



WINE COUNCIL
OF ONTARIO



PRESENTATION TO THE STANDING COMMITTEE ON GOVERNMENT AGENCIES

Wine Council of Ontario

Ed Madronich, Chair

Hillary Dawson, President

June 25, 2012

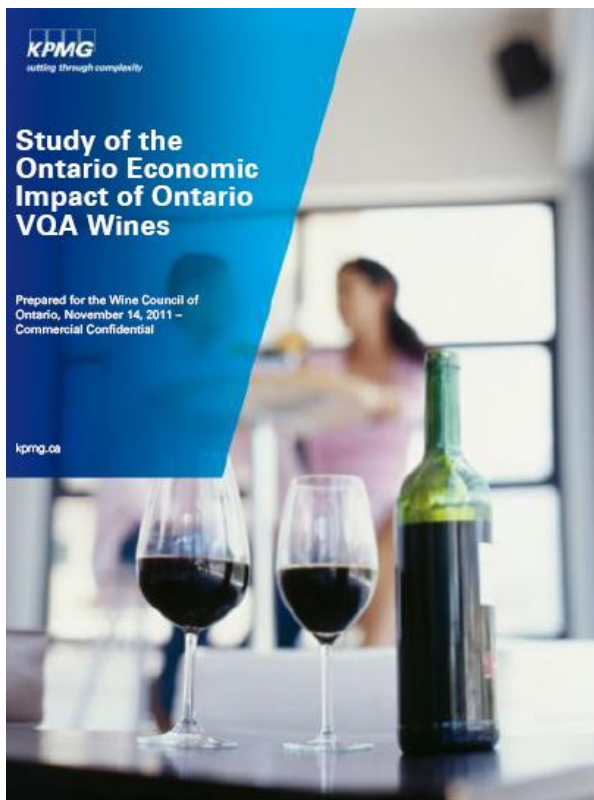
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WHO WE ARE

- ◉ The Wine Council of Ontario (WCO) is the champion of Ontario's high quality, authentically local Vintner's Quality Alliance (VQA) wines and of promoting wine country as a destination.
- ◉ As a non-profit trade association, WCO represents 80-plus wineries from across the designated viticulture areas of the province . We represent the vast majority of commercially active wineries in the province.
- ◉ Within the marketplace where all wineries are able to participate WCO members represent 75% of Ontario wine sales.
- ◉ Our members are small and medium sized enterprises - they are grape growers, manufacturers and leaders in tourism in their communities. We are leaders in manufacturing and investment across rural Ontario.
- ◉ Our members are the future of Ontario's wine industry, which is a source of new investment,
- ◉ The Wine Council of Ontario promotes the unique qualities of Ontario's locally grown wines through its consumer facing brand Wine Country Ontario.
- ◉ We believe that wine can be and is a powerful tool for enhancing our culture and our Ontario brand.



WHY SELLING VQA WINE IS IMPORTANT....



- Ontario wineries are unique in today's economy.
 - As vertically integrated businesses we create agricultural, manufacturing, professional, retail/tourism and construction employment.
- This fact has been validated by a KPMG analysis reinforcing the broad scope of the impact across all elements of our business on the Ontario economy
 - **1300 incremental jobs** in the past 4 years
 - **Value add of \$191 million** in fiscal year ended March 31, 2011
 - KPMG observed that VQA wines were growing economic impact where other industries were status quo
- ▶ **\$12.29 of valued added impact per litre of VQA wine sold**
 - Over and above taxation
 - Up from \$11.50 in 2007
- ▶ **Clearly there is value to getting this wine to market and realizing the benefits of this wine to the economy, the next question is how and where**



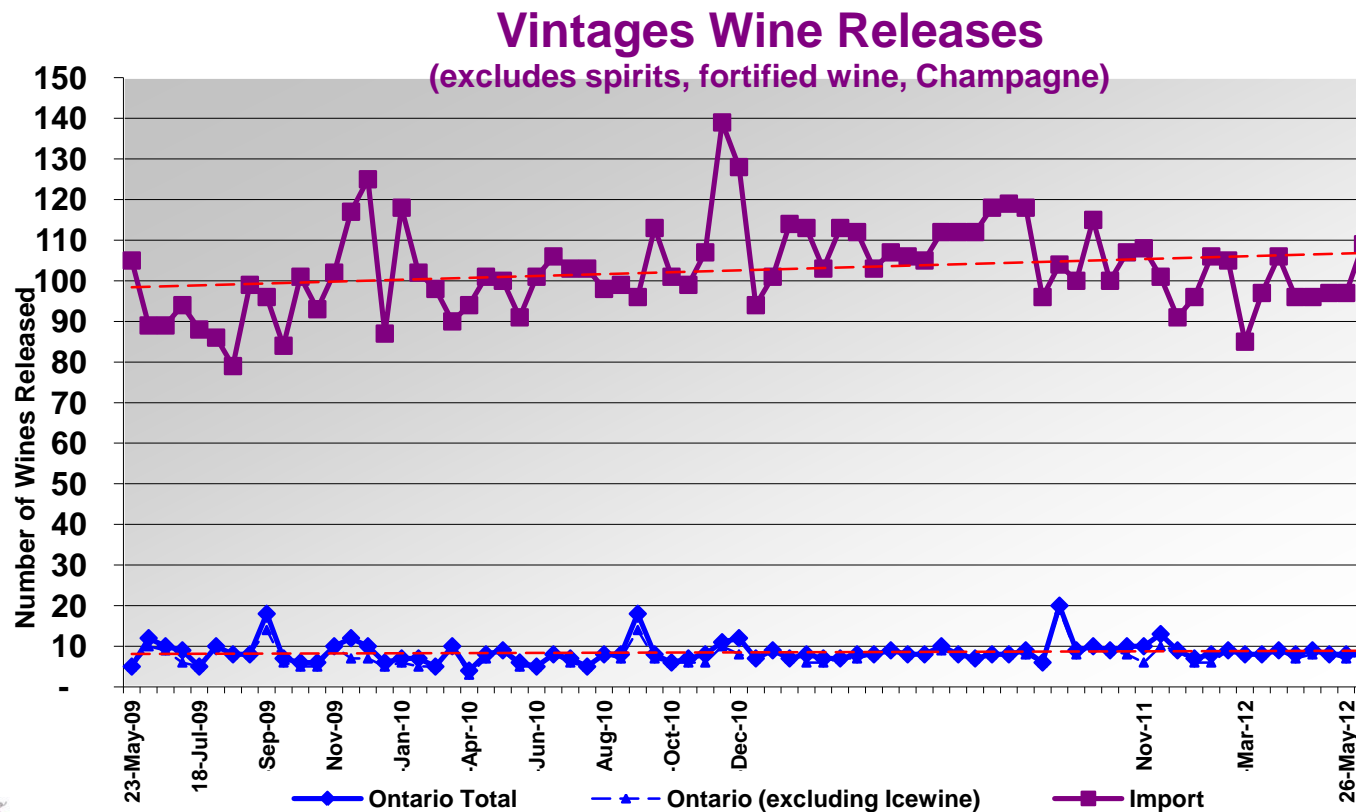
THE CHALLENGE - ENSURING OUR WINE HAS A MARKETPLACE AND OUR WINERIES CAN CONTINUE TO GROW AND THRIVE

- Analysis tells us that we have 500,000 cases of commercially viable wine that will need a market over the next 3 years
 - Over and above those that can be accommodated by forecast growth in all retail channels (LCBO, Direct Delivery to trade, Export, Interprovincial, Duty Free, Sales at Winery)
 - “Premium” Price Points
 - Why does this matter?
 - 500,000 cases can generate up to \$35 million in direct revenues for the province and generate over \$55 million in additional economic impact as well as causing demand for another 6,400 tonnes of grapes
- In the biggest channel – the LCBO - our ability to maintain or reinvigorate our momentum will be an issue
 - Costs of doing business escalating significantly
 - Systemic challenges in maintaining listings
 - Crisis of success - New product being forced into the system which challenges the shelf space, even with the additional 20%
 - Hard, if not impossible, to get the economies of scale for some growing small – medium size wineries
 - Can't rely on consistent relationship with LCBO as the customer
 - Risky to invest in inventory without other prospects



ISSUE #1 - WE CAN'T GROW BECAUSE OUR ONLY PREMIUM CHANNEL - VINTAGES - IS NOT BUILT TO FILL THE GAP

- ▶ What does the current business look like for VQA ?
 - ▶ 200 releases per year divided amongst 130 commercial wineries
 - ▶ No growth in number of releases even with “aggressive” strategy



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ISSUE #1 - WE CAN'T GROW BECAUSE OUR ONLY PREMIUM CHANNEL - VINTAGES - IS NOT BUILT TO FILL THE GAP

- ▶ What does 500,000 cases look like in terms of the Vintages business?
 - Average Vintages release declining (focus on sell through targets for channel) – one time releases, no opportunity to build business consistently
 - Clear message to industry to expect less volume for orders not more from the buyers
 - At an average of 125 cases per order, unlikely that Vintages could release all of this volume of wine
 - **Would mean 4000 releases – currently VQA has 200 per year**
 - Opportunity to distribute is limited
 - 5 stores (1500-2000 skus each), 62 Boutiques (800-1500 skus), 147 corners (50-800 skus)
 - No planogram, no measure of linear feet of product, no accountability of Product Consultants to buyers/sales
 - Almost impossible to plan and execute a significant growth strategy in this channel
 - **Our most successful wineries are having their least successful years in Vintages – that is concerning for the future of our premium business**



ISSUE #2 - WE CAN'T GROW BECAUSE OUR VOLUME DRIVEN CHANNEL - LCBO WINES - CAN'T ACCOMMODATE VOLUME OR PRICE POINT

- ▶ LCBO Wines Channel more able to accommodate volume, but not premium pricing
 - Only 4.8% of sales in this channel are priced over \$15
- ▶ On average, distribution is around 200 stores per sku (very few have distribution throughout the system)
- ▶ Sales performance takes time
 - Wines to Watch program (expectation that over 1000 cases in 3rd year)
 - Best performing skus sell 5,000-7,000 cases in red and 6,000-10,000 cases in whites
- ▶ Shelves are full
 - Challenging to keep listings
 - Constant craving for “new” from the buyers – churn and burn approach does not favour brand building and has helped generate some of this new pressure – need for new brands as well as supporting existing performers



CONTRAST THIS LACK OF OPPORTUNITY WITH BC

VQA Wine Sales - LCBO vs. BCLDB

Rolling year ended 30-Apr-12	Volume (9 L cases)	Number of Brands	Case volume per Brand	Population (millions)	# of Brands per 100,000 pop	Case Sales
Ontario						
Red	358,579	269	1,333	13.4	0.45	629.9
White	455,767	307	1,485			
Rosé	29,655	33	899			
	844,001	609	1,386			
B.C.						
Red	381,553	499	765	4.60	2.36	1,943.1
White	483,666	502	963			
Rosé	28,623	86	333			
	893,842	1,087	822			



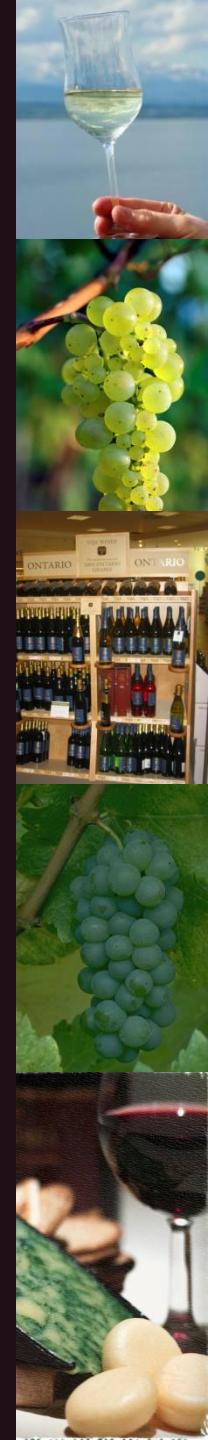
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ISSUE #3 - THE GROWING COSTS OF DOING BUSINESS AT LCBO ARE IMPACTING MARGINS AND PROFITABILITY

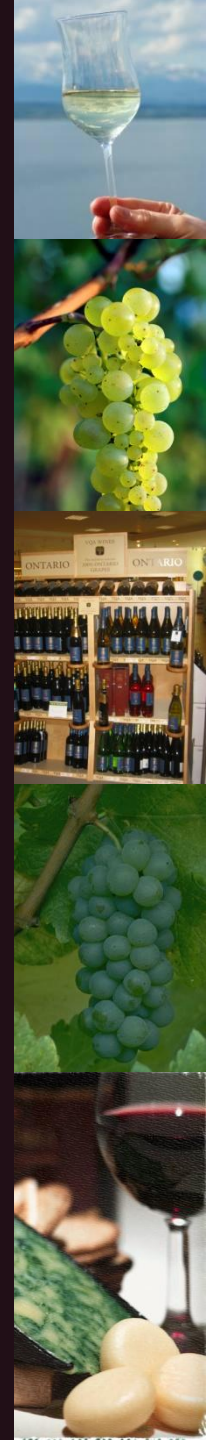
- Pressure on the LCBO to increase returns to government has incited them to aggressively raise fees to all suppliers
- For VQA producers these increases are now effectively eroding the support from the VQA support program
- Many programs designed to support VQA (and very successful) now have significant fees

Winery Revenue for Sales through LCBO FOR 3,000 CASES (2 SKUs at quota of about 1,500 cases per year)		
	April 2010	April 2012
Winery Revenue from sale to LCBO	\$ 204,664	\$ 211,177
Display Merchandising Costs:		
End Aisle	13,333	13,333
Fridge Space	-	13,625
1 Pod display for 1 period per year	-	6,775
Shelf Extender	13,000	13,000
Superstars	-	3,000
Support Merchandising Costs:		
\$1.00 LTO	1,900	3,100
Bonus Air Miles (BAM)	2,325	3,693
1 FSI per year	7,000	9,200
1 shelf talker for 1 period per year	500	700
Other Program Costs:		
Tasting Fees	5,250	6,400
Shopping Cart	-	?
Total Merchandising Costs:	\$ 43,308	\$ 72,826
Offset by 30% VQA support - assumed full support:	61,399	63,353
	18,091	(9,473)
Incremental Cost		27,564
OTHER - charges for Sale of Data information:		Up to \$35,000



BALANCING NEEDS AND LEVELING THE PLAYING FIELD

- ◉ Our analysis is clear on a some key things:
 - Simply opening more LCBO stores will not address our issues – same problems, just more stores to deal with
 - LCBO reviews and collaboration, which have been significant, are only generating marginal changes, if any at all
 - Unless there is a substantial shift in the way the LCBO does business, there is no ability for the existing system to accommodate the wine that needs a market
 - Especially a significant volume which is premium priced
 - We will be challenged to continue to be price competitive in the way that the LCBO would like
 - We will continue to fall behind our competitors who have far more favourable home market opportunities and programs
 - California – 60% advantage
 - BC – significantly more opportunities for wineries to list and consumers to buy



REFOCUS LCBO ON SUPPORTING VQA WITH PROGRAMMING

- Pressure from government for revenue has caused significant growth in fees including new charges for programs designed to support VQA wines
- Recommend rolling back charges for VQA on programs that are designed to support results for VQA and that were previously without cost
 - Superstars, Fridge Space, Tasting Program fee increases as examples
 - We would support LCBO reducing the level of supports that are focused on channels where all wineries are not able to participate as a way to grow revenue to reduce the pressure on these critical programs
 - Benefits to ICB wines , benefits focused at off site retail stores, programs for imports
 - **Incremental dollars gained gives LCBO some flexibility in how to deliver savings to government versus universal pressure on all suppliers**



OUR APPROACH - PRIVATE WINE SHOPS

- ◉ We have proposed to government that they need to look beyond the LCBO to diversify access points for the consumer and drive revenue for the province
 - In line with the retail models in other provinces, especially those with wine producing regions (NS, BC, Quebec)
- ◉ Framed our approach in a way that aligned with the government's priorities
 - Responsiveness to the marketplace and consumer demand
 - Lessening the burden of capital costs on the public purse
 - Propose solutions that appreciate the potential for economic development and driving value into the economy
- ◉ Supported the analysis with research and support
 - Public opinion research
 - Retail store analysis – Grant Thornton LLP
 - Legislative, Regulator and Trade Review – Fraser Milner Casgrain



CONCLUSION - IMPORTANT TO GROW VQA AND ENCOURAGE SOLUTIONS THAT ARE VIABLE

- ◉ The challenges for VQA wines clearly can be focused on improving the opportunities for growth, profitability and leveling the playing field.
- ◉ We have 500,000 cases of wine to sell over and above forecasted growth
 - Priced at premium price points
- ◉ The LCBO does not seem poised to accommodate this growth, though they are making significant efforts to do so
 - System not set up to accommodate our domestic market in the same way that BC seems to be
 - Costs are further challenging our home team – the makers of 100% authentically local VQA wines – to be successful in their only retail channel
- ◉ We are committed to finding any solution that can deliver
 - Increased government revenues
 - Accelerate growth and profitability of Ontario wineries
 - This necessarily will be mean demand for more quality, high value grapes
 - Greater selection for Ontario consumers
 - Generate more employment in key areas of the province
 - Within the greenbelt and areas with declining manufacturing
- ◉ For us this helps VQA wineries support their goals on growth, profitability and helps level the playing field for our wineries that do not have access to a private retail network

