individual winery's sales. Developing good relationships with these agents becomes increasingly important in the higher price segments, where competition is less fierce and margins higher. Sales promotion influences in-store buying decisions, which is especially important for low-involvement consumers who often have not yet made up their mind when they enter a store. Advertising such as brochures and newsletters is supposed to increase brand awareness. In the wine industry, promotional activities aimed at the end consumer are mostly handled by the importers, distributors or even supermarkets (such as in-store advertisements). They often have a better understanding of the local consumer and can often command more resources too, especially when compared to smaller wineries. This leaves the local wine producers with focusing mainly on their product and how to push the product through the distribution channels most profitably and efficiently. Apart from the actual product, the wine itself, brand name and label (and perhaps some promo materials, such as leaflets) seem the only way for small producers to influence customer buying decisions directly. However, some large importers, with a lot of negotiating power, might even decide on which label or brand name the winery should use for its wine. Some wineries actively seek out importers which have the marketing and branding skills, and well-developed distribution channels, to both develop and distribute a brand successfully. These wineries, such as in the case of the Espiritu de Chile brand by Chilean winery Aresti, focus only on the production process and leave the rest to the importer and/or distributor.

The choice for a certain Distribution Channel (Place) depends in part on the consumer. In recent years there has been a shift in power within the wine distribution channel. Whereas the competition among wine producers is fierce, more and more wine is being sold through supermarkets (especially in the lower (popular) premium segments, where consumers seem to have a lower level of involvement). These supermarkets are often large and their power has been on the increase. They often import directly or do business mainly with large importers and distributors. Supermarkets prefer to buy large quantities of consistent wines to minimise their transaction costs. This is an advantage that larger producers have over smaller producers: they are able to supply larger quantities of wine and are able to offer supermarkets discounts to compensate them for the costs these supermarkets incur for in-store advertisements and discounts. This is called *promotional gain* (Terheijden, 2005). Since the 1990s market power of major distributors and importers has also risen considerably. Also, one might presume that the lack of marketing focus, capital, and customer knowledge among small wineries exporting to a multitude of countries makes these firms dependent on even the smaller local importers and distributors, which arguably have a better understanding of the local consumer as well.

4.3 Branding

Branding is an important part of Marketing and Strategic Brand Management is considered an important part of a firm's marketing strategy and ultimately its business strategy. According to the American Marketing Organisation a *Brand* is a:

"Name, term, sign, symbol, or design, or a combination of them, intended to identify the goods and services of one seller or group of sellers and to differentiate them from those of competition"

Keller (2002) adds: "*a brand is therefore a product, but one that adds other dimensions that differentiate it in some ways from other products designed to satisfy the same need*".
These differences may be tangible and rational, but also intangible, symbolic and emotional.

A brand helps consumers to reduce risk as it offers them a seal of quality and reliability. Secondly, it helps simplify buying decisions. Thirdly, it should convey a feeling, a way of life, or sense of belonging. Furthermore, a brand offers a consumer a certain image or characterisation, perhaps a sense of continuity; and hedonistic and ethical satisfaction, e.g. satisfaction linked to the attractiveness of the brand or its logo and satisfaction linked to the responsible behavior of the brand in its relationship towards society (Kapferer, 1997).

A brand is also helpful to the firm (Keller, 2002); a strong brand:

- Increases customer loyalty and thus repeat purchases
- Is less vulnerable to marketing efforts from competitors
- Increases margins (by being able to command premiums)
- Is less price elastic when prices are increased
- Is more price elastic when prices are decreased
- Increases negotiating power vis-à-vis retailers
- Increases the effectiveness and efficiency of marketing communications
- Increases the possibility to introduce brand extensions successfully

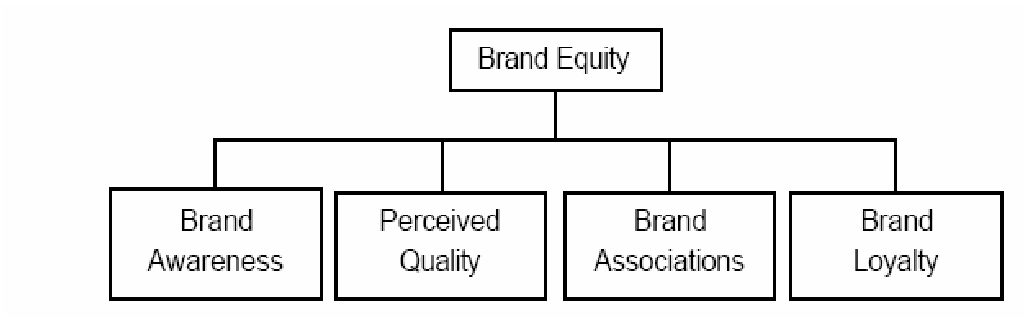
4.3.1. Brand Equity

The goal of branding is to enhance *brand equity.* The term *brand equity* was introduced in the 1980s and led to an increase in importance of branding in the marketing process. However, there is no consensus on the precise definition. A definition often used has been devised by Aaker (1991):

"A set of brand assets and liabilities linked to a brand, its name and symbol, that add to or subtract from the value provided by a product or service to a firm and/or to that firm's customers".

In Aaker's view *Brand equity* depends on five important elements: *brand awareness, brand associations, brand loyalty* and *perceived quality* and other proprietary assets such as *patents* and *trade marks* (Aaker, 1998).

Figure 2: Brand Equity

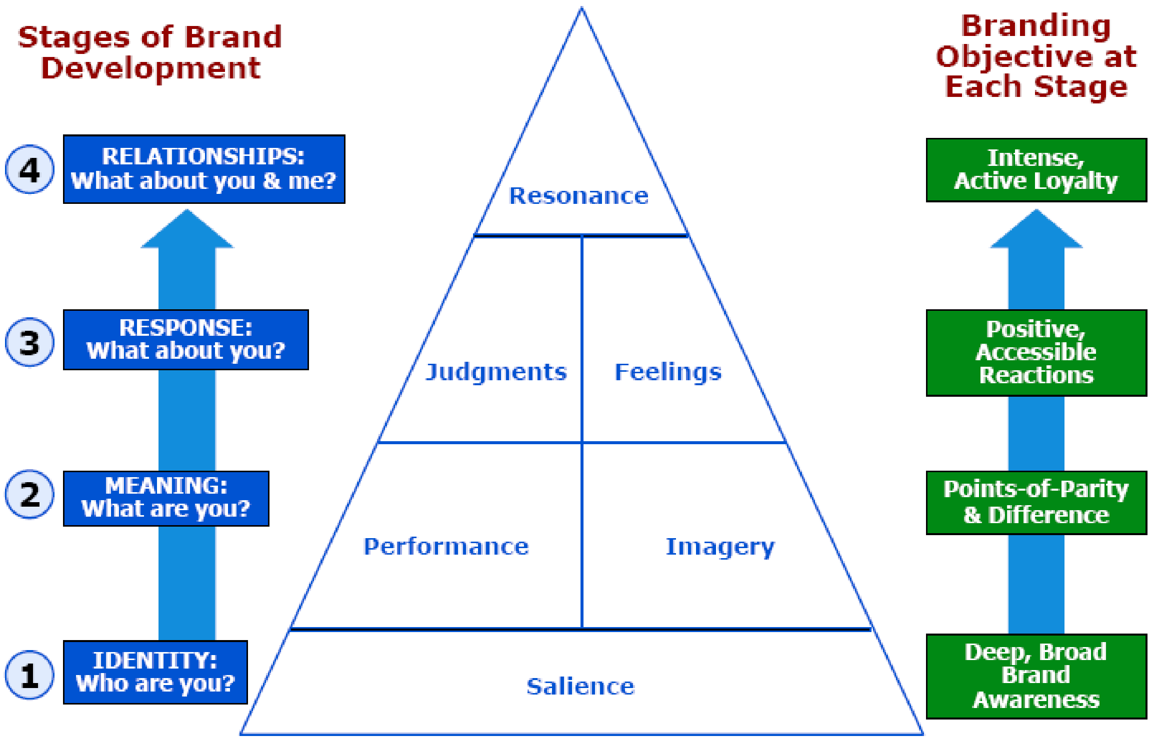


Source: Aaker and Joachimsthaler (2000).

According to Aaker (1998, 2000) Brand Awareness affects consumers' perceptions and taste (perceived quality). Perceived quality in turn influences brand associations and affects brand profitability. Brand associations are anything that connects the consumer to the brand, such as user imagery, product attributes, organisational associations, brand personality and brand symbols.

However, according to Keller (2002) brand equity depends only on *brand awareness* and *brand image* (including perceived quality) of which brand associations are also a part. Keller feels that brand equity does not depend on brand loyalty, but sees increased loyalty as an extra advantage and a result of brand equity. Keller has introduced the Customer Based Brand Equity (CBBE) Model; also know as the Brand Resonance Pyramid (see figure below). Keller defines the CCBE model as: *"the differential effect that brand knowledge has on consumer response to the marketing of that brand"*.

Figure 3: the Customer Based Brand Equity Model (CBBE)



Source: Keller (2002). http://wpcarey.asu.edu/AMA2007/upload/Brands-and-New-Media-Keller.pdf

In Keller's view *Brand Awareness* consists of *brand recognition* and *brand recall. Recognition* relates to the consumer's ability to confirm prior exposure to the brand when given the brand as a cue (passive recollection). *Recall* relates to his/her ability to retrieve the brand from memory when given the product category, or purchase or usage situation as a cue (active recollection). Recall is more difficult to attain than recognition. Brand awareness is created by (a mix of) brand elements such as name, symbol, logo, character, jingle, packaging, slogan etc. The choice between various brands in a certain category is called a consumer's *consideration set.* Within a certain product category a consumer will normally have no more than 5-10 brands in mind to choose from, so it is very important to be "inside" the consumer's consideration set. This is currently a major problem for individual wineries whose wines are shelved in supermarkets around the world among literally hundreds of other wine brands.

B*rand Associations* or *Brand Image* is what the consumer directly or indirectly thinks when thinking about the brand. *Brand associations* are divided into three elements: *strength, favourability* and *uniqueness.*

The *strength* of associations depends on *brand attributes* (descriptive features that characterise a product or service) and *brand benefits* (the personal value and meaning that consumers attach to the product or service attributes). Attributes are divided into *product related attributes* (for instance, grape variety) and *non-product related attributes* (for instance, price, *user and user image*-what type of person drinks what kind of wine, and under what circumstances- *brand personality, feelings and experience*). Wine has a high degree of *experience attributes* and so the ability of consumers to assess quality prior to purchase is severely impaired, and consumers will fall back on extrinsic cues in the assessment of quality (Speed, 1998). This is analogous to price as a cue for low involvement wine consumers following a risk reduction strategy when concerned about the wine's taste. *Brand benefits* are divided into *functional benefits* (the intrinsic advantages of drinking wine, such as health benefits), *symbolic benefits* (status symbol, social process), and *experiential benefits* (what feelings/benefits does the consumer experience after having dunk wine). Wine has some important symbolic benefits; it is often seen as a status symbol and a sign of good taste. This explains the basis for occasion based market segmentation: people tend to buy more expensive, higher quality wine when they want to impress somebody and/or at formal or important occasions.

Favourability consists of *desirability* and *deliverability* of the image associations. *Desirability* depends on the *relevance, the distinctiveness* and *believability* of the brand associations/image.

Uniqueness of associations depends upon a firm's ability to create *points of difference* of the brand in consumers' minds, so as to create a competitive advantage.

In short, these unique, strong and favourable brand associations are not only controlled by the marketing programme, but also by direct personal experience, word of mouth, country of origin, distribution channel, etc.

The way to build a strong brand, according to the CBBE model, is by following four sequential steps, each one representing a fundamental question that customers ask about brands:

1) Ensuring the identification of the brand with a specific product category or need in the customer's mind -who are you?

2) Establishing the meaning of the brand in the customer's mind by strategically linking tangible and intangible brand associations with certain properties -what are you?

3) Eliciting customer responses to the brand identification and meaning -what about you?

4) Converting the response into an active, intense and loyal relationship between the customers and the brand -what about you and me?

The CBBE model is built by "sequentially establishing six 'brand building blocks' with customers" (Keller 2002), that can be assembled as the Brand Resonance Pyramid (figure 3).

Brand salience relates to the depth and breadth of brand awareness. *Salience* (the number of attributes that come to mind associated with a product) leads to a greater likelihood of retrieving the cue in a purchase decision. According to Lockshin and Tustin (2003) different wine regions have differences in salience. *Brand performance* relates to the satisfaction of customers' functional needs. *Brand imagery* relates to the satisfaction of customers' psychological needs. *Brand judgments* focus on customers' opinions based on performance and imagery. *Brand feelings* are the customers' emotional responses and reactions to the brand. Lastly, *Brand resonance* is the relationship and level of identification of the customer with a brand.

4.3.2. Brand Loyalty

Brand Loyalty, whether seen as an element necessary for creating brand equity -Aaker-, or as a result/advantage derived from brand equity -Keller- is an important factor. Loyalty means repeat purchases by a consumer and thus increased sales. Loyalty can be caused by consumer preference, but –as in the case of large wine brands in supermarkets - also by having a large share of the market and therefore prominence in stores as well as advertisements. Increasing customer loyalty can be seen as a sustainable competitive advantage (SCA). First of all, it is easier to retain a customer than to attract a new customer, so loyalty reduces costs. Secondly, a strong brand loyalty can function as an entry barrier to competitors, as they would need to attract customers away from your brand (Aaker, 1998). Recall that a barrier to entry strategy is part of the outside-in approach to strategy. At the same time, a brand's ability to create loyalty, or better said, a company's ability to devise brands and branding strategies leading to loyal customers might also be considered a core competence, an inside-out view on strategy. However, brand loyalty in the Wine business, even among the lower premium branded wines in the supermarket, is relatively low.

4.3.3. Brand Name

A very important brand element is the *Brand Name.* Especially in the wine business, as brand name and (back) label are generally the only direct ways a producer might reach the end consumer. A name (as well as other brand elements such as logo, symbol, character, slogan etc) should be *memorable, meaningful, likable, transferable, adaptable and protectable* (Keller, 2002). A brand name should preferably not be descriptive, such as pure, clear, soft, etc as these are words that can also be easily used by competitors. Also, a Brand name should be able to stand the test of time, so it needs to be distinctive and creative. To be distinctive a brand name needs to convey a *personality*. Ideally, the name should be short; the shorter the better although there are a lot of successful exceptions to this rule (Bernick, 2005). Of course, once a brand name has been devised it is important that it is communicated well. At the same time, a brand name is often already an effective shorthand means of communication.

Landor's Associates have developed six distinct types of brand name categories (Keller, 2002:

Table 24: Landor's Associates six Brand Name Categories

Category	**Description/Example**
Descriptive	Describes function literally: *Singapore Airlines*
Suggestive	Suggestive of function: *Agilent Technologies*
Compounds	Combination of words: *Redhat*
Classical	Based on Greek, Latin: *Excelsior*
Arbitrary	Real words with no tie to firm: *Apple*
Fanciful	Words with no meaning: *Avanade*

Source: Keller (2002)

There are numerous suggested procedures for naming a brand. These may be summarised into six steps (Keller, 2002):

1. Define the branding objectives of the firm. What is the ideal meaning of the brand? What is the role of the brand in the brand hierarchy? Also, the role of the brand in the marketing programme must be understood, as well as keeping in mind what the target market is.
2. Generate as many names and concepts as possible (perhaps between 50-100).
3. Screen the names based on the objectives and considerations in step 1. Start to eliminate and do a quick legal search to screen out certain names.
4. Pick 5 to 10 names and do an extensive legal search.
5. Do consumer research with the names that are still available. It might be wise to simulate the actual marketing programme: price, promotion, and packaging.
6. Choose the name that maximizes the firm's branding and marketing objectives and register the name.

It is often not necessary to come up with a new brand and thus a new name. A new brand is expensive and difficult to introduce and might not succeed or cannibalize existing offerings. A new brand should only be considered if one or more of the following rationales should be present (Aaker, 2004):

- All existing brands have associations incompatible with the offering
- The offering would damage the existing brand name(s)

- A new name is needed to realise the chance to create and own an association
- Only a new name would signal the newness of the offering
- An acquired brand has significant loyalty that would be at risk if a name change were to occur
- A channel conflict requires a separate name
- The business is of sufficient size and longevity to justify inventing a new brand

4.3.4. Branding in the Wine Business

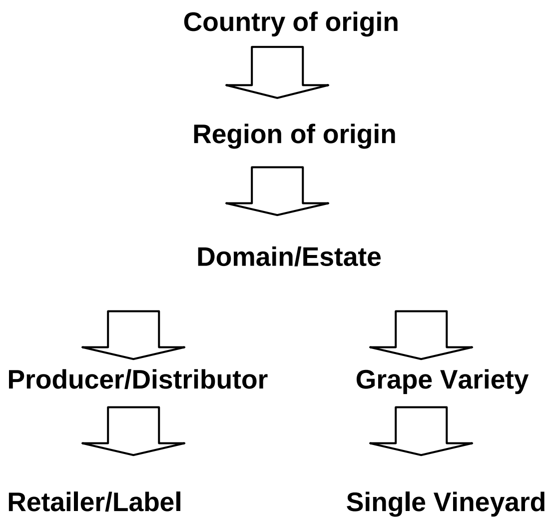
Recently, branding has become a buzz word in the wine business. The importance of branding might be explained by increased competition, as well as consumer confusion, due to world wine oversupply (especially in the popular premium and premium segments). For many consumers in any given supermarket anywhere in the world it is almost impossible to choose between the many wines on display. It is therefore important to invest in a well-known brand name (Visser and de Langen, 2006). Furthermore, more and more wine is being sold through supermarkets and negotiating power of supermarkets is increasing, reinforcing the increased importance of branded wines. This is why wine labels and design play such an important role. The increased importance of brands will likely lead to concentration in the global wine industry, since a larger firm size leads to economies of scale and scope in marketing, distribution and production (Visser and de Langen, 2006). Larger brands have an advantage in the supermarket. A large, well known brand, representing a variety of different wine varieties, takes up a larger amount of shelf space, increasing the chance that a typical consumer would reach for one of these wines. At the same time one might argue that high involvement consumers have a larger consideration set and are willing to pay a higher price if convinced of a wine's quality, thus downplaying the attraction of certain widely available brands, at least for this consumer segment.

Geographic Indicators can be seen as the first element of branding in the wine sector. Since the 17th century it has been commonplace to mention the region of origin on wine bottles. In the 1990s Australian wine producers also realised that style and quality of wine are related to the region of origin and so started using Geographic Indicators as branding elements on their labels (Lockshin and Tustin, 1999). Other important elements are *country of origin*, *appellations,* and *grape varieties*. Country of origin creates *secondary associations.* People associate certain product types with certain countries such as Italian fashion, or

Japanese consumer electronics (Keller, 2002). In the wine business country of origin is often associated with certain price-quality ratios, as we have seen in the previous chapters.

Terheijden (2005) has created a *brand hierarchy* of wine, based on Aaker (1996) and Lockshin and Tuskin (1999):

Figure 4: Brand hierarchy model of Wine



Source: Terheijden (2005)

The top side of the model consists of the largest common denominator, followed by the smaller ones below. The following elements influence consumers' buying behaviour and thus should be part of a wine producer's strategic brand management (Lockshin, 2004):

- *Positioning in Subcategories:* a brand should have the same positioning (including price) across different types of wine (red, white, rosé)
- *The grape variety:* Argentinean Malbec, Chilean Carmenère
- *Origins*: Country, Region, Appellations
- *The Company (Estate) Name*: a certain reputation can lead to brand loyalty
- *Single Vineyard Specification*: a small, specific vineyard is important for a producer's prestige, especially in the *icon* segment.

These elements, combined with *year* and *price,* are called the *Brand Constellation* of wine. The importance of these elements to consumers (and thus the choice of combination of elements) may vary across nations, and certain market segments, such as *low* versus *high involvement* consumers. In general, it is assumed that higher segments warrant higher quality wines, for which country/region of origin and terroir are considered more important. These wines are mostly sold to high involvement consumers. As was mentioned, in the super and ultra premium sectors branded wines still exist, but more expensive wines are more dependent on their quality image than their brand associations (Terheijden, 2005).

Quality and price are therefore often mentioned as the most important elements of wine and country/region origins communicate impressions of this quality and (perceived) value, which explains the importance of developing the right country image. The link between quality perceptions and price provides the core for each region's or country's value proposition. For instance, Chile is well known for its reasonably good quality, low priced wines. Equity is eroded away all too easily, but by basing quality communications on inimitable origins rather than readily procured associations, the value added nature of the wine business can be preserved (Atkinson, 1999). It has also been argued by Atkinson (1999) that trying to use grape varieties and individual winemakers (estates) as points of difference will not work as well. First of all, grape varieties such as chardonnay may trigger purchase decisions, but are easily imitated. Secondly, using an individual brand such as an estate name is difficult as wine production in most regions is piecemeal; meaning that exposure to a named origin (region or country) is more frequent than exposure to individual brands, prompting greater awareness. Furthermore, Orth et al (2005) found that, apart from price and quality, wine region equity consists of five dimensions which could be identified as drivers of consumer preferences: different wine regions signal specific *functional, price, social, emotional* and *environmental* benefits to consumers. Orth et al (2005) also developed a six-stage process for defining a marketing strategy utilising place-based branding:

1. Establish the place's distinctive characteristics
2. Asses the place's competitive position
3. Use lifestyle segmentation of the consumer market
4. Asses and add additional relevant variables
5. Select target segments
6. Communicate selected place benefits to the selected audiences

Tying together all the information on the relationships between wine origin preferences, wine benefits sought by consumers, and consumer lifestyle would provide marketers with a powerful tool to for effectively addressing and persuading consumers (Orth et al, 2005).

Although leveraging Country (or region) of Origin effects is often seen as a rationale for marketing and branding standardisation, these effects can also be seen as a threat to global branding. Brands leveraging their country of origin make use of beliefs (sometimes stereotypes) about those countries. The significance of such beliefs however, may differ widely across nations -and so ultimately might affect purchase decisions negatively- (Van Gelder, 2003).

4.3.5. Branding and Marketing Trends

According to Euromonitor (2008) wine producers marketing wine to specific consumer segments are expected to reap rewards. Indeed, as was mentioned before, Foster et al (2002) found that those Chilean wineries identifying select groups of consumers receive a higher price and this relationship apparently holds regardless of winery size. Interesting global segments are felt to be financially independent women and older baby boomers. The packaging is also considered increasingly important. Apart from screw caps, wineries are now switching to PET bottles and cartons which should appeal to environmentally conscious consumers. As was mentioned before, wineries may also stress the health benefits of their wines. Euromonitor states that healthy lifestyles will be one of the most significant marketing tools at the Wine Industry’s disposal in 2008. Low-alcohol wines, organic/biodynamic wines, and wines containing extra anti-oxidants are expected to create new consumer bases. In order to attract younger consumers, wine labels are expected to become more attractive and attention-grabbing, at least in the premium sectors. In North America in particular, so-called “critter labelling” is becoming very popular (using animals on the front label, for example kangaroos, penguins and crocodiles).

Chilean wineries (and wineries from other countries) are now also trying hard to develop “stories” around their products to differentiate themselves from competitors and target certain consumer segments. Many Chilean wineries stress their history and wine making tradition -often their family business nature or their Indigenous heritage, e.g. Mapuche- while others pursue an image of novelty, consistency, flexibility, using state of the art technology, using new terroirs, producing organic and/or environmentally friendly wine, etc.

4.4 Conclusion

This chapter reviewed a number of generic strategies individual wineries (as well as wine exporting countries) might pursue. By implementing one or a combination of these strategies a winery should be able to create a strategic competitive advantage over competitors. Marketing can be viewed as the implementation of the company’s overall business strategy. The marketing process consists of targeting, segmenting and positioning the company and its brands in such a way to be able to attract consumers. This is done through establishing a good marketing mix; *price, product, place, promotion*. The importance of the STP process is demonstrated by the fact that Chilean wineries identifying select groups of consumers indeed receive a higher price and this relationship apparently holds regardless of winery size. Part of the marketing strategy is the firm's branding strategy. The goal of branding is to create brand equity, which is dependent on brand awareness, brand loyalty, brand associations and perceived quality.

Increased competitive pressures in the World Wine Industry demonstrate the importance of a good business strategy, although many small Chilean wineries do not seem to have a coherent business strategy, perhaps due to a lack of resources. It is argued that most Chilean wineries are mainly focussed on keeping production costs down, although a low-cost strategy alone is not sufficient to increase competitiveness on the export market. Other important factors are an increase in variety and quality of the wines produced, as well as investment in branding. The main ways branding can influence end consumers is through brand name, labels and packaging. It is argued that larger Chilean wineries generally have an advantage over small wineries because of economies of scale in production and presumably because they have more resources available. This translates into lower production costs and the possibility to produce a wider variety of wines, as well as commanding more resources which can be used to invest in branding. However, they need not necessarily have an advantage when it comes to producing higher quality, higher priced, innovative and differentiated offerings.

As has been mentioned before, the Chilean Wine Industry as a whole has rightfully recognised the importance of increasing the quality of the wine produced so as to be able to target higher price segments, where competition is less and margins higher. Quality and price are considered important elements of wine and country/region origins communicate impressions of this quality and (perceived) value, which explains the importance of developing the right country image. Although it is difficult to say exactly what brand elements play a role in what consumer segments buying behaviour, it is clear the level of consumer involvement plays a major part.

5. The Small Chilean Wineries

This final chapter focuses on the small Chilean wineries. The aim is to identify, in a general manner, the main problems facing small Chilean wineries, as well as formulating a general answer to the question of how a well defined country image might positively influence the success of these small wineries on the export market.

To be able to answer this question I draw conclusions from the previous chapters, as well as from the answers given by experts interviewed for this thesis. The complete interviews may be found in the appendixes. The number of experts interviewed for this thesis does not represent a large enough sample to be able to come to any statistically viable conclusions. However, as a background and illustration they do offer some interesting finds combined with the literature reviewed so far. The experts interviewed belong to three small exporting wineries, two mid-sized exporters and one big exporter, at least in terms of export *value* in US$ FOB (January-July 2007). Also, experts belonging to ProChile and Chilevid (the business association of the small export oriented wineries) and a few independent wine experts were asked for their views and opinions.

Table 25: Interviewed Companies Ranked according to Exports US$ FOB Jan-Jul 2007

Company	Cases Exported	US$ FOB	Average Price p case
Montes	444,009	23,882,376	53.79
Aresti	84,980	2,228,868	26.23
J. Bouchon	43,940	1,447,346	32.94
Korta	18,845	415,874	22.07
Alempué	8,258	176,687	21.40
Nogales	710	19, 276	27.15

Source: ProChile (2008)

Although a few generalisations have to be made, we might assume that for the majority of smaller wineries the competitive situation is fairly similar: first of all, we have seen that Chile has a strong competitive position compared to other wine exporting countries, its weak points having to do with its domestic market structure and growth potential. This limited domestic market, together with high domestic market share for the country's top three wineries (in terms of production volume), leaves the majority of smaller wineries with a focus on increasingly higher quality exports.

Furthermore, Chile has a few distinct (natural) advantages and disadvantages considering wine exports, which small exporting wineries can both profit from or have to learn to deal with. Similarly, worldwide trends of oversupply, increased competition, increased bargaining power of importers and increased importance of marketing and branding to simplify consumer buying decisions in the supermarket segments, are treated as a reality by small Chilean wineries. All these factors together form the environment, or playing field that small export-oriented Chilean wineries have to compete in, such as is normally identified according to the *outside-in* view on strategy. The next paragraphs will discuss the main problems and constraints typical small Chilean wineries might encounter, as well as the best ways to deal with these. Also, the role of *country image* on these shall be discussed more specifically.

5.1. Main Problems and Threats

The first major obstacle for small Chilean wine exporters is that many often do not have a coherent business strategy worked out; including vision, mission statement, concrete targets, budgets and action plans. This immediately implies a non-existent or improvised marketing and branding strategy as well. Small wineries, like any businesses competing in dynamic and complex environments, must have a clear understanding of their objectives and the methods for efficiently and effectively attaining them (Olve et al, 2003). Other problems or weaknesses identified were: a lack of capital, a lack of marketing & branding focus, a lack of cooperation among wineries, as well as between the wineries and public organisations, and the difficulty to find the right distributors. Obviously, all these weaknesses and challenges are intertwined with each other. It should be noted that not every small winery has the same problems, nor to the same extent. In the next paragraphs some of these problems shall be discussed together, as they are believed to have a direct influence on each other.

5.1.1. Lack of Capital and Marketing & Branding Focus

Often (although expert opinions are not unanimous in this respect) small wineries are believed to operate with a lack of capital and resources. This is not only the case in Chile however. The wine business in general is still quite fragmented and most small wineries are seriously under-capitalised, and that has all sorts of quality and focus-issues because all of a sudden a winery runs short of funds and can't buy what it needs to generate cash flows (Demediuk, 2003). Some experts feel that this lack of capital is the main reason for the lack of marketing focus; not because small Chilean wineries are not convinced of the necessity to focus more on marketing. That a lack of capital and marketing focus seems to be a problem for small wineries in other countries too may be seen by this quote by Beverland (2000) about small Australian wineries: "*To survive wineries will need to develop strong brands, offer adequate product support, be prepared to move away from cellar door sales and mailing list as means of distribution and form relationships with distributors…All of this requires an increased emphasis on marketing strategy if wineries are to survive*". Another problem facing small wineries without a lot of capital is travel. It is expensive for small wineries to travel extensively and look for new distributors and importers and to develop strong personal relations with them. It is however viewed as very important, as well as being able to speak English, yet another problem among Chilean wineries. Whether or not it's a lack of capital that is predominantly responsible for a lack of marketing focus, it is obvious that for most small wineries it is impossible to directly target the end consumer through elaborate marketing strategies, as marketing costs are too high to position an individual producer. This immediately leads us into the direction of developing a certain form of cooperation, or the development of a *Brand Chile*. Furthermore, a well defined country image would not only be useful to target consumers, but also other agents in the wine business which influence consumer perceptions and buying behaviour, such as wine writers, sommeliers, importers/distributors, etc.

As was also mentioned before, the lack of marketing focus has led wine to become a *push product*. The main problem for the Chilean Wine Industry is selling, not producing the wine; making marketing the key factor. An often heard complaint among experts is that although Chilean wineries are good at producing, they should look at the market first, not at the product. Ideally these processes (marketing and production) should be separated. First one needs to know the needs and wants of the consumer, and then one should produce the wine to supply this demand (and even create *future* demand). In practice, wineries first concentrate on producing the wine, and then try to place it in a certain market. A generic marketing and promotion strategy through an industry wide promotion organisation (ideally with government support) developing a *Brand Chile* would significantly contribute to a more marketing oriented focus of the Chilean wine industry. This is the reason that experts believe that a *Brand Chile* is vital for the wine industry's future. Organisations such as Wines of Chile and ProChile are considered by most experts to be helpful in creating a Chile Image and helping small wineries promote their products on export markets, although there are a few exceptions. A country image would be helpful in various respects. First of all, a well defined quality image for the entire Chilean Wine Industry would facilitate the Industry's struggle to enter higher segments. Furthermore, as we have seen, a well defined country image would benefit wineries competing in all segments; first of all, in the popular premium and premium sectors where the majority of branded wines are to be found. Secondly, in the super and ultra premium sectors wines are more dependent on their quality image than their brand association, which also merits a high quality country or region of origin image. Lastly, a well defined country image to support marketing efforts would arguably be even more important for smaller wineries because of their assumed lack of capital and resources compared to the larger exporting wineries.

Considering branding, experts said it is important to add value to the product; to have a brand name, label and back label that are distinctive and different from that of competitors. As was discussed, a brand name and label are often the only way to directly target the end consumer and create awareness. However, this is more easily said than done, and most experts did not have a clear opinion on how to achieve these goals. Almost every winery hires a professional Chilean design and consultancy company to develop their labels, promo materials and other package design features. An often heard complaint however, is that the choice for a certain name and label is either made by those design companies or by the winery's owners, often resulting in fairly subjective choices. Of the wineries interviewed, only Montes uses foreign (both a European and Asian) design companies, to better connect with consumers there. Under the same logic that one should look at what foreign consumers want and then produce the wine accordingly, it might be a wise option to do the same concerning brands and labels. However, opinions are not unanimous in this respect.

Apart from the brand name and label, innovative packaging enables wineries to add value to their offering. It is also a good way of signalling and reinforcing quality and exclusivity, especially in combination with a high quality country image. Developing innovative labels and packaging need not be very expensive and so should be considered as a very interesting option for small wineries.

In short, a well defined *Brand Chile* signalling high quality would benefit and support any small winery's branding strategy based on signalling high quality.

5.1.2. Lack of Cooperation

A lack of cooperation between Chilean wineries, wine business associations and the Chilean government is often held responsible for the lack of country image. Two explanations are generally offered to explain this lack of cooperation. First of all, Chilean wine producers are said to have a very entrepreneurial attitude and are therefore not as inclined to cooperate as much as their competitors in other wine producing nations. Also, a lack of trust and fear of free-riding are mentioned as impediments to cooperation. Apart from this cultural explanation there is the idea that the Chilean government's attitude is very neo-liberal and focussed on enabling exports. It is believed that the Chilean government is unwilling to directly support or subsidize the wine industry. Also, the Wine sector only accounts for around 1.5% of total Chilean exports, perhaps further diminishing the willingness of the government to get directly involved in the business. However, as was shown the government has at least established a few important organisations to support the wine business, such as ProChile. For instance, ProChile's wine fairs and testing offer producers a good possibility to gain medals which should signal quality and induce consumers to buy the producer's wine, but it also offers the winery an opportunity to benchmark, by comparing its wines to those offered by the competition. Furthermore it offers opportunities to meet and develop good relations with wine importers, journalists, connoisseurs, sommeliers and other agents. Especially in the case of smaller wineries which might not have the capital to travel extensively ProChile offers a lot of opportunities. Another advantage of ProChile is that it is the national export promotion agency, so developing a country image through, or with support of, ProChile (Such as the: *Chile, All Ways Surprising* campaign) would benefit all export products and possibly induce the government to commit itself more and spend more funds. As was mentioned before, a country image beneficial to all export products could generate positive externalities for society at large and might therefore be considered a collective good.

Among the experts interviewed (excluding the ProChile officials) there is no consensus on whether or not ProChile is helpful in promoting their exports. Some feel ProChile is too demanding and constraining and perceive wine fairs as putting a number of competitors in a room, competing against and undercutting each other trying to get the attention of importers and distributors. Other experts see ProChile in a more positive light.

Cooperation between the business associations ChileVid and Viñas de Chile, leading to the *Wines of Chile* association and its generic promotion campaign, is seen as a positive and long awaited development which should benefit both smaller and larger Chilean wineries.

Apart from these government and business organisations it was also argued that it might be wise for smaller Chilean wineries to start cooperating among themselves. According to the experts, cooperation between wineries in terms of marketing or branding is not considered an option, although cooperation in R&D and selling together is. Selling together ensures producers have a better position in negotiations with importers, distributors and supermarkets, as it enables them to offer a wider variety of wines. A group of producers pooling resources to find a common sales manager that exports the wines in their name would also enable the wineries to focus only on production. However, it is strongly advised that a group of producers which want to cooperate in this manner produce the same level of high quality wines, to be able to present the importer/consumer with a consistent offering. Another advice given by the experts is to enter into a joint-venture with a foreign winery, which would offer small Chilean wineries an opportunity to profit from the foreign company's marketing- or branding skills, or perhaps its distribution channels, again leaving the winery with only the production side to focus on.

As was previously mentioned, the importance of cooperation for high quality wine exports was noted by Foster et al (2002): *The orientation towards a high quality product at a competitive price is a priority of all Chilean wine companies; it does not matter if we are talking about small, medium or large wineries. Industry coordination is therefore critical to positioning these concepts in international markets*. Furthermore, cooperation makes even more economic sense for small wineries as was just explained.

5.1.3. Finding the right Distributor

Distributors have an important role to play in promoting the wine of their producers. The distributors hold the market power and have better local consumer knowledge, and often also the means to target these consumers. In most cases, small wineries cannot target the end consumers directly. Thus, finding the right distributor is also considered as crucial to the future success of the Chilean wine business. Finding the right distributor is difficult however, given the current situation in which there are many (small and large) wineries, whereas there has been a process of consolidation when it comes to distributors and importers.

According to the experts there are essentially two options to find a good distributor: either a large distributor or a small distributor equal in size to the winery itself. The advantage of a large distributor is that they would ideally offer the winery marketing and branding expertise, consumer knowledge, as well as an established distribution channel, again enabling the winery to focus on what it knows best: producing the wine. The problem with large distributors is that they are often not interested in smaller wineries, as they prefer to do business with larger wineries that offer a wider variety of wines and are able to offer larger quantities. Also, even if a large distributor is interested in a small winery, it is often to fill in a small gap in its portfolio, still leaving the smaller winery with supplying a small market niche. Also, it has been argued by some that large distributors do not take smaller wineries seriously and hold all the negotiating power, leading to lower prices obtained by the producers. To counter-act this behaviour on the part of large distributors and importers, small wineries are advised to cooperate in selling their wine, as we have just seen in the previous paragraph. Smaller importers, according to the experts, are assumed to be more interested in the offerings of smaller wineries and have their best interest at heart. Consequently, a mutually beneficial relationship is more easily developed with a smaller importer than a large importer. This would also imply smaller distributors would ideally give more and more honest feedback about the winery's brand name, label and the quality of the wine. However, smaller distributors might lack a good distribution channel, as well as the marketing and branding skills to reach the end consumer in the right way. It seems that finding the right distributor is not easy and should depend on the winery's overall marketing objectives and so ultimately its business strategy.

In any case, establishing and maintaining good personal relationships is considered very important, not only with the importers/distributors, but also with wine journalists (good P.R.) and restaurant owners; people who are often more capable of reaching and influencing the end consumer than the wineries are. These people offer a smaller winery a way (sometimes the only way) to advertise and ultimately create awareness and influence consumer buying decisions. Targeting these agents is called a promotional push strategy, as was discussed in the theoretical chapter. The goal of developing good relations with distributors is that it should make selling the winery' s products more enjoyable than selling other wines the distributor might have in its portfolio. This is also contingent on the quality of the wine of course. So a critical success factor which underpins the distribution strategy is an ability to develop relationships that eclipse those maintained by competitors. Financial or material inducements (dinners etc) are not the differentiators here. To motivate distributor representatives takes levels of time, energy and resources that are difficult but necessary to divert from the more mechanistic tasks of winemaking (Demediuk, 2003).

5.2. Targeting Higher Price Segments

Both the studied literature as well as the general consensus among the experts interviewed points into the direction of increasing quality and entering higher price segments as the most sensible general strategy. Indeed, it is clear that if the Chilean Wine Industry wants to avoid getting stuck in the "supermarket segments" where competition is fierce, market power lies in the hands of large distributors and supermarket chains, and prices are expected to fall, an effort has to be made to enter higher, more promising price segments. It seems very unlikely that global supply will decline in the next few years and consumer demand has also shifted towards higher price segments, so it is in the longer term strategic interest of the entire Chilean Wine Industry to target higher price segments. As was demonstrated, the Chilean wine industry has already begun a process of continuously increasing the quality of wine exported. Chile's competitive advantages, especially its unique terroir and natural resources, enable the production of a wide variety of wines of the highest quality. All of the above holds true for both small and large exporting wineries. However, as was said before, it is easier and cheaper for smaller wineries to increase the quality of their wines than it is to invest in significantly increasing production capacity. Indeed, the smaller wineries are capable of withstanding competition from the big three mainly based on product differentiation, adding value to both their wines and their brands, so they can focus mainly on the export market with high quality wines. It might be concluded therefore that this strategy is even more advised to small exporters than larger wineries. Although we have assumed here that it is “possible” to increase quality and prices for all small Chilean wineries, this does rest on a few key factors (Demediuk, 2003): the selection of the grapes, the quality and professionalism of the wine-making team, planned access to capital for the winery to actually be able to buy the right oak and do all the things it needs to do to produce the wine; a planned market for the wines, deep relationships with distribution agents, and feedback/benchmarking. All these factors drive the ultimate quality of the wine. The quality of the wine in turn holds consequences for the marketing strategy. Marketing, as a critical success factor, can only work in a sustainable way where wines represent outstanding value for money (Demediuk, 2003). In other words, certain marketing, promotion and distribution strategies are only possible if the quality of the wine enables these.

However, as was discussed before, increasing quality and price is a very difficult process, especially for the same smaller wineries which presumably often lack a variety of skills and capital. One expert pointed out that *within* the higher price, higher quality segment however, it might become an advantage again being seen as the cheaper alternative (good value for money), as long as the quality of the Chilean offerings is seen to be equal or even better than those of competitors. But the difficulty is how to get to that higher segment. Currently Chilean wine is still not perceived as having competitive quality at all price points., as the only country image Chile might be considered to have is that of a low-cost, reasonable quality wine producer. Consumer perceptions of Chilean wine as good and affordable, perhaps even cheap, need to change. This is exactly where a well defined Country Image would come in handy again.

In any case, to become more successful small Chilean wineries who want to target higher price segments are advised to increase the quality and packaging of their wine, after which they should concentrate on finding the right distribution and devise a promotion budget, according to one expert.

5.3. Conclusion

Small export oriented Chilean wineries take the current situation and trends in the World Wine Industry as a given. These include: increased producer competition, a worldwide oversupply of wine, increased bargaining power of importers and increased importance of marketing and branding to simplify consumer buying decisions, especially in the supermarket segments.

Similarly, the Chilean situation is also considered fairly similar for most small wineries: Chile has a strong competitive advantage position on the world export market; especially its natural advantages and low costs stand out. Chile's main weakness is considered to be the domestic market, making exports the preferred option for small wineries.

Both the international and national environments thus push small wineries into focussing on higher quality (and higher price) exports, which is considered to be the most attractive market segment. In general, small Chilean wineries have the technological know-how and skills to produce a variety of high quality, more expensive wines which would appeal to increasingly sophisticated and international consumers, willing to pay a premium. However, a few problems and constraints facing small Chilean wineries have been identified. First of all, they often lack a clear, coherent business strategy. Secondly, a lack of capital, a lack of marketing & branding focus, and a lack of cooperation among wineries, as well as between the wineries and public organisations are considered the most important threats to success on the export market. Lastly, finding the right distributors is also difficult. These weaknesses and threats are interrelated and do not apply in the same way to all wineries.

The main problem for Chilean wineries is the lack of country image. The only image that exists is that of Chile as a low-cost, reasonable quality wine producer, which is not considered the right image for an industry that wants to upgrade and target higher price segments by producing high quality wines. The Chilean wine industry (and ideally other export sectors) as a whole would benefit from a well defined country image signalling high quality. It was argued that this holds even more true for small Chilean wineries which supposedly lack the resources to devise elaborate marketing strategies, not only targeted at end consumers, but also at other agents.

In conclusion, to become more successful small Chilean wineries need to devise clear business strategies, including clear marketing and branding strategies. Wineries should upgrade the quality and packaging of their wine, after which they should concentrate on finding the right distribution and devise a promotion budget. In general, it is advised to cooperate, either by entering in joint-ventures with foreign wineries, or by pooling resources and develop a way to sell together. The right distribution channel is considered vital, although opinions differ on what kind of distributor, small or large. This presumably depends on the wishes and goals of the specific winery involved. Developing personal relationships with agents such as wine writers, sommeliers, distributors, etc, are considered of the utmost importance for promotion especially for small wineries in higher price segments.

6. Conclusion

The central question of this thesis was:

What are the effects of country image on the performance of smaller Chilean Wineries and what strategies could these wineries pursue in order to become more successful on the export market?

This thesis started with an overview of the increasingly globalised World Wine industry and the position of Chile. The world wine market has seen an impressive increase in production mainly due to the ascendancy of the New World. Worldwide consumption has not risen accordingly, leading to an oversupply of wine; particularly in the (popular) premium segment, the so-called supermarket segment. This has led to an increase in competition between producers and consumer confusion, which has meant an increased emphasis on marketing and branding. Another recent trend is the increase in market power due to consolidation among distributors, while the wine industry is still highly fragmented. Exports have become increasingly important in the world wine industry, as traditional (Old World) wine producing countries, who traditionally also have always been the major consumer nations, have seen a significant decrease in consumption. Demand in other, non-wine producing counties, has risen though. The most attractive export market segment is said to be the higher quality, higher price segments. First of all, consumers are now willing to pay more for good quality wine, and secondly competition is not as fierce as in the lower segments, leading to higher profit margins.

Given the international environment the Chilean wine industry seems well positioned for the future. Chile has shown some impressive growth rates concerning production, planted acreage, and exports. Only local consumption has not shown such positive figures. The Chilean wine industry has a strong competitive position compared to most other exporting nations. Its major advantages are to be found primarily in lower production costs and perfect terrain and climate to produce high quality wines. There is a general consensus that increasing the quality of wines produced would enable Chilean wineries, both large and small, to target higher price segments, a strategy already identified and actively pursued by many. However, individual wineries in general lack the ability and resources to invest in and establish elaborate marketing and branding strategies. A form of cooperation among wineries is therefore considered very important. The major disadvantage of the industry is a lack of country image. Developing a country image to support exports by organisations such as Wines of Chile and ProChile is seen as crucial, although experts are not unanimous in their opinions of how effective these organisations have been so far. It has been argued that Chile at present lacks a well defined country image which could be beneficial for all export products. The current image of Chile is that of a low-cost wine producer, making it difficult for individual wineries to target higher price/quality segments.

The third chapter dealt with the importance of strategy, marketing and branding for the wine industry and small Chilean wineries especially. Increased competitive pressures in the World Wine Industry demonstrate the importance of a good business strategy. It was argued that most Chilean wineries are mainly focussed on keeping production costs down, although a low-cost strategy alone is not sufficient to increase competitiveness on the export market. Other important factors are an increase in variety and quality of the wines produced, as well as investment in branding. The main ways branding can influence consumers is through brand name, labels and packaging. Quality and price are considered important brand elements of wine and country of origin images communicate impressions of quality and (perceived) value, which explains the importance of developing the right country image. It was established that small Chilean wineries generally have the know-how and skills to produce higher quality wines necessary to enter the higher price segments. Although it seems that firm size is not a decisive factor for success in the (higher segment) export market it is generally assumed that large firms have an advantage when it comes to economies of scale, more resources available for marketing and branding, and less difficulty in finding large distributors and importers. It is therefore concluded that smaller wineries are generally considered to be even more dependent on industry cooperation and the development of a beneficial country image.

Indeed, the final chapter of this thesis focused on small wineries. As was mentioned, the main threats these wineries face are: a lack of business strategy, capital, branding & marketing focus and cooperation. Also the current situation makes it difficult to find the right distributors. It was concluded that small wineries should develop smart and coherent strategies, including marketing and branding strategies. Wineries are advised to upgrade the quality and packaging of their wine, after which they should concentrate on finding the right distribution and devise a promotion budget. Furthermore, small wineries would be wise to cooperate, either by entering in joint-ventures with foreign wineries, or by pooling resources and develop a way to sell together. It is also considered important to find the right distributors and develop personal relationships with distributors and other important agents which might influence consumer buying behaviour. A well defined country image signalling high quality would facilitate entering higher segments by influencing consumer perceptions of Chilean wine being low-priced. A *Brand Chile* would also take at least part of the necessity to focus more on marketing away, which is especially attractive for small wineries that might lack the appropriate resources.

Appendix 1: Interviews

Interview:

Jimena Castillo Sánchez. ***Representative of ProChile in the Netherlands***

Place and Date: ***The Hague, September 5, 2007***

Language: ***English***

Chilean producers focus on the product, not on the market, on the consumer. They have fixed ideas about the product, label and wine. Enologists fall in love with their own wine. Now markets have their own voice and customers are becoming pickier every day. One example is the bad reception of Chilean wines in Spain. Chilean wines have too much oak for Spanish taste. So we should prepare wines for the Spanish market, and not for the Chilean market. Chili has this problem with almost every export product except perhaps fresh fruit.

The main problem is lack of innovation in Chile, both product and marketing innovation. You have to adapt the product to the new consumers. A different brand/price segment should mean a different wine too, because oenologists and connoisseurs can taste if different brands are actually the same wine. It's different if you sell the same wine using different brands in different markets of course. But if you try this in the same market it could be damaging for the company's reputation.

The problem with developing a Brand Chile (in Holland) lies in Chile. So far, Wines of Chile has decided not to market Brand Chile to the Netherlands. The reason is ProChile puts up half the money and the private sector the other half. Wines of Chile is reluctant to participate with promotion (materials). For Pro Chile the fresh fruit sector is easier to work with because the fresh fruit association is much more aware of market demands and the exporters (not the same as producers, such as is the case in the wine business) know their business. Now that the two major wine associations merged to Wines of Chile, there is hope they might come to realize they need to do more about generic promotion (through Pro Chile). Pro Chile has one major wine tasting in Holland per year, directed to importers, not consumers. Apart from Chilean producers, there are mainly importers, who also bring their own wines to show. So it's more of a retail thing. Pro Chile just pays for a stand and is the facilitator of the fair. The importers have their own stands. Pro Chile would like to organize more tastings, or do more with wine. Such as Chilean wines + Dutch cheese (a project 8 years ago, ProChile + Campina, big success). You have to convince people to invest more in marketing/promotion. Producers are reluctant: they haven't got people or money. But you have to be creative. Producers might invest in importers to do some research, but producers are very reluctant.

Chilean wines have been successful in The Netherlands because of:

1. price quality ratio
2. Dutch importers have made an enormous effort to import Chilean wines in the past.

Chilean wines need an export organization. Producers now tend to do producing, selling and distribution themselves. Logistics is becoming an important marketing tool as well. Chilean wines need marketing, they have lost market share to Australia and New Zealand. Producers and Pro Chile for that matter must do something different, perhaps not just one tasting a year.

Chilean producers should focus better. Premium wine means premium packaging and labeling. You need European (or even Dutch, as we are different from Spain) consumer research for this, not Chilean design bureaus. Having good wine is not enough, everybody has good wine nowadays. Chileans have preconceptions about Europe.

A good example of a small company without own grapes is Picante. These are marketing people. They hired a UK oenologist, who tasted different wines and said which ones were good for the UK market. I think it is necessary to make more personalized wines. In premium/gourmet wines, packaging is paramount. It is important to see wine not just as a product, but as a story. Chile is a far away country, the Andes, pacific ocean, desert, Antarctica. We are unique, and have the best climate for wine. The problem is that (Dutch) consumers are not aware of Chile at all. One problem for instance is that people think Chile is tropical as it lies south. Pro Chile therefore stresses Andes Mountains with Snow. Chile is a phytosanitary paradise, wine is fun and healthy. These things are provocative for Yuppies, who are very concerned with the environment and social issues as well. Yuppies want to have fun, be healthy and cool (Chile is exotic) and drink without a guilty conscience. Chilean premiums are always good, as they don’t have good or bad years, always the same: consistency in quality. The water of the Andes, the good environment, natural sun, etc should be stressed in marketing.

Another segment option would be to sell to older people, who are more educated and perhaps more willing to pay a higher price for Premium wines. They are looking for new wines. The same holds for Yuppies: wine is trendy, they want to learn, be educated, and go to tastings. The little cat of Gato Negro adds that little something extra. An option is to use indigenous (Mapuche) designs, which are nice and clean. There are some Chilean wines already doing this successfully. I think Mapuche and Indians in general are more appealing in Holland. That’s why you have to make wine into a story. Perhaps you can add something with a cord around the neck of the bottle for instance, or perhaps a (wooden) box. People who buy premium want something different, something extra. A wooden box for instance makes it look more premium and you can take it as a gift (and command a premium price as well). This means you could tackle different channels, such as enterprises making gift boxes.

Marketing directly to consumers is expensive however, so it might be better to aim at retail, buyers, and category managers. Perhaps even cooperate with them (and organizations such as ProChile). It’s important to create an atmosphere for your clients. Apart from tastings (with presentations on Chile, special guests such as Chilean ambassador, etc), Pro Chile is able to help with posters, cards, promo materials. Growing in the premium segment means investing in a premium channel through: creating a story, and making use of brochures and little add-ons in packaging. You drink the story, the atmosphere, not just the wine.

It is important to realize that nowadays everybody knows all the wines of all the different countries, including the New World. So you have to differentiate through attributes: a country far away, a phytosanitary island, a story about Indians. Better to focus on one of the attributes as principal, the rest you can try and take along. Focusing on creating an organic image is difficult. You’d need organic channels.

Interview:

Pedro Hiribarren. ***General Manager of Viña J. Bouchon and Director of ChileVid.***

Place and Date: ***Santiago, October 3, 2007.***

Language: ***Spanish***

ChileVid is a business association which started out with about 20-something wineries and now has around 50 members. Now ChileVid is separated into two parts: the commercial department, to promote the wines, and a R&D department. It was created to give more weight to the smaller wineries in the local market, which has always been dominated by the larger companies who were organized in *Viñas de Chile*. Last year the two organizations merged to form *Wines of Chile*, or *Vinos de Chile*. I am director of *ChileVid*, but not of *Wines of Chile*. It wasn't good that the two were separated. There used to be a lot of communication problems on a national level, with *ProChile*, with all the official organizations. On the one hand official government organizations have always favoured the smaller wineries, making *ChileVid* popular on a government level. On the other hand, the larger wineries have been very important to the industry's success; concerning image, country image, etc.

What are the most important advantages of Chile on the Export Market?

We started out from a position where we weren't successful at all (the end of the 80s, beginning of the 90s) but then it became relatively easy to export Chilean wines. The main reason for this initial export success was the great price-quality ratio of Chilean wines. Secondly, the natural conditions we have in Chile are excellent to produce wine and production costs are low. At first growth was good, but problems started when more and more wineries started up.

What are the main differences between Chile and other New World Producers, such as Australia?

Both countries have positioned themselves in different niches. First, Australia has different production costs and second, nowadays they have specialized in certain types of wine. I think we do not have a distinct advantage over Australia and others, apart from perhaps costs and distance from certain markets. There is space for all of us: Australia, New Zealand, Chile and Argentina. Although we are competitors, we will all have our chance.

What are the main disadvantages for Chile?
Above all, the increase in competition and the reduction of worldwide consumption levels. We always speak about Australia, New Zealand, South-Africa, etc, but nowadays they produce wine in Peru, Bolivia, Uruguay, Paraguay, Eastern Europe, everywhere. So we are in a difficult position, it is hard to find importers. And one needs an enormous amount of capital to be able to achieve a concept of marketing. This is the main problems for smaller exporters, such as ourselves at J. Bouchon, and Alempué. Resources are limited and the investment needed is very costly.

Is this increased competition between producers and increased market power of importers going to lead to lower average prices for the wineries?
On the contrary! Producers need to position themselves in a higher segment, to obtain *higher* average prices. 12 bottle boxes for US$14 make no sense anymore. First of all, because of higher fixed costs. And secondly, because everybody else tries to sell as cheaply as possible…in Bulgaria, the Ukraine, wherever you want. Chilean wineries need to enter higher price segments with better quality wines. Let’s hope this will work, the big problem is how to sell the wines, not to increase the quality.

So is it fair to say the Chilean wine industry is focused more on production than on marketing?
I think so, but not because Chilean wineries do not understand the necessity of marketing and selling, but because there is a lack of capital.

And will marketing and branding become ever more important because of this increased competition?
Of course. The most important assignment for our new organization (*Vinos de Chile*) is to invent and promote Chile’s *Country Image*. No doubt.

What should be the focus of exporting wineries?
More than anything else: look for new markets. It is very hard to increase prices in markets where you are already established; where your wine is already on restaurant menus, etc. What new markets depends very much on the wineries themselves, but in the case of J. Bouchon, we feel we need to expand in Asia above all: Japan, China, and India. Also, other countries which aren’t yet consuming Chilean wine, such as Vietnam. We are also active in Russia.

What do you envision for the future of the Chilean wine industry? Acquisitions; (foreign) investment, etc?
Acquisitions yes. The entry of international wine companies perhaps, but not a lot. There's always new companies starting up and others leaving. We won't see any "super-companies". If bigger companies will appear, it will be because of organic growth, or because of one Chilean company buying another. Considering investment in technology, I think there will mainly be investment in machinery that has an effect on the winery's costs. There won't be a lot of mechanization in the vineyard. And technology levels are already high in the bodegas. I don't see it as a problem that most machinery is imported, the same holds for most other wine producing nations.

What about branding? Is the development of a Brand Chile really that important? What is Chile's current image abroad?
Yes, it is very important. Look at how Argentina has been positioning its wines. Their wines are constantly related to Patagonia, meat, tango, football….it's a country image. We do not have symbols such as the Australian Kangaroo. This is the challenge: we have to find one. *Wines of Chile* is trying to develop a country image for Chile, but the ultimate goal is that we develop a global country image, not just benefiting the wine sector, but every export product we have, with government support. And not only for current export products, but for future products too, such as herbs, parsley, oregano, whatever you can think of, the image needs to be there to profit from. *Wines of Chile's* been successful in the UK, but less so in the US. We have recently begun targeting the German market.

But there is a sort of image: Chile as a cheap, yet good quality wine producer. Is this image still an advantage if wineries should try and target higher price segments?
I think it is still an advantage to be known as a "just as good, yet cheaper alternative" *within* a higher segment. The trick is to get to the higher segment without people noticing it. You can do this by good packaging, or by good service. The key is to add value to your product offering. However, the majority of Chilean wineries are still operating in segments much lower than the super and ultra premium sectors.

What marketing and promotion strategies are most popular among the smaller exporting wineries in Chile?
Principally, to make use of the promotional campaigns organized by *ProChile*. Most wineries start exporting through these programmes.

Why don't smaller companies work together more?

You can invest in marketing, but it's not easily quantifiable. There's often no direct relation visible between a certain increase in marketing spending and increase in revenues. So there is a certain level of cooperation between companies in research and development of technology, but not considering marketing. Secondly, I feel that there is cooperation between wineries, but perhaps on another level…not on a strategic or political level. For instance, wineries often save costs by sharing a certain booth at a wine fair or expo.

What are the marketing trends? What will we see in the near future?

First of all, we need to stress the Chilean nature of the carmenère grape, such as the Argentinean malbec or South-African pinotage. And in the future I believe Chile will be famous for its excellent red wine blends. We won a gold medal for our Syrah/Carmenère blend recently; but we didn't win a medal for our carmenère which was used as the basis for the carmenère/syrah blend. I feel organic wine is also interesting, but I'm not convinced that people are willing to pay more for wine because it's organic. People look upon organic wine producers positively, but this doesn't mean that you will be able to sell your wine for a higher price. But I'm speaking about today; it might change in the future.

As a director of ChileVid, what would you advise smaller Chilean wineries?

The only thing that we can control at this moment are our costs, and for the rest I'd urge everybody to take advantage of the opportunities offered by all the different expos, wine testing contests etc. If you go and travel to places such as India and Japan all by yourself and on your own account, you'll end up taking a tourist trip.

What are J. Bouchon's marketing and branding strategies?

The truth is we also do not have the resources to invest heavily in marketing of any type. So, you have to start from there. We started exporting to various countries through very small importers. We try to develop very close relations with them. We try to serve them the best we can, we invite them over, we show them around etc. This strategy has served us well in the past and we are doing well in countries such as Russia, Germany and Holland. We can't reach the end consumer ourselves, because of our company structure. We cannot devise distinct individual marketing and promotion campaigns in every market, aimed at the final consumers. This is too expensive. Some larger companies, such as Concha y Toro run TV commercials in various countries in Europe and on international TV channels such as CNN. But this is an exception.

Interview:

Pedro Grand. *co-owner of Viña Montes and owner of Viña Nogales*

Luis Simian. *Chilean winemaker in Australia*

Place and Date: *Curicó, October 4, 2007*

Language: *Spanish*

Pedro Grand (P.G.): Montes started out with 4 founders: Douglas Murray, 100% salesman, the marketing brain. Aurelio Montes, the winemaker. Me, in the bodega and a fourth associate who works as a consultant. A big problem for a lot of Chilean wineries has been over-investment, resulting in debt. Montes started out without investing, except in bottles, corks and grapes. The infrastructure was already there. In this business you have to start small. The challenge for small wineries is a lack of capital; you need to travel to find importers. Without a minimum level of background capital it is difficult. Another issue is language: the English language is important, but not a lot of people in Chile are able to speak English. Not only to enter the US, UK and other Western markets, but also countries such as China, Japan and Russia. It is difficult to do business in Russia; you need to have certain capacities that small producers often lack.

If I'd have to give a solution to small wineries, I'd tell them to cooperate with foreigners, through joint-ventures or other means. The only way to start exporting is to mix with foreigners. In Chile, a lot of managers or owners are trying to do everything, but you should focus on the things you are good at. We have a saying: *no se puede chutear el corner y cabezear el gol. (You cannot take the corner and head the ball at the same time).*

What are Chile's strengths compared to other wine exporting nations?

It depends on the wineries, but in general we offer an attractive relation between the price and quality of our wines. Furthermore, Chile is like an island, very sheltered, so phylloxera and pest free. Our climate and terroir are perfect, we have a paradise here. Sunlight, humidity, soil quality, wind, irrigation possibilities, it's all perfect here. That's why Miguel Torres came to Chile. Since around five years ago new terroirs have been discovered, new valleys, where a lot of good and different wines are now being produced: valle de Leida, Casablanca, etc. There are some interesting valleys for Syrah: Colchagua, Santa Cruz, Apalta; and some really good Cabernet zones.

A second advantage is that in general Chileans are very serious and honest. That's appreciated abroad. For importers it is important that they receive exactly what they expect from their producers. Trust is an important factor in this business.

Luis Simian (L.S.): Chile is the least corrupt country in Latin America and this is a well known fact among people abroad.

What are the main disadvantages that Chile faces?

P.G. The distance. We are far away from all major markets. To send wine to Asia you need to cross the entire Pacific. To send wine to Europe you need to go through the Panama Canal and then over the entire Atlantic. The US is the closest market. Even Brazil is further away because everything has to go by road. That's an expensive trip because you have to go through Argentina. You have to bribe people there to be able to pass. There's a lot of corruption.

Is the Chilean Wine Industry more fragmented than in other major exporting nations? Is there a lack of cooperation?

P.G. In countries such as New Zealand, Australia and France they do have some fine research institutes that we do not have.

L.S. In Australia there's a Wine Conference every year. The government has a system of tax cuts to help producers. R&D spending is exempt from taxes, so every winery has an R&D department. Furthermore, the findings are shared among producers at the wine conference. Also, universities tour bodegas to learn from producers and vice versa, and there's another research centre, independent from the universities. Because of this we have already reached a lot of goals set out in Australia's programme (*Australia 2025)* in the third year, which were envisioned for the 15th year of the programme! There's also much more cooperation concerning marketing. There are no secrets between producers and the government has helped to create a country image. First as a country; and then as a wine and tourist country. Tourism is a very serious business in Australia, which is not the case in Chile.

Why does this not exist in Chile?

L.S. It does, but not on the same scale.

P.G. First of all, in countries such as Argentina and Australia, the government invests a lot of money to promote the export of wine. In Chile this amount is nothing compared to those countries.

L.S. Australia has wine fairs in London, Hamburg and various cities in the US.

P.G. Chile is only known for Zamorano or Pinochet abroad. There are no other parameters or symbols. Even though we have Antarctica, the Atacama Desert, the Andes mountains, the perfect climate for wine, etc. We don't have the kangaroo or the tango.

L.S. We do however have a free market spirit. We have the most free-trade agreements in the world, although there are only 16 million Chileans.
P.G. Argentineans send dancers to perform spectacular tango shows at wine fairs, it's magnificent. What can we do? Send a pair of Chileans to dance the *Cueca*? The *Cueca* is not sensual or passionate; on the contrary, it's a dance depicting a woman resisting being conquered by a man. The Tango is the exact opposite. I'm afraid of Argentina. There's a lot of potential there.

Do you fear Argentina more than countries such as Australia, New-Zealand and South-Africa?
P.G. No, Australia will always be the biggest new world exporter, because they speak English which is important in the biggest market in the world: the UK. The same holds for the other countries you mentioned. Even Argentina has an advantage over Chile in this respect. For years, it was the most Anglophile country in South America. Everything was either owned by Britain or people wanted to copy Britain.

What are the main industry-trends concerning production and consumption?
L.S. In Australia, production is going down. So I imagine that prices of Australian wine will go up. The same goes for New Zealand.
P.G. Looking at Chile, consumption has gone down dramatically. Nowadays we either drink good wines or we drink beer. We need to keep increasing the quality of our wine. Exploring all these new valleys is part of this quality increasing process.

In this respect, is the fame that Chilean wines have (inexpensive, good quality) still an advantage?
P.G. The best advantage there is. The problem of Chile is that we have never formed a cartel, wineries have never cooperated. So importers would go from one Chilean producer's stand to the next and insist on a lower price. At Montes we have never played this game. We have a different way of seeing things. A producer who perhaps doesn't have the same prestige or name as Montes might lower his price to sell his stock. But this fame, this prestige is something you have to create yourself as a producer. In everything that we produce and sell, we can't comply with all the demand, there's just not enough supply so we don't need to sell our stock for a low price. We have never had to make cheap wines to enter a market. Who wants to buy our wines can buy them, if they don't want to then they don't. But the wines are out there. We also don't advertise on TV, that's what all the big companies do. We have carefully created our name; we have a different way of promoting ourselves, a different way of entering markets.

Of course, we are only able to do this because of the quality of our product. Nowadays, I'd advise new entrants in the wine business to make only high quality wines. If not, your strategy should be completely different. If our wines wouldn't be of the highest quality we'd have to face brutal competition. It's a different sector. There's so much on offer in the supermarkets nowadays. I believe in occasion-based segmentation. People who want to impress their guests will pay more for a good quality wine. Another problem in lowering your price: people are going to think: wow, that's cheap, it must be bad wine.

What about branding? What are the most important branding decisions and challenges?

P.G. The label and back label obviously. But also the package; the box. A big problem of Chilean wineries is that they often use somebody from their family who studied design or something to develop a label. But who should the label appeal to? Where the wine is going to be exhibited! In Tokyo, London, New York! So we at Montes hired two professional designers, one in Europe and one in Asia. Another thing is the taste of the wine. It doesn't really matter if I like the wine, I'm just the producer. I have to produce wines that my customers like to drink! Countries such as Australia have developed a certain wine style, with certain well-liked characteristics; also, they have a certain price that people are willing to pay. The consumer respects this and likes the wine. For Chilean producers who are just starting up it is hard to impose a certain wine style. They have to adapt to those who are already producing a certain type of wine.

L.S. Yes, but there's another side to this story. Sometimes you have to educate the consumer. You say you have to make wine that the people like. But in countries such as the US and Australia there weren't a lot of wine consumers! In England it's different, they didn't know how to eat, how to drink, etc. But they learned and they learned a lot. They never produced wine, although now they do, but I think Britons now know more about wine than the French and Italians together. Chile is in between these two types of countries. We have been producing wine for a very long time, but when the modern wines were introduced, nobody liked them. Chilean wine was very bad. People would get headaches from really badly produced white wines. Nowadays, there are still Chilean consumers who believe every white wine will give you a headache and who refuse to buy white wine (even though we are talking about decades ago). Chilean education started when Torres entered the Chilean market.

You might view the Chilean wine industry in two parts: before and after Pinochet. Pinochet enabled exports, and the import of stainless-steel machinery, French oak, etc. The first to take advantage was Miguel Torres, with his stainless steel tanks and cooling machinery. He introduced a new type of wine. This was only possible because our country had changed, the laws had been changed.

Interview

Maria de los Angeles Arraztio. *ProChile, representing Wines*

Place and Date: *Talca, October 18, 2007*

Language: *Spanish*

The way *ProChile* helps wineries with their exports depends on their size. For small wineries we have the PIAC programme: *Programa Internacional de la Agricultura Campesina*. We act as a consultancy agency really. And we co-finance consultant fees. We can also assist small wineries to visit international wine fairs. For the mid-sized wineries we organize *Muestras y Catas*, or wine showing and tasting fairs in different countries around the world.

Do you cooperate with Vinos de Chile?

Vinos de Chile doesn't do muestras y catas, they have other activities. Concerning country image you'd suspect that both organizations would coordinate their efforts. Both organizations at least try to promote Chile. We promote our country image through Muestra y Cata. Wines of Chile are a private organization, but also receive government funding to organize their activities, so they have to promote Chile's country image as well. For wineries it is cheaper to sign up for our Muestra y Cata than to participate in Wines of Chile. Although Muestra y Cata is for mid-sized wineries, we sometimes let smaller wineries join. The smaller wineries that are able to participate in muestra y cata are also supported a bit extra; for instance, we might pay for their plane tickets or finance the shipment of their wine samples. We don't do this for the mid-sized wineries. These smaller wineries are only allowed one Muestra y Cata per year though. And we only chose the ones who have good wines, a quality product, good infrastructure etc.

In the same way we organize these Muestras y Catas, we also organize international fairs. Here the government also helps: Chile has a stand in these international fairs. Within this stand we unite all the Chilean companies and/or wineries that enlisted and paid. This is cheaper than when they all have to pay for there own stand.

In both instances, Muestra y Cata and International Fairs, ProChile invites potential clients such as importers, which we believe are the ones that fit the profile and should be interesting to the Chilean companies/wineries. We are the middleman between the buyers and sellers. Everything ProChile does has to do with export promotion of Chilean products. We only organize generic activities for the sector; we cannot organize things that would benefit only one or a few companies.

What are the main advantages and disadvantages of Chile as a wine exporter?
The main disadvantage is that Chilean wines are positioned as cheap wines. We should try and demonstrate that we have good quality wines and that we can compete with countries positioned as producers of excellent wines. At ProChile we try to promote bottled wine exports mainly, to create a better image for our wines. We don't support bulk wine producers, only wineries that produce wine with value added, so they can obtain higher prices.

The main advantages are our climate and terroir. Also, we have a good socio-economic environment, low country risk; we are serious in business and are seen as trustworthy. At ProChile we are trying to promote the country as a whole, in a sort of Macro form, so that it may be used for all our export products. In every product we export it needs to show that Chile has culture, film, that we have beautiful and diverse nature, etc.

What kind of image does Chile have at the moment?
We are busy with creating a country image because we didn't have a specific or clear image. You can look at this as a disadvantage but perhaps it might be considered an advantage as well. A lack of image is a problem, as people do not identify us with anything. But a good thing is that this means they identify us with nothing good, but also nothing bad. That's why ProChile created the slogan: *Chile, always surprising.* We want to convey that Chile shouldn't be identified by a single specific product, but that Chile always surprises, that we have a wide variety of products.

What can small wineries do in terms of marketing and branding to increase their success on the export market?
The first thing is that they should go out there, export! For the very small companies I'd advise to start out in countries close to home, because of language, distance, etc. Also, to be able to increase the quality of their wines and to be able to compare themselves to other, international wineries, it is important to participate in Muestra y Cata. This enables the small Chilean wineries to see who the competition is and how people consume wine in that specific country. Furthermore, we are working closely together with a CORFO programme, *Programa Territorial Integrado,* which is all about increasing local product quality. For instance, we invite experts from France and Australia, so local wineries might learn from them how these countries marketed their wines, as well as increased the quality of their wines. Through CORFO, we also finance technical commissions to look at our main competitors and how wine is produced there. Also, we have been able to organize international wine testing fairs,

so our wineries can be judged by international judges, to see how the quality of our wines compares.

What about cooperation between the wineries themselves?
I'd say there's more and more cooperation. It's been difficult, but at the end of the day, everybody has understood that the only way to penetrate foreign markets is by uniting. Concerning marketing, everybody understands there's a need to cooperate, although there will always be differences of opinion when it comes to image. The wineries that are at the fairs are competitors of one and other, but their relationships are relatively good and they help each other in any way they can, apart from things that have to do with competition.

What strategies are small wineries using most? Targeting market niches such as organic wine?
Yes, more and more. We help them by informing them about what standards are required in what country, etc. That's also why I told you my advice would be to start out exporting to countries close to home, as they normally have less strict rules and standards when it comes to wine.

What do you predict for the future of the Chilean wine sector?
I think the future looks quite good. Better than it used to. Exports have been on the rise, in both volume and value. Bottled exports are gaining compared to bulk exports. And average prices are increasing. About investment, we are always alert, but this is not our main focus, it's CORFO's. Mergers and takeovers are difficult, I think because of cultural reasons. People in the small wineries sector have a problem uniting. This is also true for forming cooperatives. Even though people understand the need to sell a common product, they will still try to free-ride. The only thing really small wineries can do is to cooperate and form an export company however.

Another thing we do by the way is to organize a national competition where wineries send us a strategic export plan and we co-finance all the activities the winning company presents to us in their plan.

Interview:

Eugenio Eben. ***Production Manager Viña Aresti***

Place and Date: ***Lontué, October 30, 2007***

Language: ***Spanish***

Aresti is a family business. We are lucky to have a holding company and own many different businesses, such as Master Dog, the No. 2 pet food brand in Chile. Aresti also has the largest rice company, and is one of the top 10 producers of fresh fruit. That's why we were able to invest more and get bank loans more easily than other wineries. A major problem in the industry is a lack of capital; many wineries borrowed too much money and had to sell out.

A huge advantage of Chile is that we have perfect *terruño*, a lot of different valleys and climates ideal for producing a wide variety of wines; not only in north-south direction, but also in east-west direction. There is still a lack of "pioneer spirit" however; we should look for other interesting valleys to produce different wines. But in Chile we do know how to make good wine.

Another important thing is that Chileans (or at least we at Aresti) are good in production, not in marketing. Producing is one thing, selling the wine is something completely different. We don't have very good consumer research institutions, and our level of technology is not as highly developed as in other countries. There are foreign wineries where they can see what temperature it is in what corner of the vineyard at any given time, from anywhere in the world; completely real-time and up to date information. That kind of level has not reached Chile yet. The same goes for marketing. So we decided to work together with a German company called Racke to come up with the brand Espiritu de Chile. We produce the wine that they want and they developed the brand name and label, and have a large distribution network, as well as customer knowledge. All we had to do was put in half the money and they did all the customer research. Espiritu de Chile even won a design award in Europe.

Our other brand is Aresti; at first we were afraid to use our own family name, because what if it failed? The A on the Aresti label was developed by a Chilean design company. We recently changed our focus: we use our own grapes to make "vino de granel" or bulk wine which we sell cheaply. Around 40 per cent of Aresti's production is still shipped in bulk. With that money we buy better grapes and make high quality wine which we can sell for higher prices. It is important to keep costs down and increase quality so as to sell for higher prices. We expect to raise our prices a little every year, at least for the next years to come.

Another problem the Chilean wine industry is facing is the low dollar rate. We sell our wine and receive dollars, but our production costs are all in pesos. So our advantage of having low production costs is currently in danger. In fact, Argentina has already surpassed us. We are near first world producer levels now. At the same time, I think it is important to pay good salaries and develop a good relationship with your employees. All our employees are part of unions, and everybody can always knock on my door. I think this is important as it ensures that they are motivated. I think Chilean workers are very productive.

Yet another problem we face is the lack of government support. The Chilean government doesn't invest in the wine sector as governments do in other countries, especially New Zealand. Although ProChile and other organisations such as Vinos de Chile help, it is nothing compared to other countries, where they invest millions of dollars. In terms of country image, Chile is completely unknown in the world. In Europe people have no idea where Chile is on the map, they haven't got a clear picture of South America. They don't even know that Santiago is the capital of Chile.

If I'd have to give advice to a small winery (on a personal note) I wouldn't come to this valley (Lontué Valley, part of Curicó Valley, in the large Central Valley). There are better places to plant grapes. And I wouldn't get stuck in the middle like we are at the moment. You either have to be really big and profit from economies of scale, or really small and make high quality wines in low volumes. I know somebody who has a little vineyard in Germany, producing high quality wines. It is a family affair and they have long-lasting distribution channels and customers. They sell for high prices. In Chile this is also possible, only there is a need to export as we do not have a large enough domestic market.

Interview:

Francisco Korta. ***Owner, General & Export Manager of Viña Korta***

Place and Date: ***Sagrada Familia, November 16, 2007***

Language: ***Spanish***

Tell me about your Winery

The bodega took off ten years ago when we bought land and began our first plantations. This year we are finishing our own bottling facility and next year our own oak. We started very small and are taking it step by step. We're doing almost everything with our own money, we use very little debt. The project started with a vision of having 130 HA of our own vineyards and a bodega of 2.000.000 liters. Our focus is on the exports of high quality and hopefully high priced wines. That's the plan. We are in a good zone for grapes (the town of Sagrada Familia, in the Lontué Valley, part of Curicó Valley, which in turn is part of the Central Valley); we are doing a good job managing the vineyards and have good quality production. So in that sense we have already partly reached what we wanted. Our prices are above Chile's average and we reached an interesting volume of sales so far.

What are your principal markets?

Basically the US and a few countries in Europe: Sweden, Finland; especially in Sweden in the *Systembolaget* we are doing very well. Not in terms of volume but with high quality wines that fetch high prices. We are also doing well in South America, especially Brazil. Currently we are entering Asia: principally China. And in South Korea we recently found a distributor that has bought a lot for the first year

What is important to produce high quality wines and enter higher price segments?

Concerning our personal experience: we have our own vineyards; our own grapes. I think that's our strength. We have a bodega with good wine and we have our own vineyards. That's a plus if you want to sell abroad. Because if I talk to potential clients, I can tell them: look we have our own vineyards, we have our own bodega where the wine is produced, etc. This also means we are not dependent on grape producers. Furthermore, to be successful, -I'm not saying that we are successful-, but to be able to compete with the Big Brands, the Big wineries, you have to find your own space in the market. For instance, our vineyards have certain characteristics, we hired some good consultants to investigate micro-climates, soils and sub-soils, and we searched for the best grape varieties given our *terroir*. So we weren't necessarily interested in the best selling varieties. Of course, we planted a lot of Cabernet Sauvignon because it's the best selling variety, but we also planted carmenère, syrah, cabernet franc, merlot, petit verdot and other varieties. Only the varieties that are best suited to our particular terroir. And varieties that we know how to produce well; only wines that we know how to produce well will be able to compete. We compete with wines that have distinct characteristics; that are very much “our” wines, different from the others. We are not trying to copy others and make a Cabernet Sauvignon Reserva or Gran Reserva, if we don’t have the grapes to do so. We don’t want to compete with *Almaviva* or *Clos Apalta* and produce the same blends or wines as they do. No, we want to compete using our own terroir, our own grapes, etc, and we have been pretty successful with this strategy. The demand for our Cabernet Franc is much higher than what we can supply at the moment, the Syrah has extraordinary characteristics, and we have extraordinary conditions to produce Syrah I think. So basically this is what we are doing: finding our own space, finding our own wines, in our own style and in our own way.

The second important characteristic if you are taking about this “success” -since I took over from my brother exactly one year ago, our sales have risen to 70.000 cases (local and international), with an average case price (12 bottles) of around US$ 30-. This “success” is based on the fact that we are searching for markets where the big companies aren’t fighting for. We are looking for different niches. For instance, in the US we aren’t in the biggest states, we’re in the smaller ones such as Michigan and Idaho. We look for smaller distributors, which aren’t interesting for big wineries such as Concha y Toro. We are, on the other hand: we visit them; we try to help them and support them in selling our wines. The capital of Idaho is only a little bit bigger than Curicó. It’s a state of 2 million inhabitants. So, obviously sales projections aren’t very large. But because of that, Concha y Toro aren’t there, San Pedro isn’t there…this is more or less what we are looking for. In Brazil it’s a bit different. We entered early, before many others. We started in São Paulo; we have a few distributors there and now serve other parts of the country too. We already knew our first distributor in Brazil through our family business (leather). Brazil is relatively close by, so we have a lot of reunions with clients, with our distributors, etc.

So we are trying not to compete with Concha y Toro. If they are there, forget it. We cannot compete with them. Also, if they are there, it means that there are large distribution channels, who will demand volumes of 20-30 containers which we cannot supply. We have to look for smaller distributors, smaller channels. Concha y Toro has cheaper wines in every price segment, they have a much bigger range of wines so a big buyer will always try and solve his assortment problems with Concha y Toro. To complement the same range of wines and varieties an importer would have to buy from me, and at least 5 other smaller wineries. Concha y Toro is one-stop-shopping for them.

So in short, you have to search for an importer of the same size as the producer, who feels you are just as important to them as they are to you. You are not as important to big importers, or you might not be able to produce what they want. Furthermore, large importers might use you to solve their own problems. For instance, we have a big importer in England who has a small client in Ireland. They use us to solve this “problem”. What we generally try to do is to not enter markets through the front door.

A third characteristic we have is our company structure. We have a very small structure, very flat, horizontal. This keeps fixed costs down considerably. There’s me, as general manager and export/sales manager; we have a secretary and a person who does all the accounting and paperwork. The rest is production: the oenologist, his two assistants, and other people working in production. We don’t have economies of scale to benefit from, so we need this structure to keep down costs.

And do you have a marketing or branding strategy; do you do something different than others?

We have a very nice label, the letter K. Our last name, Korta really is spelled with a K, not a C in its Spanish version. This is because it is a Basque name. We have always worked with good consultants, as we don’t have our own people for this. So we have looked for the best people that work in the label design business. We started with our K before Aresti came up with the A. Perhaps they got the idea from us. Now there are more wineries that use a letter as a symbol on their labels. We always work with the best consultants and advisors, not only concerning our labels, but also in the field and in the bodega. It doesn’t matter if it is expensive; we are aiming for the highest quality. If I want to sell wine, competing with Concha y Toro’s Casillero del Diablo, I have to make a wine that is much, much better to sell even at the same price as Casillero del Diablo. If it isn’t clearly better, people will always go back and buy Casillero. The big wineries have well known brands, so if we want to enter the market and compete, we need to make much better wines for the same price. I do all the sales and I travel a lot.

A nice label isn’t enough though; you need to be different, distinctive. If you go to the US, you see thousands of wines, so how does the consumer pick you? First they might choose country, then grape variety. Then let’s say he/she still has about 40 wines to choose between, so how does he/she do that? In that case a different label helps. And the K is memorable.

Why do you say Valle de Lontué on your label? Why not the bigger Valle de Curicó, or even Valle Central?
Well, we indeed are in the Central Valley, more precisely in the Curicó valley. The Curicó Valley is divided into the Teno Valley and the Lontué Valley. We are in Lontué, and to be more precise in the sub-valley of Sagrada Familia. We are trying to stress Sagrada Familia, as there aren't many wineries here, so nobody has Sagrada Familia, Valle de Lontué, on their bottle. If we can position ourselves as coming from the Sagrada Familia area, it's another way of being distinctive. I'm not saying it's better or worse than other (sub)-valleys, but it is different. In Brazil we are even working with wines that say: DO (Denominação de Origem or Denominación de Origen) Sagrada Familia. It's about differentiating ourselves form the rest. Nothing more. It might be for the worst or for the best. But in any case it is distinctive and sets us apart.

Do you use ProChile?
No, never. I've used ProChile in another business. In the end you travel in a group of people who all want to do their own thing and in the end nobody ends up doing the things they came for. Ok, so you save some travel costs, but you probably go on a trip of a week, which you could have done in three days if you went by yourself. So in the end it isn't even cheaper and you don't get done what you wanted to do. And they don't help you that much with contacts either; I've never had problems finding importers/distributors on my own. We work with a lot of brokers, or middlemen. Look, you receive let's say 150 business offers, of which only 45 are useful at that moment. Of these, only five are really interesting. You have to be really careful in assessing which ones are really interesting. That's why we always work with credit insurance. We need to know if they are solvent and trustworthy.

I have never liked ProChile. They spend a lot of government funds. They have offered me a lot of state money, through all kinds of interesting programmes and projects. One day CORFO offered me money to manage our image and I was very interested. But then they sent me a list of people I could spend the money on…a list of four consultants, who I didn't know. So I said, I don't want to work with these people, I have my own people. But that was not allowed. Plus it's very expensive, you need to enlist and the consultants/people they use are often not the best out there. So you have to wear a jacket that you don't like and that doesn't fit you. I prefer to spend the little money if have by myself, so I have to be super efficient. So I only take a few trips a year and I have to do well! If I go to the US for ten days I have to come back with something, because I'll only travel to the US once or twice a year. So if it's not a productive trip I'll be spending a lot of my promotion budget for that year. Next year I will have to travel to a few European countries, such as Sweden, where I already secured sales, to help my importers to sell our wine; visit some events with them to support them; basically to do things that serve them, not me. It is important to develop good relationships. But if I travel to the US with ProChile, they will visit the States and cities where the group of Chilean wineries wants to go. Obviously, not the states I want to visit. That's why we operate independently; we aren't part of the *Ruta del Vino* either. One day we might, but first we need to be able to show the tourists/journalists something interesting. Why would I pay a lot of money on promoting my bodega if my bodega isn't even finished yet? So currently that is not an option yet.

We have been looking to find our own way, with our own wine and our own ideas. And so far that has worked for us. It has been an interesting year.

They say a problem for Chile is its lack of Country Image. How do you feel about this?
Well, I think we do have a country image, but it's probably not the best to have. We are known to make good, cheap wines. Although….I'm not sure it's that bad either…it would be better to be famous for making good, *expensive* wines, such as la Rioja, or some French wines. Those are very expensive wines that people want to pay for. But we have lower production costs than Europe. A lot lower. And we have our *terroir,* lower labour costs. So our advantages enable us to produce cheaper wines of the same quality. That is why we sell our wines more cheaply. The last few years some Chilean wineries made the mistake however, to enter the super cheap segments where there is a lot of price competition. Examples are Via Wines, San Pedro with Gato Negro and Valdivieso. A case of Chilean wine in the UK would sell for US$ 14, or even US$12. That makes no sense (US$ 1 per bottle of wine). If you sell a brand for one dollar one year and the next year the price of grapes increases, you have no margin left. That is another advantage that we have, we only use our own grapes, so we are not affected by fluctuations in grape prices. This is what happened to Valdivieso. They didn't sell that cheaply, but entered the market selling for a very low average price and wanted to increase price over the years. Then others entered and sold for even lower prices. If you are competing like this, brands don't matter anymore.

What are the major problems and threats you face at Korta?
The first and foremost is finding the right distributors. The market is typically run by big distributors. The distributors hold all the power, the wine business is run by them; not by the producers. If you see at what prices producers sell and what consumers pay in the end…there's an enormous difference and all that money goes to the distributors and intermediaries. And the distributors are increasing in size and they buy up greater volumes every time; they have negotiating power and they prefer to do business with the large

wineries. A problem for smaller wineries is to get these big distributors interested in your brands. That's how it is nowadays.

I've also read a lot about a lack of cooperation and capital
I think there's always a lack of capital in any kind of business. If you want to enter a certain business and be successful you always need a lot of money. You need to borrow money from banks.

Should the Government help out more? Perhaps in helping more to create a Country Image?
That'd be great, but I think the main problem is that the money the government is currently spending is used badly. First of all, people at ProChile are working with a lot of different industries and products. Also, the people (importers/distributors) you meet at ProChile fairs and events are often not interested, or not the ones that have decision making responsibility (purchase managers) about buying your wine. Furthermore, you are there with let's say 30 other wineries, so often distributors send someone to have a look and make a list of the various wineries. What I do however do sometimes is to go to Wine tasting contests organised by ProChile, perhaps with my distributor.

And business organisations such as Wines of Chile?
Wines of Chile are doing some very interesting things.

Interview:

André Luteijn. *Co-owner of Viña Alempué.*

Place and Date: *Curicó, November 12, 2007*

Language: *Dutch and English*

How does the Wine business differ from other businesses?

One of the problems is that the wine industry sounds so good. A lot of people got involved in the industry because of this. If they ask in what business you are it sounds better to say in the wine business than in the toilet paper business. If they ask me what I do, I tell people I'm in the fruit, flower and wine business. The first thing that they say is: tell me something about the wine. So a lot of people here in Chile are in the wine business as long as they just don't loose too much money. I am currently one of them, although if I could sell today, I would.

It seems a lot of successful Chilean business men see their wineries as a hobby, as something along the side.

I'm not saying that those are the only companies in the business. Just take a look at Concha y Toro, they are very successful. But I think that even the family that own San Pedro would probably sell, if they had the chance. So I think it's a difficult industry because of that.

But is this only the Chilean case or is this a world-wide phenomenon?

Probably worldwide, but perhaps in France it's not as bad. In the US it's the same case. Not for the bulk producers, because that's a real industry.

What are the major advantages of Chile?

A very good climate.

Low(er) Labour costs?

That can never be the premise of any long term business. I think climate is probably the only real advantage, although we have reasonably low labour costs if you compare us to for example Australia.

And the main disadvantages?

No country image. New Zealand and especially Australia have done a very good job in positioning their countries, which is very important for wine sales. Most people first decide between red or white wine and then usually ask themselves: ok, what country? Chile hasn't done a very good job at this.

Are organisations like ProChile, ChileVid and Wines of Chile helpful?
I'm not the right person to ask, because I haven't been involved with them.

Is there a lack of capital in the business?
Not really…but of course if you can get the government to help you out…but I'm not sure if creating a country image should be done by the public sector.

Is there a lack of cooperation then among the wineries themselves (marketing and R&D wise)?
Yes. I do think it would be beneficial if wineries would join forces. But I don't know what benefits there are by mergers or take-overs. Buying up very well known brands? That's the only value there is in the wine business, the brand. But who really has a brand? Nobody in the world, except maybe Gallo. Even Gato Negro from San Pedro is selling wine in volumes and very cheaply. They have no margin, so again there's no real value in that either. What other reasons are there for mergers or acquisitions? To get access to knowledge, branches, customers, buyers, suppliers, growers, clients? It's all based on personal relationships. Brands, infrastructure? So I don't see the case for mergers in the wine industry. That's probably the reason why even though we would like to sell the winery, there is no way we can. Because who is going to be interested?

So what could Alempué do to increase its sales abroad?
You tell me.

For example develop relations with the international press, give a lot of attention to PR?
It's a must. And there's definitely a case for joining with other companies and sell together. Developing a brand together or pool marketing resources is not an option, because everybody makes different wines, you cannot put one brand name on completely different wines.

What about choosing the right importer?
Absolutely.

However, most importers will probably not do all the consumer research and develop a brand name, and do all the selling and promotion too, leaving only the production to the winery, such as in the case of Espiritu de Chile by Aresti and Racke?
Most importers just buy the wine and if you're lucky they will tell you if they like or don't like your label.

They probably have better local consumer knowledge though.
They do, but they don't consider it their job. Look, when you start a winery, the first step is fantastic; you have a budget with which you set up the business, starting production etc. But most people don't have a budget for the second step which is more important. The most important thing is *first* to set up sales and *afterwards* the winery (production) or separate the two completely. Montes has done an excellent job at this. They also started at the right moment, in the beginning of the nineties when exports took off. They had (and have) the right strategy and the right people. And the quality of their wines is very good.

All the literature seems to point in the direction of developing a Brand Chile and cooperating. Furthermore, the only thing the (smaller) wineries can do and directly influence are: to increase the quality and try to push down production costs.
Yes, but we are talking about boutique wineries, which is still a niche market.

And is that what you envision for Alempué?
I have given it a lot of time and thought…..and in our case we have always tried to extend services to other wineries to make a profit, while at the same time produce our own wines, trying to make a name for ourselves and increase our own production at the expense of the services we conduct for others. But when you look at the bottom line, even the services we provide aren't profitable, or hardly. And you always have to look at new wineries interested in our services because they are mostly interested because of their own (temporary) production capacity problems. So to them we are always only a temporary solution.

Aren't there any possible spillover effects?
There's always something to be learnt, but not a lot. For example, some wineries are going to produce real premium wines at our winery and need to bring in certain smaller machinery, especially geared towards producing real premium wines, which we are allowed to use too, so that's very positive.

An interesting option would be to sell wine together with others, in the sense of offering wines to supermarkets in a group of wineries together. Then you could say to the supermarket: we'll come up with a different wine every month.

And what about niches such as Organic Wines? Do you think people are interested and willing to pay more for organically produced wines?
I'm not so sure that people would pay a lot more for organic wine in Holland, but in the US it' might be a different story.

Chile's country image could play an important role in this, as it is known for its natural beauty and as a pest/phylloxera free paradise.
I think you have to develop awareness first.

And what about Chile's name as a producer of cheap, but reasonable wines? Is that still an advantage if you want to increase quality and prices to enter higher segments?
Exactly, it is very hard to increase prices. Another factor, probably the most important, is costs. That is the only thing that you can influence/control directly.

But even that is becoming difficult in the current situation of the low dollar exchange rate and high electricity prices, which rose about 40% in one year if I'm not mistaken.
And labour costs are also going up….

Argentina's labour costs might be close or even lower than Chile's right now, as they don't have the same exchange rate problems, plus they have a better country image. Why is Chile so "unknown" in the world?
Well, if you compare Chile to Argentina….they've won a few world championships, they have the tango, it's a bigger country, and it's also "closer"; at least to Europe. In the old days, when I flew to Chile with KLM, you first landed in São Paulo, where half the people would get off. Then you'd land in Buenos Aires were another 75% of the remaining people would get off. Only a few people (and a few unlucky people who had fallen asleep) would go to Santiago. And the years of Pinochet gave Chile some negative publicity too. Most people remember Chile and see a dictator with sunglasses.

But Chile is also more stable than Argentina for example, it scores lower on the corruption index and it has a lower country risk, which make Chile attractive to foreign investors. And

Chile has a lot of bilateral free trade agreements and is much more export oriented. These are very important advantages.
The export apparatus in Chile is functioning very well. The authorities, the documentation, etc, it's going very well. So that is an advantage we have.

So what exactly is Alempué's strategy at this point? Or what should it ideally be?
First of all, I think we have to create a good name, a name that everybody can pronounce.

Have you had professionals look into this?
No, we haven't. Then, secondly, an attractive label. Thirdly, an interesting back label. And lastly, a good price-quality ratio. Selling wine is a three part game:
1. Consumers need to be *interested*; you have to get their attention through an attractive label
2. Then they *pick up* the bottle, read the back label etc
3. They *put the wine in their basket*
However, the most important is step number 4: *repeat purchase.* They have to have tried and liked your wine and come back to buy it again. So in a sense you haven't really "sold" a wine unless people come back to buy your wine for a second time. So that's the marketing of wine. I think we took a few wrong turns in the past. First of all, the name Alempué is a difficult name and hard to pronounce. Also, our old May May brand label didn't really work either. Thirdly, our varietals are very good, but our reserve wines weren't good enough in quality for the first five years. In 2001 we came up with a premium line which was very good, but it wasn't a real premium wine. It was too light to be premium. So there was no consistency between what was *on* the bottle and what was *in* the bottle.

At the moment we have a good product, also our reserve wines. The only thing that we could improve is our premium wines (gran reservas).

And the premium wines might very well be the most important at the moment, if you want to increase quality and price.
We should participate more in contests to gain medals. We also need to create more awareness.

How do you feel about the labels for your PRO brand?
PRO sounds like a power tool instead of the name of a wine.

But it's all very subjective. Even if you have a focus group of 30 people to test different brand names and labels, another group might come to a completely different conclusion.
The same holds for taste. One of the biggest problems of wine is this: if you have somebody who doesn't know anything about whisky and you let him taste a few different brands: one bottle of $10, one of $20, one of $30, one of $40 and one of $50; they will be able to appreciate in let's say 70% of the cases which whisky is better and therefore more expensive. It's far more difficult concerning wine. Some people prefer a $5 dollar wine over a $25 dollar wine. It's very personal and more difficult to appreciate. Brand Names and labels are the same.

Furthermore, if I go to a Chilean supermarket…I know what to choose because I know the Chilean wines. But if I go to a supermarket in the US or Europe, where I don't know the wines, then I think ok, how much am I willing to spend? If they ask €12 for a wine, it has to be of reasonably good quality. But, depending on the occasion, I might spend €25 for a special occasion, or perhaps just €6. So this is your strategy when you want to buy a wine. I feel most people approach buying wine this way. And they might come back to buy your wine again if they really liked it. But there's such an enormous assortment of wines on display, there is so much choice…

Do you think the future is in single variety or in blends? Single variety might be more recognizable to consumers, but blends might be a way to differentiate your wine better from others.
If you look at a wine card in a restaurant and you can choose ten cabernet sauvignons, ten merlots, five carmenères, a few pinots and then only two blends...you might be more inclined to say: well, let's try one of these blends. But then, if there are ten blends on the wine card as well, you loose that advantage too. Concerning wine it's a bit like the famous saying: *If you can't be better, then be different.* And it's clear it is very difficult to be better. So you need to distinguish yourself. This is also difficult however, given the industry. An example: a standard bottle of 750 ml is too much for two people on a typical evening during the week, if you have to get up at 06.30 to go to work the next day. So in my case, we drink a few glasses and throw away the rest, because if we don't, we'll finish it all in the end and feel bad the next day. However a small bottle of 350 ml is often not enough for two people, who'd like to have more than one glass. So a bottle in between would be ideal, and there'd definitely be a segment for this. The problem is that we are dealing with a *consumer good*. I'm used to work in the fruit and flower business, which is a *commodities trade.* If you have something good to sell, you have a customer. And there is no marketing budget. Wine is a consumer good, with a budget for marketing, promotion….and that's why it is hard for small wineries to be profitable.

Not only for small wineries; even big companies with large budgets struggle sometimes. A lot of beer and liquor companies have been expanding their portfolios the past ten years by buying wine companies and they have also struggled, even though they have distribution channels and marketing and branding budgets and know-how.

The wine business is a challenge. I'm lucky I have a very good fruit and flower business. We are the number one fruit exporter in Chile and our clients in Asia are very happy with us. And if you have a winery that isn't going that well, it hurts. It's like an eyesore. At the same time, I'm not too proud to say: you know what? I'm going to sell the business. Yet if I had the chance I'd do it, but that's also not the case.

Appendix 2: Questionnaires

Questionnaire

Willem Wagner. *Former President Rabobank Chile*

Willem Wagner has been general manager for Rabobank Chile from 1998-2002, in which period he was in touch with Rabobank clients in the Wine Business.

- *What are the most important differences between Chile's success on the export market compared to the success of other major New World exporters, such as Australia and Argentina?*

In general Chilean wines have a very good price-quality ratio -when it comes to table wines- compared to other wine exporting countries. However, there are a few things Chileans haven't given proper attention to: presenting the market with a Chile-image and the development of specific varieties where Chileans could offer first class quality. Both will be addressed in this questionnaire.

- *What are the main weaknesses of the Chilean wine industry at the moment? Is there a lack of*
    - *Government support?*
    - *Cooperation between the industry and public/government organizations?*
    - *Marketing and Branding focus in the industry?*

These are all weaknesses indeed, although the wine industry operates without government support in many countries, not only in Chile. So that's not a decisive disadvantage.

- *What is Chile's image abroad? Why doesn't there exist a Brand Chile (yet) such as in Australia? Are Wines of Chile and/or Pro Chile capable of developing such a strategy?*

The main problem is the Chilean entrepreneurial spirit. Chilean businessmen are individualists. Because of a variety of factors they trust themselves better than the added value of cooperation, or worse, government intervention. The organizations you mentioned are not strong enough to change this pattern. Another problem is that Chile is now lagging behind other countries concerning image and it will be very expensive to make up for lost ground. The volume of the Chilean wine industry is not sufficient to bear these costs.

- *What does the (near) future hold for the Chilean Wine Industry? Is there an ongoing trend of increasing quality so as to penetrate higher price segments? Are we going to see acquisitions, mergers, joint-ventures, investment, etc?*

One of the problems Chilean wine producers face is finding a distributor. This is vital. Because of this, individual winemakers and small wineries will always hold marginal market share abroad, unless they are able to differentiate themselves by producing extremely good wine. So it is to be expected that we will see two differentiated strategies: placing power versus specialization. Obviously this is already the case, but I think this trend will increase. An extra problem is that there is too much table wine in the world, even table wine of a higher category, which makes it even harder for producers and marketers.

- *Is Chile's image of a good, affordable wine producer an advantage or disadvantage for wineries trying to enter higher segments?*

One of the problems is that Chilean wine isn't very interesting. By this I mean there are no differentiating factors of Chilean wine. Chileans copy good wines from California so the differentiation is only to be found in the price difference. The price difference is there, but to be able to profit from that you need to be a strong player with placing power.

- *What are the main disadvantages of the smaller exporting wineries in Chile? A lack of a coherent business strategy? A lack of capital? A lack of cooperation between wineries?*

  Yes, yes and yes. All three aspects are of course related to each other. But this is a generalization; there are some very interesting exceptions.

- *What are the most common strategies for small exporters? Lowering production costs, increasing the quality of the wine to target higher price segments?*

The most successful strategy for smaller wineries is indeed to increase the quality of their wine and enter higher price segments. Lowering costs is important of course, but there is not much room left for cost cutting. In the wine industry of today it's not enough to produce good wine, good marketing is the key, and for the reasons I mentioned before, this is where the major restrictions are.

- *What are the most popular marketing strategies now? What are the trends; Carmenère, organic wine, blends, entering "new" markets in Asia, etc?*

There are a variety of strategies, including the ones you mention, but there isn't one that stands out or dominates.

- *Is there a way for smaller wineries to reach the final consumer, apart from the label and back label?*

Small producers are a hostage of the distribution system, where we see the same trend as in supermarkets: generic products in various quality ratios; the presentation of the product is dominated by the distributor, not the producer; products are being "anonimised".

- *What would you advise smaller wineries in order to be successful?*

Join a larger unit, in whatever shape/way. Focus on only wine production if that has an obvious effect on quality and image, for example by developing a terroir.

- *What would you advise a small winery in search of a distributor/importer?*

Again, join a larger unit, in whatever shape or way. And then to produce the wines that the distributor needs.

- *What markets will prove to be the most interesting?*

Most markets offer certain possibilities, as long as you focus on the needs of that particular market. But the wine industry will remain a marginal business unless you produce a Grand Cru Classé, or unless you are very big, or a mix of both.

- *What would you advise in terms of marketing and branding?*

Work your way back from the market, instead of starting with your wine product. Analyze the market itself, what does the market want/need, instead of looking where you can place your wine. It might not be as much fun as focussing on creating your own wine, but it makes better business sense. Unless you're less interested in the bottom line and the business and more interested in only producing your own good quality wine; and if -at the same time- you have the money to operate in this way. As a consumer and wine enthusiast I'm always very interested in these kinds of people, of which sadly there aren't too many!

Questionnaire

Cees van Casteren. *Wine writer, freelance journalist and wine consultant*

Cees van Casteren is (among many other things) author of: *Paradiso. De nieuwe wijnen van Chili*.

- *What are the most important differences between Chile's success on the export market compared to the success of other major New World exporters, such as Australia and Argentina?*

Chile has a broader market base; they are well represented in all import countries. Australia is mainly focussed on the US and UK, and South Africa mainly on the Netherlands, UK and Germany.

- *What are the main weaknesses of the Chilean wine industry at the moment? Is there a lack of*
    - *Government support?*
    - *Cooperation between the industry and public/government organizations?*
    - *Marketing and Branding focus in the industry?*

Major weaknesses are:

- Exchange rate problems dollar, euro, peso.
- Lack of Government support, at least if compared to the EU
- A lot of personal initiative (not much cooperation)
- Wines of Chile focuses on the two most important markets (UK and US) and so neglects other important markets

- *What is Chile's image abroad? Why doesn't there exist a Brand Chile (yet) such as in Australia? Are Wines of Chile and/or Pro Chile capable of developing such a strategy?*

Image? What image? Chile has no image. The wines have more of an image than the country. The wines are smooth, warm, easy to drink, affordable. If there is a *Brand Chile* it is more influenced by the image of Pinochet than by any other, more positive associations. ProChile is a good organisation and has set up something positive with their *Chile, Al Ways Surprising* Campaign. Sadly, it hasn't been sufficiently adopted by the wine industry so the ultimate effect has been zero.

- *What does the (near) future hold for the Chilean Wine Industry? Is there an ongoing trend of increasing quality so as to penetrate higher price segments? Are we going to see acquisitions, mergers, joint-ventures, investment, etc?*

The first thing is upgrading the quality of the wines as well as the packaging. A few Chilean wineries have already started (Errázuriz, Carmen, Cono Sur, Concha y Toro). Too many other wineries are still afraid to invest in this, even though it's the first step. After upgrading quality and packaging, wineries should concentrate on the right distribution and devise a promotion budget.

- *Is Chile's image of a good, affordable wine producer an advantage or disadvantage for wineries trying to enter higher segments?*

Chile has an image of producing affordable wines, not cheap wines, which is South Africa's image. Furthermore, Chile has enough *icon* wines to stay out of the cheap segment in terms of image, but again, more producers need to work on this.

- *What are the main disadvantages of the smaller exporting wineries in Chile? A lack of a coherent business strategy? A lack of capital? A lack of cooperation between wineries?*

All of the above, although there are some exceptions (such as Klaus Schröder). The most important thing for these smaller wineries is to get in touch with the right distributor. What they really should do is to have ten small wineries cooperate and together find one very good sales manager that exports the wines in their name. This would enable the wineries to focus only on production. There are numerous of successful examples of this structure in other countries.

- *What are the most common strategies for small exporters? Lowering production costs, increasing the quality of the wine to target higher price segments?*

Generally, just improving quality would already be enough. The major problem is finding export markets.

- *What are the most popular marketing strategies now? What are the trends; Carmenère, organic wine, blends, entering "new" markets in Asia, etc?*

Biological (organic) wine is currently *in fashion*, but is probably here to stay. Chile has an advantage in this over other countries and should be able to exploit this further. BRIC countries (Brazil, Russia India, and China) are popular, but so far these markets haven't really delivered what was expected of them. Especially India and China have been disappointing. They import a lot of cheap bulk wine, but are still not a very interesting market to export bottled wine to.

- *Is there a way for smaller wineries to reach the final consumer, apart from the label and back label?*

Only through a good distribution strategy. I feel pooling of a sales manager is the most practical option.

- *What would you advise smaller wineries in order to be successful? What would you advise a small winery in search of a distributor/importer? What would you advise in terms of marketing and branding?*

I'd take the advice of local consultants to find the right distribution strategy and again, I'd work with a common (pooled) sales manager.

Questionnaire

Patrick Valette. *High-end, quality wine producer and wine consultant*

Patrick Valette has produced some of Chile's top wines such as Viña Neyén's Espiritu de Apalta and works as a consultant covering viticulture, vinification, marketing and commercial planning.

- *What are the most important differences between Chile's success on the export market compared to the success of other major New World exporters, such as Australia and Argentina?*

It seems to me that Chile has the capacity to sell a more complex image. Chile has distinct valleys, more easily identified than Australian sectors. Australia has a country image, which Chile still doesn't have and if we work on this we have to do it in the combination of country image/ valleys. We have a lot of diversity and we need to know how to sell this.

- *What are the main weaknesses of the Chilean wine industry at the moment? Is there a lack of*
    - *Government support?*
    - *Cooperation between the industry and public/government organizations?*
    - *Marketing and Branding focus in the industry?*

There is a lack of knowledge on how to work together, but this is not the same as cooperation between wineries. Everybody who participates in Wines of Chile thinks of their own interests first and not in the future interests of the Chilean wine industry as a whole.

- *What is Chile's image abroad? Why doesn't there exist a Brand Chile (yet) such as in Australia? Are Wines of Chile and/or Pro Chile capable of developing such a strategy?*

Chile's image within the wine industry is very well known, but not strong enough to the consumer. There is a lack of promotion trips, of wine tastings, but one can't think of organising these with the existing concept of Wines of Chile. The actual director's departure is an opportunity, but we'll have to see if the directors are able to change the way Chilean wines are promoted.

- *What does the (near) future hold for the Chilean Wine Industry? Is there an ongoing trend of increasing quality so as to penetrate higher price segments? Are we going to see acquisitions, mergers, joint-ventures, investment, etc?*

Viticulture, clones, limitation of production, more natural oenology…there's a multitude of details that will make the difference.

- *Is Chile's image of a good, affordable wine producer an advantage or disadvantage for wineries trying to enter higher segments?*

It's an advantage, wines should stay BBB, but a parallel image of quality needs to be developed

- *What are the main disadvantages of the smaller exporting wineries in Chile? A lack of a coherent business strategy? A lack of capital? A lack of cooperation between wineries?*

A lack of time…they have to continue like they have so far, but they need to be supported to partake in the order of national and international wine. And let them take their space in the industry. It's a big contribution to competition.

- *What are the most common strategies for small exporters? Lowering production costs, increasing the quality of the wine to target higher price segments?*

Increasing the quality of the wine, to be able to enter higher price segments. Costs are never going down. The only strategy is increasing quality and prices, to be able to be more present on international markets.

- *What are the most popular marketing strategies now? What are the trends; Carmenère, organic wine, blends, entering "new" markets in Asia, etc?*

They should create a promotion group, based on the quality of their wines and then export. I know this is a very lucrative strategy after a while. The following questions are the same and receive the same answer.

- *Is there a way for smaller wineries to reach the final consumer, apart from the label and back label?*
- *What would you advise smaller wineries in order to be successful?*
- *What would you advise a small winery in search of a distributor/importer?*
- *What markets will prove to be the most interesting?*
- *What would you advise in terms of marketing and branding?*

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CHILEAN WINE REGIONS