

Global market review of Champagne – forecasts to 2010

2007 edition



Just-drinks

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2007 edition

by Richard Woodard

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Seneca House
Buntsford Park Road
Bromsgrove
Worcestershire
B60 3DX
United Kingdom

Tel: +44 (0)1527 573 600

Fax: +44 (0)1527 577 423

Web: www.just-drinks.com

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Holly Nash

Research manager, just-drinks.com

Tel: +44 (0)1527 573 609

Email: holly.nash@just-drinks.com

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Chapter 1 Introduction

The rest of the French wine industry is casting envious glances at Champagne in 2006. Rising sales at home and abroad, with revenues also on the increase, make this the saving grace of an industry that is currently suffering amid the global oversupply of wine.

And the prospects are broadly positive as well. Core markets look solid and, although some may decline in volume terms, improvements in the product mix should help value. Meanwhile, emerging markets like China, Russia and India are creating genuine excitement in the boardrooms of Reims and Epernay.

There have been one or two changes in those boardrooms of late: after a sorry few years, the Lanson International business has been taken over by Boizel Chanoine Champagne, with president Bruno Paillard intent on repositioning the Lanson brand further up the price ladder, separating it from the core of the own-label business.

The Taittinger story reached its broadly desired conclusion when the Taittinger family, thanks to the financial assistance of bankers Crédit Agricole Nord-Est, bought back control of the house from equity group Starwood Capital. Now, the Taittingers have to find the investment to buy out most of Crédit Agricole's stake, which could be tricky. That saga still has some way to run.

Elsewhere, Moët Hennessy continues to lead the sector by a country mile, while Vranken Pommery Monopole is maturing with an increased accent on value, as well as chasing volume. Pernod Ricard is set to drive up the luxury focus at Mumm and Perrier-Jouët, while the profitability of Louis Roederer and Bollinger will remain the envy of many.

So many in Champagne are enjoying prosperity, but as ever in the region, that prosperity rests on a knife-edge. Sales increases have put pressure on grape supplies for the past three to four years, pushing up prices and threatening a repeat of the crash of the early 1990s. Hopefully, some intelligent proposals – to increase the appellation in the long term, and to increase yields immediately while safeguarding quality – should help prevent history repeating itself.

Chapter 2 The markets

Introduction

It should be a dream scenario for any drinks category: booming international demand, both from core and emerging markets, for the most part uninterrupted by price rises – caused by currency fluctuations and the rise in the cost of raw materials – and no sign of any halt to this buoyant trend around the world.

And in truth, the *Champenois* are not complaining – but quite a few companies are privately worried that the market might be overheating, and that a slump or even a dip in the world economy could threaten the prosperity that the industry is currently enjoying.

For the *Champenois* have been here before. The last time grapes were this expensive, in the early 1990s, along came a widespread economic downturn. The market plunged, profits were decimated and grape prices followed suit. No one in the region wants to see a repeat of that scenario.

Since post-millennium overstocking drove export shipments below xxxm bottles in 2001, Champagne's international trade has risen steadily, boosted by stable core markets, unpredicted growth in its number one export market (the UK) and fast-rising interest in small but potentially lucrative markets like China, India and Russia.

The latest figures suggest a continuation of this trend. Export shipments in the seven months to the end of July 2006 were up xx%, with even the recently static French market showing a xx% increase over the same period.

That is enough to worry many companies who are already struggling to find supplies to meet this fast-increasing demand. *“Ideally we would prefer xx% [growth],”* says Yves Dumont, chairman of the management board at Laurent-Perrier. *“We simply don't have the supply to fulfil such growth.”*

There are signs that Dumont's wish will be at least partly granted. Price rises, again caused by exchange rates in dollar markets and – more generally – by the simple mechanics of supply and demand pushing up grape prices, are likely to lead to a slow-down in growth towards the end of the year. Volumes

Chapter 3 The companies

This covers the top xx companies in Champagne, accounting for all the major négociant businesses in the region. Companies are listed in order of last recorded annual turnover (in most cases, 2005).

Moët Hennessy

2005 turnover: EURxxbn (estimated, including EURxxm for Moët, Ruinart and Mercier)

2005 sales: xxm bottles, up xx%

Domestic/export split: xxxx (excluding Mercier)

Major markets: US, France, UK, Italy, Germany

Brands owned: Moët & Chandon, Veuve Clicquot, Mercier, Ruinart, Krug

Vineyard holdings: xxxxha

The Moët Hennessy Champagne business, in which LVMH has a xx% share and Diageo xx%, continues to dwarf the rest of the industry, despite the disposal in recent years of brands such as Pommery and Canard-Duchêne. Global market share remains a touch under xx% (2005).

Precise figures are hard to come by, not least because the group is notoriously secretive about detailed sales statistics for its brands. Educated estimates would now put global annual sales of Moët & Chandon, plus prestige *cuvée* Dom Pérignon, at well over xxm bottles, with Veuve Clicquot at around xxm bottles. French market specialist Mercier accounts for more than xm bottles, with the balance made up by premium brand Ruinart and luxury name Krug.

The latter two, plus Dom Pérignon, remain a key focus for the group – and a notable success story – as the emphasis shifts from volume to value. Some commentators have voiced concern that quality at Dom Pérignon may be compromised in the drive for extra sales, although this has probably been over-stated. Anecdotal evidence from key market Japan suggests that LVMH was concerned that Dom Pérignon was becoming “ubiquitous” in such a luxury-obsessed market, prompting price rises to enhance its exclusivity.

LVMH head Bernard Arnault has made no secret of his wish to concentrate on the most profitable brands – hence the disposals of Pommery in 2002 and

Chapter 4 Production

Each year, Champagne's regulatory body, the Comité Interprofessionnel du Vin de Champagne (CIVC), announces the dates on which each village's harvest can start. The announcement in early September 2006 was marred by a small but vocal demonstration by angry grape growers. Unlike their counterparts in the south, these farmers were not complaining about having tonnes of grapes for which there was no market – in fact, the situation in Champagne is just the opposite. The limit on harvests of xxxxxkg per hectare, at a time when grape supplies are much sought-after, means that growers are left unable to pick a decent proportion of their vineyards' natural yields, which can be anything from xxxxx-xxxxxkg or, in the case of less well-managed plots, even more. Grapes are left to rot on the vine or are simply destroyed.

That situation is likely to be addressed by the time of the 2007 harvest, but the protest by growers who are not known for their militancy illustrates the supply challenges facing Champagne in 2006: market demand is reaching unprecedented levels, which puts huge pressure on a region where the appellation is more or less fully planted. Something has to give, and all are determined that grape prices should not be allowed to reach dangerous levels, which could threaten a repeat of the boom-bust cycle of the early 1990s. Thankfully, the region in general, and the CIVC in particular, is taking steps to keep Champagne's fragile balance – between supply and demand, and between the big houses and the humble growers – intact. In an area where the big producers are responsible for nearly xx% of sales, but only control xx% of the vineyards, each group needs the other – and the continuation of that balance is crucial.

The 2006 harvest

Early reports on the 2006 harvest suggest that it has delivered what the *Champenois* wanted: good quantity and quality, despite heat spikes in July, a cool and damp August and some more humidity and rain around harvest-time. Rot was a problem in some areas – as was spring hail – but overall everything looks good.

Chapter 5 The value question

When not discussing the vexed questions of how to balance supply and demand, and how to stop grape prices spiralling out of control, you will hear a lot of talk from the Champagne houses on how to build more value into their business.

This is only natural at a time when raw material costs are rising and markets are resistant to price rises; meanwhile, currencies, particularly the US dollar, are working against profitability.

Perhaps the most obvious way of doing this is for houses to introduce their own prestige *cuvée*, designed to tap into a market where the likes of Dom Pérignon, Cristal and Krug have been so successful in the recent past. As well as a growing appetite for these products in core markets like the UK, the US and especially Japan, demand is also increasing in emerging markets like Russia and China.

But producing a rival to DP or Cristal in such a brand-aware market is far from easy. For example, co-op brand Nicolas Feuillatte has relaunched its Palmes d'Or luxury offering this year, removing the Feuillatte name from the label in an effort to set it apart from the mother brand. *"If we want it to go fast and target the right customer, it would not be possible through Nicolas Feuillatte,"* says marketing director Véronique Dausse. *"It's a different positioning environment and brand. For us it was always very difficult to link the two of them."* Nicolas Feuillatte's strength, she adds, is in being approachable and easy to understand. *"That doesn't fit with the positioning of a prestige cuvée."*

At Duval-Leroy, sales manager Michel Brismontier acknowledges the difficulties, but the company is pressing ahead with the launch of its Femme de Champagne *cuvée* in magnum by the end of 2006. *"It's not big quantities of Champagne, but it's very difficult for a house like Duval-Leroy to sell a high, expensive product,"* he says.

One producer clearly aiming to make a foray into the luxury market is Pernod Ricard, with its recently acquired Mumm and Perrier-Jouët businesses. Mumm will finally get its long-awaited prestige *cuvée* in the second half of 2007, while

Chapter 6 Role of the co-ops

The role of the Champagne co-operative has changed immeasurably since they were set up to protect vulnerable growers from the vagaries of the market, offering them economies of scale, services, a voice of their own and an alternative to selling their grapes direct to a *négociant*.

The two major Champagne co-ops, Nicolas Feuillatte and Alliance Champagne, are major, branded Champagne producers in their own right. Feuillatte's eponymous brand is likely to sell 100m bottles by the end of this year, and the company also sells about 200m bottles of BOB products.

Meanwhile, Alliance's international umbrella brand, Jacquart, has won critical acclaim for its wines and sold 200m bottles last year, part of a 100m-bottle-plus distribution business. Collectives they may be, but modern co-ops have almost as much power as the biggest houses.

Their greatest strength, of course, lies in supply. With thousands of hectares of vineyards at their disposal, many of them in Premier Cru and Grand Cru areas, they can ratchet up supply relatively easily and come up with innovative and value-added new *cuvées*. This has been a particular strength of Feuillatte in recent times.

Asked whether the modern co-op is beginning to look like just a different style of Champagne house, Dominique Pierre, CEO of Nicolas Feuillatte, deflects the question: *"I don't know if the growers have changed their role, or if the houses have changed,"* he says, pointing to the fact that institutional investors have replaced traditional families in owning Champagne houses, and the potentially destabilising effect of this.

"There are also new négociants like Vranken and Paillard. It's not an opposition, it's a difference of how they act and perform. The co-op is not fundamentally different. The shareholders are growers, they demand a return on investment and profits. We're like the older model of Champagne houses."

Not everyone sees things quite that way. Even some growers are suspicious of the level of ambition shown by the major co-ops. One grower-producer, who

Chapter 7 Global warming

There is a lot of nonsense talked about the effects on Champagne of climate change and global warming. Read some of the scare stories in UK newspapers and you might expect the average grower on the Montagne de Reims to start planting Syrah, while casting envious glances at the new promised land for sparkling wine: Kent and East Sussex.

No disrespect is meant to the excellent vineyards of Southern England, but reports of the demise of Champagne's viticulture have been rather over-stated. However, change is definitely in the air.

The facts speak for themselves: peak summer temperatures have risen x° C or so between 2000 and 2005 – although that is a relatively short-term sample. There is better evidence in the increase in berry and cluster size over the past xxyears, with average grape weight almost doubling from xxg to xxg over the period.

There is more than one reason for these trends. More precise clonal selection and better viticultural management have had an effect too, but earlier budbreak, flowering and harvest times are the primary causes of bigger berries and clusters in the region.

"We have ideal conditions for flowering, year after year," says Patrick Le Brun, president of growers' union the Syndicat des Vignerons. *"If you see a very good flowering, that means that you are going to get some good grapes."*

However, early budbreak can be dangerous in an area which is still on the margins in climatic terms for viticulture. *"We have the same problems with spring frosts as xx years ago,"* admits Le Brun. *"Each year, we see that we are really on the edge, we are very close to a disaster in the spring."*

This risk is intensified when combined with another change to Champagne's climate: the onset of more *"violent"* weather, with longer and more pronounced heat spikes in summer, as well as more rain and hail storms.