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# WHOSE TERROIR IS IT ANYWAY? COMPARING CHINESE FDI IN THE FRENCH AND AUSTRALIAN WINE SECTOR

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# Whose Terroir is it anyway? Comparing Chinese FDI in the French and Australian Wine Sector

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## Abstract

This paper explores recent developments in outward Foreign Direct Investment (OFDI) from Chinese companies in the wine sector in the Bordeaux (France) and West Australia (WA) regions. The objective is to explore the extent of the phenomenon, which although widely mediatized, has not been the subject of academic scrutiny. As OFDI official figures provide little detail, we undertook primary research in the two regions, in addition to analysis of secondary trade data.

Results indicate that the level of Chinese OFDI is relatively low, although the number and speed of acquisitions, especially in Bordeaux, has attracted attention. The motivations of investors in both regions were: the exploitation of growth in the home market; security of supply; prestige and diversification of risk. In Bordeaux the 'appellation' was a clear motivation, as were the vineyards' historic buildings. A final motivating factor was the wish to avoid the complex supply chains in Bordeaux, by bringing wine direct to the Chinese market. In Australia, cementing existing business relationships, as well as access to Australian residency were specific motivations. Both regions have a relatively open investment climate and no significant investment barriers were noted, although the potential exists, especially as evidence emerges of illegal funding of some investments. We conclude with some directions for future research.

*Key words: Western Australia; Bordeaux; Chinese FDI; Wine.*

## I. Introduction

The objective of this paper is to explore recent developments in outward foreign direct investment (OFDI) by Chinese companies in the global wine sector through a study of its nature and impact in the Bordeaux region of France and Western Australia (WA). Although the expansion of the consumer market for wine in China and increasing Chinese ownership of vineyards in a number of countries has motivated much interest by the media (Neales, 2012; Rabillier, 2012; Sanudo, 2012; Speedy, 2012; Compadre, 2013a; Kelly and Speedy, 2013), it has attracted little academic work to date. This paper will seek to shed more light on the extent of the phenomenon and the motivations of investors.

The wine industry is important to both regions being considered, both directly in terms of employment and foreign earnings and indirectly in terms of its underpinning of tourism and international brand recognition. However, there is rather limited study in either region of the impacts of the recent changes under way in the industry. The wine market is not immune to the increased globalization of the world economy and the shifts in consumption patterns observed in emerging economies, in line with their economic development. In this context, China is an economy where significant future growth in wine production and demand is expected (Anderson and Wittwer, 2013; Thorpe, 2009). Better understanding how this dynamic plays out at the local level is important to the development of future strategies for the industry.

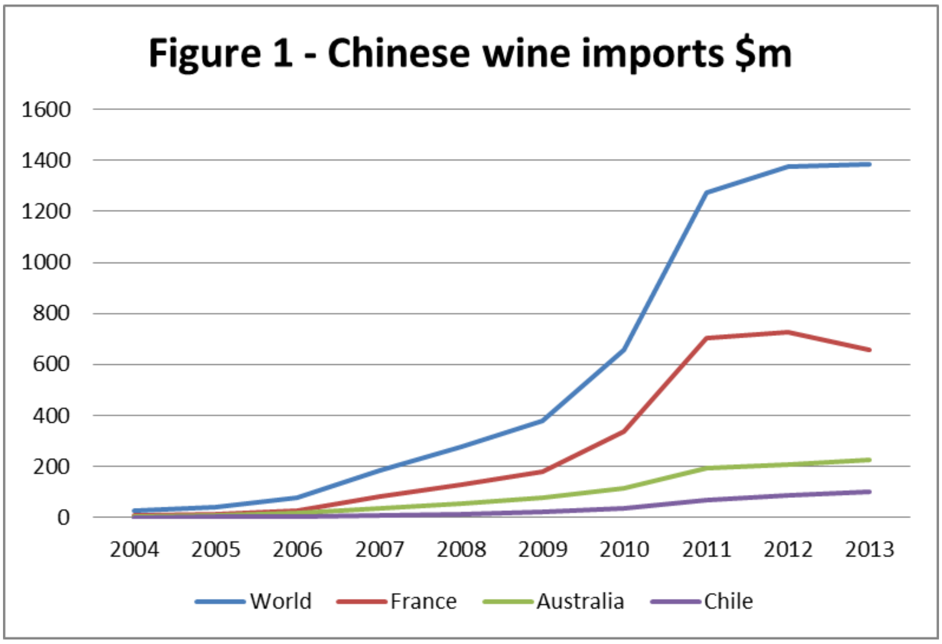
Bordeaux and WA have several similarities, most notably they are both known mainly for producing red wine at the relatively high end of the market. However they also have important differences, especially in relation to their levels of integration with the global economy. WA wine is relatively new to the Chinese market and indeed to export. Bordeaux is a much more established exporter, including to China and the number of investors there is higher. It also has a long history of FDI in wine, unlike WA (Chen, 2014). We wish to explore these similarities and differences and highlight what lessons might be learnt from experience in the different contexts.

The paper is structured as follows, section II details recent evolutions in the Chinese wine market and provides an overview of existing research on that market, while section III explains our methodology. Section IV draws on secondary trade and investment data to provide an indication of the importance of China for the two regions on which we focus, and explains the policy context which governs trade and investment in both. Section V discusses our findings from fieldwork in WA and Bordeaux in relation to the extent of FDI, the key motivations for Chinese investment in the sector and its impact on the local industry. Section VI draws some key conclusions and highlights further areas for research.

## II. The context - the growing importance of China in the wine sector

As China has emerged as an important wine market, research has begun to address its role as an actor in the world market. There is some limited research on the development of the Chinese wine sector (Jenster and Cheng, 2008) and the domestic market (Lee et al. 2009; ABARES, 2012). Other studies have focused on the impact of emerging Chinese demand on the world market. These indicate that the rapid growth of Chinese consumption will make it an increasingly vital global market (Anderson and Wittwer, 2013; Banks and Overton, 2012; Thorpe, 2009). This is also because this increase in demand in China is happening against a backdrop of long term falls in wine consumption globally, especially in traditional markets. In France for example, the annual average consumption fell from 104 liters per person in 1975 to 47 in 2011. While China was still only at the level of 1 liter per person in 2011, this was up from 0.3 liters in 2003 (FranceAgriMer, 2013).

Expansion of demand in China has inevitably had a major impact on trade (Anderson and Wittwer, 2013; Thorpe, 2009). We will here briefly highlight overall trends before turning to more detailed analysis in section IV. Figure 1 shows the evolution of Chinese imports of bottled still wine since 2004 by value (extracted from the International Trade Centre (ITC) database). The graph shows the very rapid growth of the market from practically non-existent in 2004 - $25m of imports – to a market worth $1.4bn in 2013. Although clearly French wine dominates the market, their imports fell by nearly 10% in 2013, while Australian imports continued to rise (+9%). The exports of the next most important supplier – Chile – are worth less than half those of Australia, but will have an important tariff advantage (of 14%) in 2016, once the full liberalization agreed in the Chile-China Free trade Agreement is applied (Mofcom, 2006).




**Source: ITC Trademap**

Increased demand in China has also fueled investment in the sector, both at home and abroad. Several foreign companies are active in Chinese wine production, including the French companies Remi Martin and Castel (Jenster and Cheng, 2008; Banks and Overton, 2010). What interests us in this paper, however, is outward FDI (OFDI) from China to producing regions. For this purpose, official Chinese FDI figures provide very limited insights. According to the ITC database, in 2011 63% of Chinese OFDI stock (56% of flows) was invested in Hong Kong and another 14.5% (19%of flows) in the offshore financial centers of the British Virgin Islands, the Cayman Islands and Luxembourg. This tendency for FDI to cluster in tax havens, or transit through Hong Kong, is a challenge when seeking to analyse official Chinese figures (Zhang and Daly, 2011; Kolstad and Wiig, 2012; He and Wang, 2014).

These figures do indicate that Australia was the first non-offshore destination for FDI after HK, representing 2.4% of stock (2.5% of flows). France is listed as a marginal destination with only 0.1% of stock at $244m and 26.4m flows (0%). In terms of the sectors where Chinese FDI is concentrated, agriculture is very far from being a key destination. Less than 1% of OFDI stock is in the sector compared to 16% in mining and 39% in the rather vaguely titled sector of ‘business activities’.

a. Research on the Chinese wine market

In line with the development of the Chinese wine market, there have been several studies focusing on their domestic market and especially on the characteristics and motivations of Chinese wine consumers. Liu and Murphy (2007) undertook some qualitative research on the perceptions and motivations of Chinese wine drinkers. They found very limited knowledge of wine in their sample – most did not know that wine could be other than red or that Australia produced wine. This highlights a key challenge for exporters, which is educating consumers about wine (Jenster and Cheng, 2008). Another significant factor identified in Liu and Murphy (2007), was the importance of the Chinese concept of face - 'mianzi' - in wine consumption. The Chinese buy more expensive – usually French – wine on special occasions or as gifts to impress others. Face was also identified by Somogyi et al (2011).

The impact of Country of Origin (COO) on consumer perceptions and behavior has been subject of some research. Balestrini and Gamble (2006) explored how COO, brand and price of wine impact on Chinese consumer behavior. They find that COO is the key defining element in choice, particularly for gifts. Hu et al (2008) reached similar conclusions in their study, where they found that COO was the key defining variable in wine choice for gifts, when foreign wines were favoured. Camillo (2012) found that taste, COO and quality were the most important motivating factors in Chinese consumers' choice of wine .Yu el al (2009) also explored COO in China, where French wine has a considerable advantage over others in terms of consumer perception. It is most popular for a business dinner or a gift, with Australia 4th most popular.

Finally health issues are a key factor in the perception of wine by Chinese consumers. Camillo (2012) found that over half of his sample of Chinese consumers considered that wine, particularly red wine, was a healthy drink. This perception was also mirrored in other studies (Liu and Murphy, 2007; Somogyi et al, 2011)and has been encouraged by government policy which seeks to reorient Chinese drinking from grain based to fruit based alcohols both because they contain less alcohol and in order to prioritise grain use for food (Jenster and Cheng, 2009).

The structure and distribution systems of the Chinese market have also been subject to some analysis. The distribution system was identified as a key difficulty by research in the mid-2000s (Jenster and Cheng, 2008) and this situation has not improved markedly since.

Supermarkets are the key retail outlet for foreign wine, yet the level of choice and the extent to which they stock foreign wines is still low (Lee et al, 2009). The on-trade – restaurants and bars – remains a key distribution outlet for foreign wines (ABARES, 2012; Lockshin, Cohen and Zhou, 2011), however this limits sales. Access to wide-scale distribution systems will be key to developing the Chinese market for imported wine.

## III. Methodology

This research uses a mixed method approach, through a combination of analysis of secondary data and primary data from interviews. The key reason for our use of primary data in this case, is the very limited amount of data available on FDI at sub-sectoral or regional level. Trade data is readily available at high levels of detail, and indeed we draw on this data to give us an overview of the evolution of the market for different countries and regions. FDI flows, however, are much less extensively aggregated. In addition, as indicated above, Chinese FDI is often directed through off-shore financial centers like the British Virgin Islands, or simply through Hong Kong, making official figures rather imperfect indicators of the true destination of investments.

In order to establish the extent and evolution of FDI in the two regions studied, we therefore undertook direct fieldwork. We interviewed the key associations and economic institutions in the regions studied, as well as wineries, investors themselves and local journalists. In all we undertook 20 interviews - 13 in FR and 7 in Australia (see table in annex for details – note some informants preferred to remain anonymous). Interviews were transcribed and translated from French by the authors. Through such direct contacts and analyses of local and national press reports, we established a comprehensive database of Chinese investment in both regions, which gives us a good overview of the extent of FDI. Our interview data also provided us with insights into motivations and impacts of this FDI elaborated in Section V.

We chose to analyze WA and Bordeaux because they were representative of the two key supplier markets to China – France and Australia – and because they have quite contrasting contexts and histories which we hoped would provide interesting findings in terms of outcomes. In addition WA is a region that produces high quality wine. It is not seeking to develop the Chinese market through the mass market, but rather focuses on the luxury end. This premium wine segment is forecast to see increased production in both Australia and France in the near future, in contrast to basic wine, which is forecast to fall (Anderson and

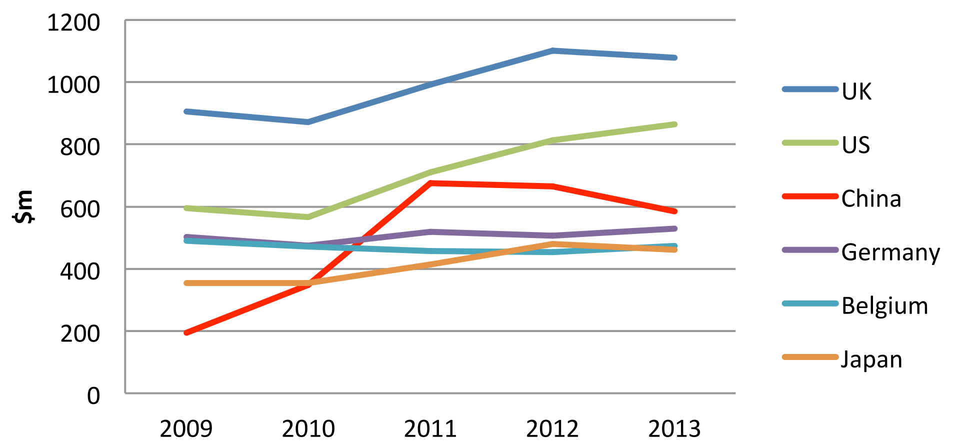
Wittwer, 2013). This premium market is precisely the market where Bordeaux wine excels, commanding the highest regional premiums (Gokcekus and Finnegan,2013).

## IV. The growing importance of China to the Bordeaux and WA wine sectors and their policy contexts

### a. Recent developments in China-Bordeaux wine trade and investment

Trade in wine has experienced quite extensive volatility in recent years. In the French context, Figure 2 below indicates the overall development of still French wine exports by value to the top 6 markets. It is evident that the financial crisis impacted on sales worldwide, although Germany and Belgium saw less marked falls than other markets. Recent research in the US indicates that the financial crisis impacted on both the quantity sold and the quality premium paid for wines from certain regions (Gokcekus and  Finnegan, 2013). As the same research found that three of the top four regional premium wines sold in the US were French, it is unsurprising that the crisis had a significant impact on the value of French exports to the US. Over the time period covered, while the top two markets remained the UK and the US, the importance of China increased markedly up to 2011, although since then there has been a fall, as was already clear from Figure 1.

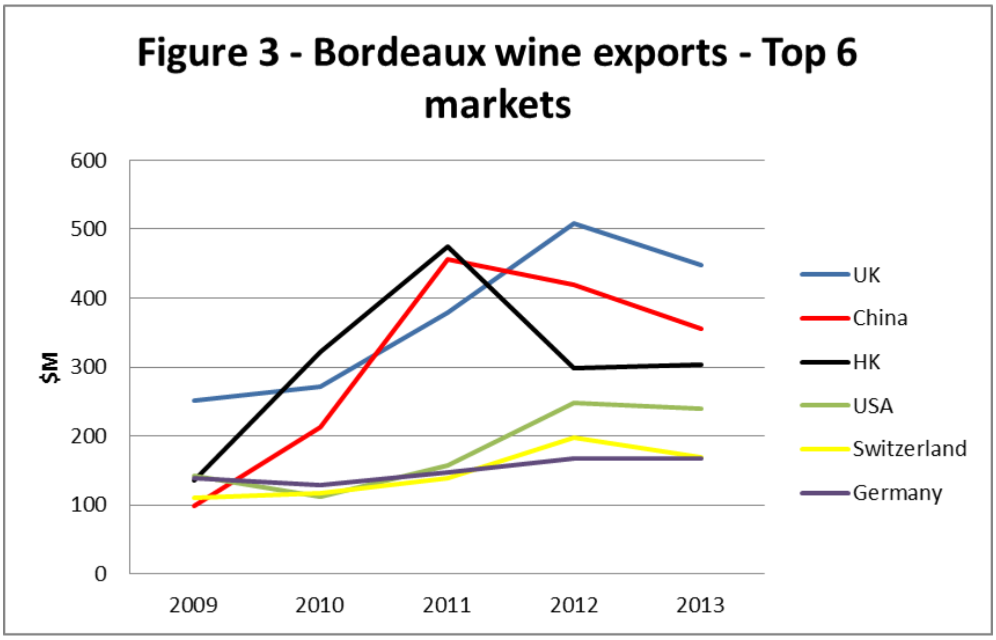
Figure 2 - French wine exports - top 6 markets




Source. ITC Trademap

When considering the Bordeaux region alone, the major export markets differ. Although the UK has historically been the most important market and remained so in 2012 and 2013, Hong Kong and China are becoming very important and have imported more than the UK in certain recent years.  However exports to both are rather variable. Rapid growth of exports between 2009-11 – up by 360% in China and 250% in HK– was followed be large falls - down 22% and 36% respectively since 2011. Informants in Bordeaux, although clearly concerned about the recent falls, felt that they were due, at least in part, to overstocking in 2010-11 when there was much euphoria about the potential of the market. Once these stocks were sold, they were confident that exports would return to previous levels.

However structural changes have also contributed to these recent trends. In 2013, with the change of government in China, a serious effort to address corruption was launched. One of the targets of the new policy was gift giving, which was a very important part of the market for all luxury products, including the type of fine wine in which Bordeaux specialises (Thomson, 2013; Compadre, 2014). Many informants we spoke to for this research indicated that the policy had impacted on the market and that there had been reductions in demand as a result.   This could signal a long term reduction in that important market segment. Indeed some respondents expressed concern about the high level of dependence of some Chateaux on such a volatile market, a concern echoed in the press (Compadre, 2012).



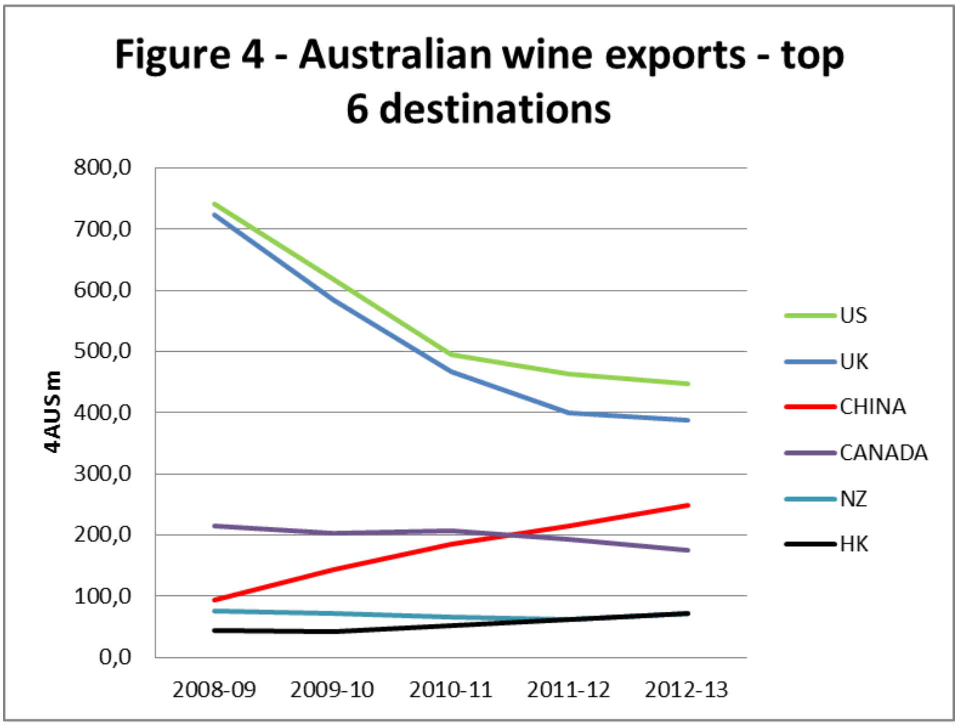

**Source – ITC Trademap.**

In terms of FDI, French official figures do not provide details of investment by sector or region. We can therefore only get a general view from official figures from the Agence

Francaise pour les Investissements internationaux (AFII). Although its importance is growing, China still is a relatively marginal investor in France overall (5% of FDI projects in 2012 and 1% of stock). Most FDI in France still comes from the traditional partners within the European Union, especially Germany (AFII, 2013). In addition, the agro-food sector attracts relatively little FDI. Only 6% of FDI projects in 2012 were in the sector. Banque de France also provides some figures, but they are very aggregate (Nivat and Terrien, 2013). These indicate that China held 1% of French FDI stock in 2011 (€3bn) and only became significant in that year, when a State Owned Enterprise (SOE) - CIC - took a 30% stake in EDF-Suez.

b. Recent evolutions in Western Australian wine trade and investment

Overall the Australian wine industry has faced a difficult period in recent years. While export performance has historically underpinned the development and expansion of the industry, the global financial crisis (GFC) in 2007-2008 led to a decline in exports in traditional markets. Total exports in 2012/13 were down 25% compared to 5 years previously. One winery insider described the situation as a 'perfect storm' comprised of the GFC, a historically very high Australian dollar and oversupply in response to overly optimistic projections for domestic demand (for more detailed analyses see Anderson (2010)). As evident in Figure 4, exports to both the US and UK fell significantly over the five years covered, by 40% and 46% respectively. In contrast, exports to China and Hong Kong have seen impressive growth – up 165% and 66% respectively over the same period. In spite of this growth, however, the US and UK remained the two key markets and demand in both has clearly fallen.




Source: WineAustralia

The export profile of WA (shown in Fig 5) is very different to that of Australia as a whole. Overall, about 20 per cent of WA wines production is exported. Exports have increased by 11% over the five years to 2012/13, with the Chinese market the key motor for this growth. Exports to China increased by 282%, although in contrast to Australia as a whole, exports to HK fell. Since 2009/10 China has been the main export destination for WA wine. Clearly the Chinese market has been key to the development of the industry in the region. There has been no plateauing off of exports as seen in Bordeaux, however we don't yet have full year figures for 2013. Informants in WA reported that demand for their wine has also been impacted by the government's anti-corruption policy, so falls can be expected.


Source: wineaustralia.

While trade data is very accessible, collecting meaningful investment data is rather more problematic. There are various databases of Chinese investment in Australia. The Australian Bureau of Statistics (ABS) provides aggregate level data on FDI inflows into Australia by source country, but there is no breakdown of where the investment is flowing within the country. The government's Foreign Investment Review Board (FIRB) publishes detail of proposed (not necessarily realized) investments, by country and by sector. These give a figure of $2.9bn of investments in agriculture in 2012-13 with the US the top investor, followed by Canada and Singapore. China was the fourth biggest investor in the sector with AUD 328m (FIRB, 2014). However these figures only cover large investments and thus most investments in agriculture are not included (RIRDC, 2011). KPMG and The University of Sydney have a database which applies a much lower threshold of USD 5 million per project and is the most up-to-date data on Chinese OFDI in Australia.

This data indicates that Chinese investment in Australian agriculture is relatively small and only a recent feature of the economic landscape. China ranks as the ninth largest investor in Australia with only 3% of total FDI. This compares with the United States (24%), the UK (14%), Japan (10%) and Singapore (4%). This data also indicates that Chinese investment in Australian agriculture is relatively small, with Chinese companies owning less than 1% of Australian land (KPMG, 2013). Over 2006-2012 China's investment in the sector was just 2%

of its total stock in Australia, with mining and energy responsible for the majority of Chinese FDI. WA, meanwhile, attracted only around 5% of the Chinese ODI in Australian agribusiness over 2006-2012.

None of these databases provides us with information at sector specific level – so wine is usually included in 'agriculture' or 'other' categories. In addition, what statistics do exist, are at national, rather than regional, level. Mapping Chinese investment in both regions, therefore, requires a more qualitative approach, the results of which we will detail in section V.

c. The policy context for Chinese trade and investment

Trade and investment flows are a reflection of the evolution of market demand and concurrent investment opportunities, but also of government policy. In both the French and Australian contexts, government policy is ostensibly open to FDI, although both have some limitations. In relation to trade, both face the standard 14% tariff on bottled wine exports to China (20% for bulk wine), as neither has a Free Trade Agreement. In addition to this tariff, a value-added tax of 17% and a consumption tax of 10 per cent are also added (ABARES, 2012). Australia is in the process of negotiating a FTA with China. ABARES forecast that wine exports to China will increase by between \$13 million and \$32 million, once the FTA is in place (op cit).

An FTA with the European Union (EU), and thus with France, is unlikely in the medium term, although a recent joint statement EU with President Xi indicated that it could be a possibility '…*once the conditions are right…'* (CEC, 2014a). In addition, wine exports were recently caught up in a much wider debate in the context of the European Commission's proposal to impose anti-dumping duties on solar panels imported from China. As soon as this proposal became public, the Chinese authorities launched a similar investigation into EU wine (Compadre, 2013b; Hook, Daneshkhu and Spiegel, 2013.). Tensions around the case were considered to have contributed to the fall in French wine exports to China in 2013 (Dyan and Testard, 2014). Although the solar panel case was resolved amicably, along with the wine case several months later, they demonstrated the vulnerability of exporters to wider trade frictions. In the final analysis the EU wine industry agreed to an undertaking with the Chinese industry to provide 'technical assistance and cooperation activities' in exchange for an end to the Chinese anti-dumping investigation (CEC, 2014b).

In terms of investment, both France and Australia have Bilateral Investment Treaties with China, however they date from 1985 and 1988 respectively and cover basic issues like fair treatment and dispute settlement. Like most of China's BITs they reflect an outdated context when most bilateral FDI flows were from developed countries into China (He and Wang, 2014). In order to update this framework, China is in the process of negotiating an EU-wide BIT, which would replace and update the bilateral French BIT (CEC, 2014c). Nnegotiations are confidential but there are likely to be several contentious issues which need to be addressed, including the elimination of mandatory joint ventures and creation of dispute settlement procedures (Nicolas, 2014).

In the Australian context, investment is included in the Australia-China FTA negotiations. The impact study of that FTA made the following assumptions in terms of the likely outcome - enhanced understanding of rules; simplified investment screening procedures and better investment protection (CIE, 2008). A key issue for Chinese investors in Australia is likely to be the threshold at which FDI is required to seek the approval of the Foreign Investment Review Board – currently $248m for all FDI with the exception of New Zealand and the US where the limit is $1,078[1]. Independently of the general threshold, the FIRB reserves the right to examine all FDI from SOEs (FIRB, 2012), a fact which can be seen as creating uncertainty for such investors (Drysdale and Findlay, 2009).

In the French context, there is relatively little institutional interference in the sales, mainly as they are so far of relatively small size. Although SOE tend to be seen as more controversial, there is no French legislation restricting SOE investment (Nicolas, 2014) and Cofco bought a small chateau of 20ha in 2011, while Bright Foods – owned by the Shanghai local government – bought 70% of Diva wine brokers in 2012 for an undisclosed sum (Letessier, 2012). In both of these cases there was no state interference. One institutional risk investors face, however, is suspicion that funds for investment are illegally acquired. France does have a system of monitoring for FDI which seeks to ensure that the source of funds is transparent and justifiable. The latest report of the monitoring body noted that the circuitous routes through which funds from China are transferred during the sales of vineyards raises questions about their legitimacy (Tracfin, 2013). Although no sale has been blocked so far, it is a risk for investors which transfer funds in manner which the French monitor considers un-

[1] http://www.firb.gov.au/content/monetary_thresholds/monetary_thresholds.asp consulted 11/12/13

transparent. This risk was certainly increased with the publication in June 2014 of a report of the Chinese National Audit Office (NAO), which concluded that 14 chateaux had been bought illegally by their Chinese investors, who used state funds provided for other purposes. It is as yet unclear how this will impact on the vineyards in question, but they may become the property of the Chinese state (Mustacich, 2014). Such an eventuality obviously complicates the situation for existing Chinese investors and their local collaborators.

## V. Chinese FDI in the wine sector extent and motivations

This section will explore the extent of Chinese FDI in the two regions which we studied, as well as its motivations and impacts. It draws heavily on our interview data, but also on local and national press reports. Chinese FDI has attracted attention in both countries and so the latter provide quite extensive details of the key investors. We believe that the majority of the key investments are included in our analysis. However Chinese investors are often very discrete and our data probably doesn't cover all investments.

### a. Chinese FDI in Bordeaux

As outlined above, China is not a big investor in France overall, however Chinese investment in the Bordeaux region is much more extensive than elsewhere, at least in terms of numbers of sales. The database which we developed for this research, based on press reports and indications from local experts, includes 64 vineyards. We use a broad definition of 'Chinese' - including mainland Chinese, Taiwanese or Hong Kong investors. The Bordeaux Chamber of Commerce and Industry (CCI) estimates that there are 70-80 vineyards in Chinese hands, out of a total of over 7000 that exist in the region – thus about 1% of Bordeaux vineyards are Chinese owned (Chen, 2014). Until recently all investments were wholly owned, but the investment of Bright Foods in Diva wine-merchants was a 70% stake (Letessier, 2012) and two recent acquisitions of chateaux by Liaoning Energy Investment are also majority stakes (Abellan, 2014). It may be coincidence, but in both cases the investors were State Owned Enterprises (SOEs).

Although the first 'Chinese' investor – Peter Kwok – a Taiwanese businessman – made his initial investment in 1997 (Anson, 2012), it was many years before others followed. In 2012-13 the rhythm of investments suddenly accelerated. It is the rapidity of these acquisitions which is unprecedented and has caused concern. As one journalist commented: '*A* *movement as rapid and important as the arrival of this Chinese capital is unique in the history of wine'*. (Author interview, March 2014). This rapid expansion, along with the sheer potential size of the Chinese market, fuels concerns about its long term impacts (Chen, 2014).

However, the fact that many chateaux in Bordeaux are small, explains to some extent the number of sales. When Goldin Group bought three chateaux in 2013 the combined size was only 15,4ha (Le Roy, 2013a). Bordeaux chateaux are rarely above 100 ha. This is clearly a disadvantage in terms of the volumes needed for the Chinese market. Thus some Chinese groups have bought several vineyards in order to secure an adequate volume of production. The You brothers, whose main business is pharmaceuticals, own at least six chateaux, covering 250ha, while the supermarket group Dashang owns at least two (Le Roy, 2013a). The most significant investor, however, is Haichang group -a highly diversified MNE from Dalian. They own 23 chateaux in Bordeaux, covering 500 ha (Sud Ouest, 2014). These investments became subject to question following the NAO report mentioned previously, which alleged that 13 had been illegally acquired with Chinese state funding provided to support the acquisition of leading edge technology (Mustacich, 2014). This controversy raises questions about the long term sustainability of the French subsidiary of this important investor's and will certainly undermine confidence in Chinese investment amongst local actors.

b. Chinese FDI in WA

The Ministry of Agriculture of WA indicated in December 2013 that there were three substantial investments in WA wineries, although it acknowledged that there may be smaller scale investments that have not been officially recorded. Two investments were by the same company – Grand Farms Group - a private company mainly operating in the meat sector, which has invested in the vineyards in partnership with a local businessman who has had long-standing business relations with the Chinese owner. This is a joint venture, the exact details of which are not public. The third investment was in a significant winery, Ferngrove, which is 88% owned by a Chinese businessman, Mr Ma, whose prime business is in ball bearings. However he began diversifying into agro food a few years ago– starting with a cattle farm and then moving into wine. Since Ferngrove, he has bought another vineyard in South Australia.

Beyond these key investments, we did find some further examples in the region. The Palandri winery was taken over by another Chinese businessman from the metal sector when it went bankrupt in 2008 (Deloitte, 2008). The company was rebranded 3 Oceans and is now Chinese managed and focused mainly on the Chinese market. There is one more wine group - Palinda - which was created when the Western Range and Woodside vineyards were bought by a Chinese businessman. Little information is available on this group and their website is only in Chinese.

Thus overall we found six confirmed investments. There are 1073 vineyards in the WA covering an area of 13,225ha, according to the Ministry of Agriculture (Personal communication, June 2014). Chinese investors therefore own only 0.5% of vineyards in the state. However at least two – Ferngrove and 3 Ocean's Franklin River vineyard - are large, at 300 and 350ha respectively. Thus vineyards owned or part-owned by Chinese investors represent over 6% of the vineyard land area in the WA region – significantly more than in Bordeaux, where most acquisitions are small. In addition, most industry participants expect this to rise. The real estate agents we spoke to reported regular visits from interested Chinese investors.

c. Motivations for FDI and differences between the two regions

The rapid increase in Chinese investment in wine has raised questions about the motivations of investors. One special issue of 'Objectif Aquitaine' in 2012 on the issue had the title page: 'What does China want?[2] Suspicion may be partly due to the non-traditional nature of many investors. In both regions studied, the key business of most Chinese investors is not wine, or even related products. The rapid growth of the Chinese market has motivated companies from very diverse industrial sectors to enter the wine sector. This has advantages. Wine is traditionally a long term investment with relatively low margins, which requires funding to develop. As one article on Chinese investment in Bordeaux put it *'..its not wine that makes money, but money that makes wine*' (Sanudo, 2012). Cross subsidizing wine investment with earnings from more profitable sectors can help to solve a common difficulty of vineyards across both regions - securing long term finance. Lack of experience is also a disadvantage however, precisely because investors may not appreciate the extent of long term investment required for their property. Several informants in the Bordeaux region expressed concern

[2] Objectif Aquitaine. Issue 205. December 2012.

that the ambitious investment plans of Chinese investors had not yet become reality and felt that this was partly due to their having underestimated the real cost of investment in France.

The reasons behind the interest of investors from such diverse sectors in wine, are various (Le Roy, 2013b, Dyan and Testard, 2014). Several respondents differentiated between those who invested mainly for the ‘trophy element’ and serious businesspeople. The former group invests primarily in Bordeaux and includes rich individuals from the arts or industry who have developed a taste for wine and for whom owning a chateau is simply a luxury. However this was a minority and most investors expect their investment to be profitable. Even in the case of those whose prime motivation was to have a ‘trophy’, they often used their property to entertain business guests, or gave their wine as gifts to contacts, thus solidify relationships in their broader business. This entertainment value also explains the preference for investors for vineyards with attractive historic buildings (Compadre, 2013a), where Bordeaux has a definite advantage over the more recent properties in WA.

Clearly the increasing demand for wine in China was a key motivation for most investors. However they could simply have imported wine and, indeed, many of them started their involvement in this way. A key reason for making the commitment to invest, common to both regions, was security of supply. Trust in suppliers to the Chinese market – both foreign and domestic – has been undermined by a series of scandals in the milk sector (Moore, 2013). In addition, wine is a sector where counterfeiting is widespread (The Economist, 2011; Le Roy, 2013b). Respondents from both regions underlined that being able to reassure customers that the wine comes from their own estates provides a level of confidence which is extremely important for the market. It is reported that half of the wine sold in China could be fake and industry experts suggest it could be as high as 90% for the high profile Bordeaux brands and premium Australian wines (Jordan, 2014). In addition, given the price points at which premium wine is sold, reassuring customers on authenticity is vital for both regions. A Western Australian company, Linkar Group has joined recently with the Guangdong Guangxin Information Industry Development company to develop a smartphone app designed to help consumers, retailers, wholesalers, distributors and suppliers to access data related to their wine and distinguish fake wine from the genuine product. Wine labels feature coding that can be scanned using the app. A WA winery, McHenry Hohnen Wine is the first winery to utilise the technology (Boothroyd, 2014)

In the case of Bordeaux, the appelation was a key motivation for investors. As indicated above, research in China shows that French wine has a large advantage on the market in terms of consumer awareness and perception ( Liu and Murphy, 2007; Hu et al. 2008; Lee et al. 2009; Yu et al, 2009). Bordeaux epitomizes this advantage. Although in the long term, local actors acknowledge that new competitors, both international and local, will emerge, they perceive that the first mover advantage which Bordeaux has on the Chinese market will ensure that it retains its leadership. The links to the terroir are important. As the CCI put it '*You can't offshore the terroir'* (Author interview, February 2014*)*.

Australian informants accepted that the Margaret River appellation didn't have the same brand power, but they counted on price advantage and quality consistency to convince customers. Bordeaux actors acknowledged that consistency of quality can sometimes be an issue with mid-range French wine and that Australian wine had an advantage on this point. This difference was considered to be linked to the more flexible institutional context in Australia, which allows poor harvests to be upgraded by mixing with more quality wines. There is little flexibility under the French AOC system, where regulation on what grapes can be used is very strict (Meloni and Swinnen, 2013). This difference has been noted in other comparative studies and reflects to a large extent the differing institutional context of 'Old World' and 'New World' wines (Jordan, Zidda and Lockshin, 2007; Banks and Overton, 2010; Grant, Dollery and Hearfield, 2011).

Avoiding middle men was a key motivation in the Bordeaux context. The local wine market is complex and strongly institutionalised, often involving several actors including courtiers and wine merchants as well as advance 'primeur' sales (Mahenc and Meunier, 2006; Anson, 2007). In addition, the various actors in China also add new costs, especially as the market is immature and value chains are thus more extensive and expensive. Bypassing these various actors is one motivation for securing direct supply. In Australia the market is organized in a less complex manner, thus avoiding domestic Chinese middlemen was an issue for all exporters, but not a key factor in FDI.

A motivation which was more evident in Australia than in France was the desire to extend or cement business relationships – guanxi, in a sense. Most investors in the WA industry have prior experience of investment in Australia. This is not the case in France, where the level of Chinese investment in the broader economy is lower. Thus there are fewer possibilities for investors in other industries to gain experience of the local environment before moving into wine.  Grand Farms indicated that the key reason for diversifying into wine was that their Australian partner had expanded into the industry. Keen to continue working together after a partnership in meat export lost its license, wine was the chosen sector (Author interview, March 2014).

Mr Ma's investment in Ferngrove was also a move into a new sector for him. His primary objective had been to invest in the meat sector. Once Ferngrove's CEO had helped to find a suitable farm, he began to import their wine and quickly decided to invest in the company (Author interview, December 2013). In both cases, personal relationships established in other sectors were key to the wine investment. This reflects a common perception that personal contacts are key to business in China, including in the wine sector (Beverland, 2009).

Finally one factor which may have had an impact on the investment in individual wineries in Australia is the new 'Significant Investor Visa' (SIV), a scheme which allows those bringing overseas investment of over $5m to obtain migration rights to Australia for themselves and their families. The scheme was said to have been developed with Chinese High Net Worth Individuals (HNWIs) in mind (Loras, 2013). It is difficult to say with certainty whether this has had a major impact. None of our interviewees used their wine acquisitions to access a visa. Although this was either because they had already acquired one from previous holdings, or the scheme was not yet in place when they invested. However recent interest reported by estate agents is said to be strongly linked to this advantage. One WA real estate agent commented: *'Its a big component. I'd go so far as to say its 50% of the interest*.' (Author interview, December 2013).

Dealing with the complexity of the Chinese market is a challenge which all exporters face, be they owned by Chinese capital or not. One solution, which has also been adopted by Ferngrove's partner, is to distribute through their own proprietary distribution system. In Bordeaux, the two supermarkets which have invested can clearly use their own shops to distribute their wine. One key investor - Tesiro – initially distributed their wine through their chain of jewelry shops (Pedroletti, 2012), but is now building a separate distribution system (Dyan and Testard, 2014). Diva, the only Bordeaux wine-merchant majority owned by a Chinese investor, distributes its wine through the latter's sales network. However it is more oriented towards tobacco sales, which has limited sales (Author interview, March, 2014). All informants recognize that for wine to become a widely accessible consumer product in China, distribution networks need to be improved and consumer education assured. Using networks set up for other goods – be they jewelry or cigarettes – is not always very effective, especially in relation to the latter point – educating customers on the specificity of wine.

Beyond the motivations for Chinese investment in wine, it is worth considering briefly those of the winemakers who sell their properties. Wine is not an easy business and long term finance is hard to secure in either country. Both Australia and France have seen reductions in their vineyard area in recent years (FranceAgriMer, 2013). Informants in both Bordeaux and WA commented on the fact that many winemakers find it difficult to convince the younger generation to continue in a business with relatively low margins, which requires a long term investment perspective. In Bordeaux, many of the properties bought by Chinese investors are in the less prestigious appelations, where producers struggle to make a profit (Chen, 2014). In WA most Chinese investments are outside of the most prestigious Margaret River area. It is reported that Chinese investors can secure higher margins for their investments in wine than other investors, because of their ease of access to their domestic market (Dyan and Testard, 2014). In this context, they should be able to secure greater long term profitability for their vineyards, thus providing a more secure future for a wider range of wines.

## VI. Conclusions

Several findings emerge from our research. Firstly, although China is clearly an interesting and growing wine market, it is a rather volatile one, where political tensions, both within the country and with partner governments, can have important effects on trade. Thus the advice from several interviewees that exporters should avoid focusing solely on the Chinese market, seems wise. Secondly, in spite of extensive interest in the French and Australian press, Chinese investment is not hugely significant in either region, in terms of share of properties. What is unusual, is the rapid rate of growth, which emerged in Bordeaux in 2012-13 and which industry stakeholders also expect to see in WA. This development has fueled some resentment in the Bordeaux region (Chen, 2014), although most professionals in the industry welcome investment as vital to securing the future of the industry.

In terms of the motivations for investment, many represent factors which will remain pertinent in the long term and thus further flows seem likely. Several of those interviewed stressed that Chinese investment was generally not speculative. In spite of concerns that some investors may have underestimated the long term cost of their investments, there has been no evidence to date of a reversal of any commitments. Factors like the long term increase in demand on the home market and consumer concerns about security of supply and, especially, counterfeiting in the sector, will remain strong arguments for investing directly in vineyards for some time to come. Non-economic factors, including residency issues and life-style and prestige related concerns, are also likely to drive a number of investment decisions.

The institutional context in both countries seems quite supportive and we found few indications of institutional barriers to FDI. In addition, both may have an even more positive environment in the near future, if the talks on the EU-China bilateral investment agreement and the Australia-China FTA conclude successfully. Potential barriers, such as the French investigations into sourcing of financing for FDI and the fact that SOE investments must pass the FIRB in Australia, do not so far seem to have caused any significant difficulties for investors in the wine sector. However the recent allegations of illegal funding of many investments may fuel calls for stronger regulation.

In terms of future research, given how recent these investments are, there is much potential for a more long term review of their impacts. One area which is likely to provide interesting possibilities for research, is the extent to which different types of ownership and types of owner, may impact on the long term success of the business. Three of the key WA investments investigated were partnerships. This form of market entry has recently begun to emerge in Bordeaux. It would be interesting to explore the extent to which such formations are more, or less successful than simple acquisitions. In addition, although all WA investments so far have been by private companies, SOEs have begun to invest in Bordeaux and press reports indicate that there is interest from some SOEs in Australia (England, 2013). Because of their links to the state, SOEs could be expected to attract more criticism and distrust than private companies (Mc Guire, Lindeque and Suder, 2012; Rugman, Nguyen and Wei, 2014), which could impact on their long term success. Indeed the question of how SOE investment is treated, has been identified as a key issue in relation to Chinese FDI in the Australian resources sector (Drysdale and Findlay, 2009).

Another issue of interest is the potential impact of these investors on wine tourism. In spite of its global renown, informants recognized that Bordeaux does not adequately exploit its brand in terms of tourist services. Some chateaux have become hotels or guesthouses, but they are relatively rare and often struggle to make money. As one informant commented: '*Winemakers discover too late that wine and hotels are very different businesses!*' (Author interview, February 2014). Observers see this as an area with great potential to assure Bordeaux's future brand positioning. Indeed, the link between involvement in wine tourism and subsequent consumer loyalty has been shown in empirical studies (Famularo, Bruwer and Li, 2010) and Chinese wine tourism has started to develop domestically (Zhang Qiu et al, 2013). However in Bordeaux its potential is underdeveloped.

In this context, the fact that many Chinese investors come from outside the sector may become an asset. Several come from the real estate or tourism industry and have announced ambitious plans to develop hotels and golf courses (Pedroletti, 2012). Clearly, if these plans come to fruition, they have the potential to significantly upgrade the wine tourism sector in the region. Although WA, and especially Margaret River, has developed wine tourism quite effectively, expanding to a wider potential customer base could clearly increase incomes and extend the tourist season. In any case, research on the interaction between FDI and tourism could be an interesting area for exploration. In spite of extensive study of wine tourism, summarized in Carlsen (2004) and extended widely since, the authors have not identified any studies which look at the interaction between FDI and wine tourism.

**Annex**

| Overview of Interviews for the research | |
|---|---|
| **Institution/ Company** | **Date** |
| ***Australia*** | |
| WA Ministry of agriculture | 06/12/2013 |
| Real Estate agent 1 | 13/12/2013 |
| Real Estate agent 2 | 16/12/2013 |
| Ferngrove | 17/12/2013 |
| Chinese investor 1 | 17/12/2013 |
| WA Wine Association | 18/12/2013 |
| Grand Farms Group | 28/03/2014 |
| ***France*** | |
| Industry expert 1 (academic) | 14/01/2014 |
| Industry expert 2 (academic/consultant) | 27/01/2014 |
| Industry export 3 (Consultant) | 11/02/2014 |
| Journalist Objectif Aquitaine | 14/02/2014 |
| Œnologue | 18/02/2014 |
| CCI Export director | 20/02/2014 |
| CCI President | 21/02/2014 |
| Franco/chinese œnologue/courtier | 21/02/2014 |
| Former CEO of Chinese investment group | 27/02/2014 |
| Diva | 06/03/2014 |
| Journalist 'Sud Ouest' | 13/03/2014 |
| CEO of vineyard exporting to China | 08/04/2014 |
| Marketing manager for group with several Grand Crus | 10/04/2014 |

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