Profit (and Mostly) Loss in SA Wine Production

By Dave March CWM

Fewer than one in five wine producers in South Africa are making a reasonable profit. One in three is running at a loss. The rest are just breaking even.

That is only one of the possible conclusions to be drawn from the latest VinPro figures discussed at the recent 'Information day', and whichever way you look at it, the numbers make difficult reading.

What was equally interesting was the regional differences in the profitability of wine farming. The differences were stark and, to me, showed a direct correlation between production yields and income. Those areas that were able to harvest big yields – say 14 tons per hectare and above – and sell grapes or juice, often in bulk, as well as wine if necessary, are often able to do better than break even. In the Breedekloof region, for example, some 80% of farms are making a profit, if only a small one. Winegrowers there have the ability to produce bulk wine quality at lower prices or to produce quality wine at reasonable cost with reasonable yields.

The most profitable region on average, Worcester, illustrates this point clearly. Only 4% of farm producers here are making a loss and 70% are profitable. However, profits are low – probably because of the low grape, or bottle, income they can command – only 15% are returning more than R20,000 per month above costs. The nature of their product, either grapes or juice for Brandy, commercial or bulk quality or mid quality table wines may provide an outlet that other regions don't have. Olifantsrivier, however, shows that it is not that simple as it has the second highest production costs to weigh against bigger yields. Large yields are not necessarily the answer; 40% are making a loss in the Orange River region, yet with yields as high as 40 tons/ha (the average is 33t/ha), still only one in four producers are making a decent profit. At the other end, Malmesbury is averaging just 9t per hectare and one in four farms are making a loss or breaking even, but the premium nature of their product combined with the overall lowest production costs sees the other three of the four making some profit.

Contrast this with Stellenbosch. Two of every three producers here are just breaking-even or making a loss. Only 8% are making a reasonable profit. Is this the nature of their product? Costs here are the highest of all regions, requiring some R46,000 per hectare to meet costs. Many producers have yields of 6 to 8 tons per hectare, so unless you are able to sell the result as a premium product – and can make sales – there is going to be a shortfall. I was once told that to make any return around Stellenbosch you need to achieve 12 tons per hectare minimum, and the average is under 10, so unless your bottle is on the shelf at more than R150 and being snapped up, the figures don't look good.

Even then, you fight the odds, as the average producer profit from a R50 bottle of wine is just R3, (taxes amount to R32, which reminds me of a provoking argument I heard; when you eat with wine in a restaurant, you might tip the waiter 10%, maybe R10-R20, probably five times more than the producer of the wine is getting!). As many costs remain the same, selling the bottle for R150 should achieve more profit, around R50 per bottle, but again, it isn't as simple as that.

VinPro's analysis of the Klein Karoo region made depressing reading. Smallish producers (on the whole) making premium products, often niche such as Port and Muscadel styles, with some higher costs (eg irrigation) though no higher than most overall, means that just one in ten can expect a healthy return and seven in ten can expect to make a loss or break-even. No wonder yields hover around 19t/ha. How will the 2016 harvest, with its reduced yields, affect those who rely on producing quantity for their margins?

Two thirds of our wineries are running at a loss, then, despite the low Rand, increasing visitor numbers and a moderate export market. How are other 'New World' countries managing to do well?

The answer is, they are not. Consider Australia, direct rivals to SA in many wine ways. There, some 85% of producers are running at a loss (Winemaker's Federation 2015). Australian regional differences are clear, too, with warm areas being a particular financial nightmare. The WF report stated that in those areas, 92% of production is unprofitable. In cool areas, the way to go, still 43% was unprofitable. And size doesn't matter, either, smaller companies, outside of the corporate 'big four' (Treasury, Accolade etc) are faring better with most managing a 6% profit. Interesting that many in Australia are lamenting the 'meagre' annual R300m that Wine Australia has for overseas market development at its disposal.

Karoo producers, take heart, for of those in the Hunter Valley in Australia, 94% are loss-making and in the Mudgee region (prime Cabernet and Bordeaux blend area), only 1% are in the black!

The cause, many feel, is over-production, a falling Dollar, too low price-points – especially on exports - and high wine taxes. Sound familiar?