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MULTINATIONAL FIRMS IN THE WORLD WINE INDUSTRY: AN INVESTIGATION INTO THE DETERMINANTS OF MOST-FAVOURED LOCATIONS

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Multinational firms in the world wine industry: an investigation into the determinants of most-favoured locations

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Abstract:

The objective of the paper is to identify some of the determinants of foreign investment of the largest multinational enterprises (MNEs) operating in the wine industry. The list of the largest MNEs has been compiled using financial databases and company websites.

The results of this study have some important implications. They indicate that location-specific advantages of host countries i.e. do provide an explication of the internationalization of firms in some preferred countries rather than others.

Keywords: Wine production, Globalization

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1. Introduction

The wine industry is a growing sector of the world economy and although of minor importance for statistics on foreign direct investment (FDI), the potential for globalization and trade has expanded rapidly in recent decades. As explained by Coelho and Rastoin (2004), there has been a continuous globalization of the world market place for wines which has led to a major restructuring of the largest wine operators into multinational enterprises (MNEs).

In response to foreign market opportunities made available by deregulation and globalization, many firms have increased their foreign direct investment and acquired other companies in part because of the belief that only very large players will have the cost advantages necessary to remain competitive in emerging global markets. Moreover, since the late 1980s, New World wine producers have emerged as significant players in the global wine market. At the same time, the traditional wine-producing regions of Europe, saddled by EU regulation, have struggled to adapt to changing market conditions.

International diversification is a growth strategy that has a major impact on firm performance. This relationship has been studied extensively in the international strategy literature (Capar and Kotabe, 2003). The reduction (or elimination) of barriers to trade has been a major factor in the expansion of MNEs abroad. Firms with strong competencies that are developed at home can utilize these in international markets (Bartlett and Ghoshal, 1989) to generate growth. One of the important questions in international business research is where and why firms invest in specific activities in specific locations. The literature on the locational preferences has long acknowledged the use of a location as a source of competitive advantage (Nachum and Zaheer, 2005; Porter, 2000) but also that these will mainly depend on the motives for investment, i.e. market-seeking, asset-resources seeking and efficiency-seeking (Dunning, 1998). Despite a resurgence in interest in the geographic or location aspects of international business in recent years (Enright, 2009), there is to our knowledge no empirical work that focuses on the location of investment in the beverage sector.

Thus, this paper has two objectives. The first is the documentation of the relative importance of the largest firms in the world wine market. The second objective is to examine where firms are expanding their operations, list the most-favoured locations, and identify some of the determinants linked to the location-specific advantages of some host countries.

First, this paper reviews the growth of the international market. Market growth, exports and imports are important factors to be considered when looking at investments of the largest firms. Second, a list of wine multinational firms (MMEs), based on several sources of information, is proposed, and analyzed. Third, drawn from this list, a sample of the most-favoured locations for affiliates of these firms is presented. Finally, we examine some of the factors that may explain the choice of these locations by multinational firms.

2. The world wine market

Wine is a global business (Orth et al., 2007, Coelho and Rastoin, 2004). Growth in supply is driven by the new wine producing regions and global demand is mainly being driven by a shift in consumers' preferences and lifestyles in some key markets, such as the United States and the United Kingdom, or by new consumers in emerging markets, such as China or Russia.[1]

2.1 Production and consumption

According to the International Organization of Vine and Wine (OIV), the 1986-1990 period was characterized by a sharp decrease in world wine production, a trend which only reversed in the mid-1990s when production increased, though at levels below those of the mid-1980s. In 2006-2007, the principal wine producing countries remained in Western Europe although their share globally has decreased slightly in favor of the new-world producing regions (South America and Australia/New-Zealand) since the 1986-1990 period (table 1).[2]

[1] See Anderson (2004, chap. 2).
[2] OIV, World Statistics, www.oiv.org. Latest information available on the web site is for the 2006-07 period.

A similar pattern is observed in world wine consumption, where Europe is by far the continent with the highest consumption. Not surprisingly, the highest levels of consumption are traditionally found in countries that are also among the leading producers, though there has been a downward trend in the individual levels of consumption. In new wine-producing countries, where production has increased over the past ten years, consumption has progressed at a slow pace. Finally, in non-wine producing countries (or those with little production), the trend generally has been one of growing individual consumption. These long-term trends are crucial drivers for the global trade in wine.

Table 1: World production of wine by regions and by periods

Region	2006-2007	1996-2000	1986-1990
Western Europe	57.6	62.1	62.7
Eastern Europe	5.8	7.6	9.9
Ex-USSR	4.7	3.4	5.4
North America	7.7	8.1	6.7
South America	10.3	8.3	9.2
Australia/N.Zealand	4.8	2.9	1.6
Asia	5.0	4.3	1.5
Africa	4.1	3.3	3.0
Total	100.0	100.0	100.0
Source: OIV, World Statistics 2007, www.oiv.org			

2.2 Foreign trade

According to OIV, foreign trade in wines, considering the world market as the sum of exports for all countries, grew at an average annual rate of 5.8% over the period 2001-2006 and even faster from 2006 to 2007 (+6.8%). The world trade in wine accounted for 36.2% of the world consumption in 2007, a strong increase compared to the 18.2% average between 1986 and 1990.

Although its share of the world market is decreasing, in 2006-2007 Western Europe remained the leading region for both imports and exports in terms of world market share (table 2). Leading wine importers, i.e. Germany and the United Kingdom, have largely maintained their share of the world market over the past ten years. Other non-producing

European counties -- the Netherlands, Poland, Sweden and Finland -- have seen their consumption increase considerably over the same period, boosting their imports.

The dominance of Western Europe in imports is being challenged by a number of countries and regions. For example, the United States of America is the third largest wine importer, accounting alone for nearly 10% of global wine imports in 2007. Consumption of wine (and by implication imports) increased more than 150% in Russia and 125% in the Ukraine over the period 2000-2007, boosting their shares in world imports. In Asia, rising consumption in China – in contrast to relatively flat imports by the region's largest importer, Japan – has been the primary driver of growing imports in the region.

Similarly, Western Europe's dominant share of the world wine exports is decreasing, even though Italy, France and Spain – in that order – remain world leaders. Other European countries like Germany and Portugal have also experienced significant increases in their exports. However, other regions have experienced rapid growth during the decade. South America, for example, is the fastest growing region for exports (+22% in 2007 over 2006), lead by Chile which is the 5th largest exporter in the world. Australia and New Zealand have also significantly improved their export performance during the decade.

Table 2: World imports and exports by regions, share of the world market.

Period	2006-2007		1996-2000	
Region	**Imports**	**Exports**	**Imports**	**Exports**
Western Europe	59,8	65,8	69,7	73,8
Eastern Europe	4,8	5,4	2,9	6,5
Ex-USSR	9,7	0,3	5,0	3,7
North America	13,9	4,6	11,1	3,8
South America	2,3	10,2	2,1	5,6
Australia/N.Zealand	1,1	9,7	1,1	3,7
Asia	5,4	0,4	5,2	0,6
Africa	3,0	3,6	2,9	2,3
Total	100,0	100,0	100,0	100,0
Source: OIV, World Statistics 2007, www.oiv.org				

3. The world's largest MNEs in the wine industry

Globalization impacts markets in terms of the concentration of production and consumption at the international level (Coelho and Rastoin, 2006). In the case of wine, production remains highly segmented and fragmented but there has been significant consolidation of production units and ownership in the past decade, with some MNEs becoming major actors in the production and distribution of wine around the world.[3] This globalization of the wine industry has occurred hand-in-hand with the emergence of specialized wine funds created by institutional investors early in the 2000s (Coelho and Rastoin, 2006). While important in their own right, these funds are not part of our analysis.

The list of the largest groups has been selected using Orbis and Thomson Financial data and inspired by the list compiled by Coelho and Rastoin (2004). Data is reported for 2009. Most of the groups have diversified activities in wine, spirits and/or beer and a few are specialized in wine only. When available in annual reports in the company's websites, it is possible to estimate the share of the wine business in the portfolio, total assets, total sales, total number of employees and the foreign components of these variables. Information for private family-owned groups is generally not available, though Freixenet (Spain) provides information on the number and location of host countries for their affiliated companies. Major cooperatives are excluded from the list. Although some of these entities may be big in terms of foreign sales, they are not generally multinationals and have not established affiliates in foreign countries.[4]

The listing of the 15 largest companies ranked by total sales in the wine sector (table 3) provides information on the percentage of wine business in the portfolio of the group (wine being defined as still wine, champagne and sparkling wines), total sales and the percentage of foreign sales. The list includes 9 groups from Europe, 2 from the United States and 4 from new world of wine producing countries. Only four of these groups are specialized in the wine business (100%) and all other groups have diversified activities in the beverage industry.[5] Some large groups like Diago are only marginally involved in the wine sector.

Empirical work on the role of FDI in host countries also suggests that FDI is an important source of capital, complements domestic private investment, and contributes to

[3] According to Heijbroek (2003), the concentration of the top firms in the beverage industry was as follows: wine (7%), spirits (25%), beer (28%) and soft drinks (80%).
[4] The complete list of groups is available from the authors
[5] For LVMH, only the wine and spirits division has been considered.

economic development and transfer of technology. Unfortunately, the wine industry is of minor importance for statistics on FDI and very few information is available on the channels of investment (M&As or Greenfield investment). It is therefore necessary to look at the geographic distribution of multinational companies operating in this sector to understand the relevant foreign investment trends.

The degree of international involvement of a firm can be measured in various ways. One such measure is transnationality, which is a function of the extent to which a firm's activities are located abroad. From the operations perspective, key dimensions include the intensity or relative importance of foreign operations, as measured by various variables including the geographical spread of its operations. This can be examined in a number of ways. One approach is to examine the intensity of foreign operations according to the number of foreign affiliates. Another potential angle to examine is the number of host countries in which a company is established. A high number of host countries may indicate a significant level of ownership advantages as well as high knowledge of market conditions across diverse markets. However, it does not take into account the magnitude of a company's activity in a given host country.

Table 3: Largest international players, total sales in the wine sector, 2009, US$

Rank	Company	Home Country	% Wine in the portfolio	Total sales in wine sector	% of foreign sales
1	Constellation Brands, Inc.	United States	87.0	2928,0	41.1
2	LVMH Moet Hennessy Division	France	(a) 47.0	1790,0	91.0
3	Pernod Ricard S.A.	France	20.2	1750.2	89.8
4	Foster's Group	Australia	42.3	1415.9	35.0
5	Diageo PLC	United Kingdom	6.0	877.2	87.2
6	Sektkellerei Henkell & Co AG	Germany	80.0	699.0	48.3
7	Vina Concha y Toro S.A.	Chile	100.0	643.0	70.6
8	Distell Group Limited	South Africa	(b) 40.0	615.6	25.2
9	Belvédère Group	France/Poland	44.8	397.0	40.8
10	Brown-Forman Corporation	United States	12.4	396.0	53.0
11	Sektkellerei Schloss Wachenheim AG	Germany	100.0	391,3	67.0
12	Vranken-Pommery Monopole	France	100.0	386,3	45.2
13	Davide Campari-Milano S.p.A.	Italy	15.4	222.3	61.5
14	Australian Vintage Ltd.	Australia	100.0	199.9	54.9
15	Société des Produits Marnier-Lapostolle / Grand Marnier	France	9.0	15.2	93.6

Notes:
(a) Division of wines and spirits accounted for 16.1% of all sales for the group. Value for wines is estimated from the brands distribution.
(b) Value estimated from the brands distribution

To examine these aspects of transnationality, Table 4 gives a list of the 21 largest MNEs ranked by the number of foreign host countries in which these groups have at least one affiliated majority-controlled company or subsidiary. In 2009, the top 5 companies have an average number of host countries (21) significantly higher than other companies in the list. These 5 groups have on average 54 affiliated companies, of which almost 70% located in foreign countries. France has the largest number of companies ranked in the list (8) and overall Europe has 13 out of 21. The United States (3), Australia, Japan, Chile and South Africa complete this list.

Table 4: Largest MNEs ranked by number of host countries

Rank		Company	Home Country	Nb of host countries	Nb of affiliates or subsidiaries	% of foreign affiliates
1		Brown-Forman Corporation	United States	26	45	73.3
2		Pernod Ricard S.A.	France	25	97	86.6
3		Freixenet S.A.	Spain	20	34	58,8
4		Davide Campari-Milano S.p.A.	Italy	17	30	80.0
5		Belvédère Group	France/Poland	16	65	49.2
6		Foster's Group	Australia	11	40	35.0
7		Diageo PLC	United Kingdom	10	11	81.8
8		Sektkellerei Henkell & Co AG	Germany	9	15	60.0
9		Vranken-Pommery Monopole	France	9	26	53.8
10		Kirin Holdings Company, Limited	Japan	9	33	39.4
11		Vina Concha y Toro S.A.	Chile	7	23	43.5
12		LVMH Moet Hennessy Division	France	7	n.a	n.a
13		Constellation Brands, Inc.	United States	6	42	59.5
14		Sektkellerei Schloss Wachenheim AG	Germany	6	47	40.4
15		Distell Group Limited	South Africa	6	n.a	n.a
16		AdVini (JeanJean/M.Laroche)	France	6	27	29.6
17		Société des Produits Marnier-Lapostolle / Grand Marnier	France	5	n.a	n.a
18		Central European Dist. Corp.	United States	3	n.a	n.a
19		Australian Vintage Ltd.	Australia	2	29	10.3
20		Henri Maire	France	2	13	15.4
21		Laurent-Perrier	France	2	n.a	n.a
Note:		n.a: Not available				

It could be argued that some of these groups are only marginally involved in the wine sector. This is particularly the case of Kirin holdings, a major Japanese beer player that has recently decided to expand its activities in the wine sector. Unfortunately it is not possible to differentiate a subsidy (or affiliate) for wine and a subsidy (or affiliate) for beer or spirits. Although the share of business generated by wine is still marginal, the group will use its network of affiliated companies in several host countries to expand operations, products and compete with other established players.

3.1 The international presence of the largest MNEs

Data for the most preferred locations by these groups listed is constructed by counting the number of host countries and affiliates in those countries for each of the 21 groups. This analysis gives a list of 30 countries for which at least two wine MNEs have an office. While interesting, ranking the host countries by the number of groups with affiliates in the country or by the total number of foreign affiliates does not give a correct picture because the country of origin of a group prevail that country to be considered as a host country. A more correct measure is a country's location intensity (LI), which is defined as the number of wine groups having at least one affiliate in the country, divided by the total number of groups in the sample minus the number of groups of the country of origin.[6]

The ranking of countries is by location intensity (first factor) and then the number of foreign affiliates. It shows that the United States is the most popular location, followed by France and the United Kingdom (table 5). The activities of the largest wine groups are highly concentrated in only a few countries. Most of these countries, with only a few exceptions (Poland and Nordic countries), are wine producing countries.[7] All the major countries in terms of wine consumption are also present in this list. There are, however, notable exceptions of countries that are not listed in the preferred locations although they are relatively important both in producing and consuming wine, such as Austria, Hungary, Croatia, Georgia and Uruguay.[8]

Table 5: The most-preferred locations of wine MNEs ranked by location intensity

[6] For example, The United States is a preferred location for 11 groups divided by 18 (21-3 groups housed in the US), and France is a preferred location for 7 groups divided by 13 (21-8 groups housed in France).

[7] Even if production is marginal like in the UK, The Netherlands or Japan.

[8] See Anderson (2004).

Rank	Host country	Location intensity	Nb of groups	Nb of affiliates
1	United States	61.1	11	20
2	France	53.8	7	12
3	United Kingdom	50.0	10	26
4	Australia	47.3	9	29
5	Germany	42.1	8	8
6	Canada	38.1	8	18
7	China	38.1	8	16
8	Poland	35.0	7	15
9	Italy	35.0	7	8
10	New Zealand	33.3	7	16
11	Brazil	33.3	7	9
12	Switzerland	33.3	7	8
13	Japan	30,0	6	7
14	Argentina	23.8	5	11
15	Czech Rep.	23.8	5	9
16	Mexico	19.0	4	9
17	Sweden	19.0	4	6
18	Finland	19.0	4	4
19	Belgium	19.0	4	5
20	Spain	15.0	3	8
21	Chile	15.0	3	5
22	Russia	14.3	3	6
23	Portugal	14.3	3	5
24	Ukraine	14.3	3	5
25	Greece	14.3	3	4
26	Netherlands	14.3	3	3
27	Slovakia	14.3	3	3
28	South Africa	10.0	2	3
29	Bulgaria	9.5	2	7
30	Romania	9.5	2	3

4. Determinants of international presence

The factors that drive firms to invest abroad and those that determine the location of those investments are the subject of an extensive literature. For example, many studies have looked at the relationships between FDI and the characteristics of recipient countries (Green and McNaughton 1995, Galan and Gonzales-Benito, 2001, Javalgi et al., 2003; Rugman and Verbeke 2004). Recent work has also sought to make use of Bayesian analysis to determine the primary factors that determine the location of investments (Blonigen and Piger, 2011). While a comprehensive literature review is out of the scope of this paper, a basic examination of the theoretical framework will serve to ease the examination of the determinants of wine FDI.

The concept of eclectic or OLI paradigm explained by Dunning (1977) and updated in later work (Dunning 1988, 1995) was put forward to identify and evaluate the significance of factors explaining the activities of large groups outside their national boundaries. A framework developed by UNCTAD (2006) and based on the work of Dunning, categorizes the forces working on multinational firms as "push" and "pull" factors. Push factors, or drivers for internationalization, cover elements such as market and trade conditions, costs of production, local business conditions, and home government policies. For example, a limited or saturated home market serves to push firms to expand abroad to exploit opportunities in other markets. Pull factors, also called locational determinants, serve to attract investors. These determinants are further subdivided by the various motivations of investors for entering a particular market: market-seeking (looking for new customers), resource-seeking (accessing key factor inputs), efficiency-seeking (reducing production costs), and strategic-asset-seeking (acquiring new technologies/brands) (Dunning and Lundan, 2007).

4.1 Determinants of wine FDI

A priori, the locational determinants of FDI in the wine industry are likely similar to those in other industries. Demand-side features such as market size and growth influence the potential sales in the market or the region (Agarval and Ramaswami, 1992; Sethi et al., 2003; Flores and Aguilera, 2007). Factors like the level of socio-economic development, the level of country risk, and the openness of an economy to trade have been shown to be positively related to foreign investment (Grubert and Mutti, 2000). Supply-side features focus on the quality of infrastructure and capabilities found in the host country, as well as the quality of inputs (Woodward and Rolfe, 1993; Kuemmerle, 1999).

Wine FDI, on the other hand, is not homogenous in nature and the motivations for entering a particular market are different for each investor. Thus, to uncover the factors that influence the choice to establish a foreign affiliate in a particular country this study makes use of a statistical validation of location-specific variables using location intensity as its dependent variable. A similar approach was suggested by Outreville (2007). Location variables considered are specific to the role and importance of the production and consumption of wine in the host country.

The size of the host economy influence FDI decision. To verify the effect of the size factor, Spearman rank correlations are calculated with GDP per capita and the size of the population. The size of the potential business is measured by wine consumption and wine imports in the country. Labor is another important factor to foreign investors. Thus a high level of human capital would positively attract foreign firms. The human resources base is generally measured by educational enrolments and literacy rates.

4.2 Spearman rank correlations

Spearman rank correlation values are calculated between the ranking of the location intensity of host countries and the ranking of the independent variables or indices for the same period. Results of Spearman rank correlations are presented in table 6. To verify the effect of the resource-seeking, wine production and the level of exports of the country were selected as possible variables. Both show as expected a positive sign but a low degree of statistical significance.

For market-seeking variables, the size factor is represented by the average GDP per capita over 2007-2009 and the size of the population in 2009. Both variables show as expected a positive sign, slightly more significant. Variables related to wine consumption in the country were also selected for the analysis. Wine consumption is significantly correlated with our dependent variable but the result is questionable when considering consumption per capita and consumption growth which are both non significant. It is important to note that imports in the country are the most significant variable in our analysis. This is typically a market-seeking activity of foreign groups entering markets to sell their (imported) goods) to a population that already has a taste for wine.

Looking at efficiency-seeking, the only available variable that we have verified is human resource development. Labor is another important factor to foreign investors. Thus a high level of human capital would positively attract foreign firms. The human resources base is generally measured by educational enrolments and literacy rates. The Human Capital Index used in this study is a weighted average of the literacy rate and enrolment ratios (secondary school and tertiary education). Results of Spearman rank correlations show that one of the highest correlations is with the human capital variable. However it could be argued that this variable is proxying for the presence of sophisticated consumers rather than the quality of labor. In that case it would be a market-seeking variable.

Table 6: Spearman rank correlations between location intensity and determinant variables

	Rho	P-value
Resource-seeking variables		
Wine production	0.173	0.361
Wine exports	0.127	0.504
Market-seeking variables		
Population	0.382	0.0373
GDP per capita	0.399	0.0289
Wine consumption	0.408	0.0251
Consumption per cap.	-0,040	0.833
Consumption growth	0.138	0.467
Wine imports	0.546	0.0018
Efficiency-seeking variables		
Human Develp. Index	0.456	0.0113

5. Conclusion

This paper documents the relative importance of the largest firms in the world wine market and examines where firms are expanding their operations. A list the most-favoured locations is proposed and is used to identify some of the determinants linked to the location-specific advantages of some host countries.

The results of this study, although limited by data constraints, have two important implications. First, they indicate that location-specific advantages such as size and human development do provide an explication of the internationalization of firms in the wine industry. A shortcoming of this analysis is that other possible determinants of FDI like the relative economic growth of markets or the differential in labor costs or in the cost of capital in the host and home country cannot be investigated.

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