Direct to Consumer Ecommerce in the Global Wine Industry: Why do some countries lag in adoption?

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Background

Direct to consumer (DTC) ecommerce in the global wine industry has trailed ecommerce adoption in other retail oriented industries over the past decade. Dominant explanations behind this lack of adoption are regulatory constraints, excessive shipping costs and intense competition. This is an analysis of online consumer purchasing patterns in a number of jurisdictions (Australia, Canada, Hong Kong, New Zealand, United States) using primary data collected from BlackSquare's ecommerce operations and secondary industry sources.

Results

DTC sales are important to the global wine industry. It comprises $3.4B in sales in 2010 in the US, out of $40B in total wine sales and is growing quickly, with 62% of US wineries reporting DTC is the fastest growing sales channel.\(^1\) Given the various benefits of DTC ecommerce, wineries should have substantial motivation to increase DTC sales\(^2\) versus any other channel (retail, bulk, trade)\(^3\) as margins are materially higher, 0.5x – 2x depending on the jurisdiction.\(^4\) However, all countries outside the United States lag considerably, indicating some barrier to adoption.

Ecommerce has evolved substantially since the first tech boom in the late 1990s and early 2000s. Complex ecommerce business models have been customized for specialized markets such as music, books, clothes and furniture. Wine has not seen the same customization, and instead relies on generic ecommerce cart applications.

BlackSquare’s global operations provide insight into several countries where the regulatory environment, logistical circumstances and competitive retail channels vary substantially. Both Canada and the United States suffer from a complex regulatory system and a long and intricate logistical supply chain\(^5\). Canada has a fragmented monopoly dominated retail wine channel, while the US has an extremely competitive retail industry. One would expect wine ecommerce to struggle in these markets, however, the US leads the globe in wine ecommerce and Canada has a substantially larger market\(^6\) than expected given its

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1 VinterActive LLC, *The VinQuest™ U.S. Consumer Direct Wine Sales Report 2011*

2 ShipCompliant’s *Direct-to-Consumer 2012 Shipping Report* indicates percentages of US DTC winery sales are: <1,000 cases 9%, 1,000 – 4,999 7%, 5,000 – 49,999 8%, 50,000 – 499,999 2.9%, 500,000+ 0.05%


4 BlackSquare Inc. internal calculations for US, Canada, Australia, New Zealand, Hong Kong, 2010 – 2013 inclusive

5 ShipCompliant’s *Direct-to-Consumer 2012 Shipping Report* points to “consolidation of the wholesale distribution tier”, “2005 Supreme Court ruling that forced many states to revisit their direct shipping laws” as key points in the evolution of the US DTC wine market.

6 BlackSquare Inc. internal calculations
environment. In the US, the DTC industry is still highly concentrated, with 49% of all winery DTC shipments originating from Napa Valley and California making up 32% of shipments received.\textsuperscript{7} By contrast, Australia and Hong Kong have extremely liberal regulatory environments, with low or no wine taxation, logistical channels set up for wine shipment (Australia), or compact (Hong Kong) and competitive retail environments. However, DTC ecommerce struggles to gain acceptance and lags other markets substantially, indicating there are alternative reasons for differing adoption levels.\textsuperscript{8}

Wine ecommerce falls into three main categories: ad-hoc (single purchases), recurring (subscriptions), and targeted (add-on purchases for recurring members). Ad-hoc websites were the first generation of ecommerce websites established in the late 1990s. Ad-hoc ecommerce uses the minimum amount of product information required to actually transact and provides little to no information on the wines sold. This leaves little reason for consumers to purchase online versus a retail store, given shipping and administrative costs. Recurring purchases manifest in the wine industry as wine clubs and have developed a strong niche. Whether wine clubs are run by third parties or by wine producers themselves, the transactions are less about the individual bottles of wine purchased and more about education and the “wine experience,” similar to that of a tasting room. Based on BlackSquare’s internal data\textsuperscript{9}, verified by secondary sources\textsuperscript{10}, between 70% and 90% of revenue derived from DTC wine sales comes from recurring purchases, indicating this more complex ecommerce style is significantly more successful for the wine industry. Targeted ecommerce is focused on providing add-on purchases to users who are already purchasing product, usually through the wine club. Unlike ad-hoc ecommerce, targeted ecommerce provides consumers with a concrete reason to conduct ecommerce rather than purchasing through a retail channel.

If there is good success with modern ecommerce techniques, why is DTC wine ecommerce stuck in decade old design mentality that provides little incentive for incremental consumer adoption? Until recently, software developers and technology companies shied away from the wine industry due to regulatory and logistical challenges. Recurring purchase ecommerce, convincingly the best option for the wine industry, is difficult and expensive to build. Point of sale providers, web design firms and marketing consultants continue to use traditional ecommerce cart technology such as Magento, Volusion or Drupal, pushing wineries further down the path of traditional ecommerce which does not handle recurring purchases smoothly. Software as a service companies focused on recurring purchases have capitalized on this niche.\textsuperscript{11} Ad-hoc ecommerce websites concentrate on less than 30% of the ecommerce market and

\textsuperscript{7} ShipCompliant, \textit{Direct-to-Consumer 2012 Shipping Report}, Page 10, Page 16
\textsuperscript{9} BlackSquare Inc. internal data and calculations, 2010 - 2013
\textsuperscript{10} Denner Vineyards – \textit{Wine Industry Conference 2011}, page 4
\textsuperscript{11} Chargify (http://chargify.com/), Recurly (http://recurly.com/), Zuroa (http://www.zuora.com/), Blackboxx (http://blackboxx.biz/) retrieved 11/03/13
are challenged to meet rates of return hurdles due to high capital expenditures. The industry needs to demand purpose-built solutions for the wine industry that recognize and understand the complexities around wine and wine ecommerce.

Conclusions: There is significant evidence to suggest that, even while controlling for exogenous factors in different geographies, it is incorrect assumptions around the shape and functionality of ecommerce websites that limits consumer adoption of DTC wine ecommerce. Companies and countries wanting to encourage deeper adoption of DTC wine ecommerce should provide tailored recurring purchase ecommerce as well as websites that perform beyond the current ad-hoc transactional ecommerce environments predominately used today.