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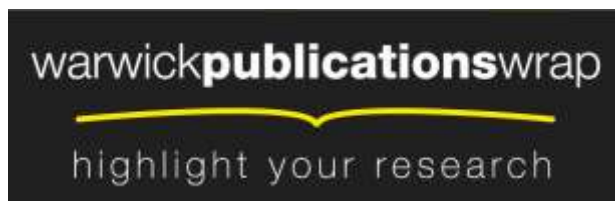
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Chapter 10. Creating and sustaining a competitive advantage over time: Managing a delicate balance between value creation and value appropriation as a regional capability

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INTRODUCTION

**The region of Champagne has achieved enormous success in the wine industry. Champagne brand is synonym and a reference for many people, of luxury consumption. While there are strong brand companies behind the marketing of**



champagne like Moët & Chandon (part of LVMH) or Vranken-Pommery, the sparkling wine produced in more than 30,000 hectares in the area of Epernay-Reims is globally known. However, there is not much information about the actors behind this success. In terms of the sparkling wine industry, the region of Champagne is constituted by a number of key figures. Many of these (e.g. the number of people employed, numbers of houses, vigneronns and co-operatives, yield etc) have been noted before, but other factors relevant to the value created by champagne include:

- 12% of sparkling wine worldwide sales
- Average price per bottle is 20 €
- 200 companies are located in the region performing activities related to the industry: machinery, laboratories, glass, cardboard, printing, corks, etc.
- The average price of grapes per kilo is 5.50€ which is substantially higher than other wine regions.
- The price of land is at 850,000€ per hectare can be compared with the average value of AOC vineyard in Alsace of 120,000 €, Languedoc at 11,000 €, Bordeaux at 64,000 €, and Burgundy at 87,000 € per hectare.
- The main producing areas in France are: Bordeaux 134,800 ha, Provence 67,900 ha, Cotes de Rhone 39,600 ha, Burgundy 30,000 ha, Champagne 30,000 ha.



**This success story can be summarized in a simple phrase: ‘a delicate balance between value creation and value appropriation’. This delicate balance, which evolved from learning processes between the social and economic actors in the region, recognises the intrinsic complexity of managing social systems and the capability to sustain a competitive advantage in the wine industry over 200 years. In order to identify the factors behind the success of champagne in terms of value creation and value appreciation, I will employ the analysis of Pommery’s managers about the success of champagne:**

- **History. Most of the champagne Houses were created in the 18<sup>th</sup> century. This is an important differentiating factor with current sparkling wine competitors and one of the most important generators of value.**
- **Quality guarantee based on expertise & terroir. The tradition existing in the region and the unique terroir are responsible for constant quality. Throughout the years, cellar masters, who may work for the same company until retirement, are responsible for the assemblage of three different grape varieties: chardonnay, pinot noir and pinot meunier. Each year, the new wine is assembled with wine reserved from previous years (sometimes seven years) to maintain the uniqueness and the concept of each house’s sparkling wine. For example, the current cellar master in Pommery is the ninth cellar master since 1856.**



- **Real creativity coupled with genuine innovation. Ongoing R&D with traditional know how where the cellar master is a key value creator. For example processes of new yeast development and new styles in champagne are usually developed in the region by diverse actors, from small vigneron (grape growers) to large champagne houses.**
- **International recognition, flanked by an expensive marketing budget. The champagne industry invests 400 million€ in marketing to sustain the brands of their wines. Names like Moët & Chandon, Pommery, and Mumm are globally recognized as luxury wines.**
- **Controlled origin appellation. There is only one sparkling wine that can be named 'champagne'**
- **Premium price. On average, the price of a bottle of champagne is 20€ even including small houses without expensive marketing budgets.**

**The initial factors are responsible for the creation of value in Champagne, while the last two factors are related to the appropriation of the value created.**

VALUE CREATION



**Value refers to the specific quality of the product as perceived by users in relation to their needs. Such a judgment is subjective and individual specific. Value creation depends on the relative amount that is subjectively realized by a buyer who is the focus of value creation and that this subjective value realisation must at least translate into the users' willingness to exchange a monetary amount for the value received (Lepak et al, 2007). Champagne generates more value than other wine regions in France and worldwide. Champagne is synonym of luxury and this perception is clearly translated into an average price higher than the rest of the wine industry. How this value was created and is created? The answer to this question is the focus of this section.**

History

**The main group responsible for the creation of value throughout the story of champagne region was the négociants. While they controlled small to medium size champagne firms, their main interest was in the business of selling champagne (Guy, 2003). Communicating with different clients, from the nobility to the rich commercial social class, was a central occupation of négociants (Guy, 2003). To ensure supply, they transformed themselves from brokers into merchant-**



**manufacturers buying large vineyards and investing in bottling and storage facilities. The négociants of champagne offered not simply a fine wine, but an exclusive sparkling white wine (Guy, 2003). The négociants became champagne houses during the French Revolution and aggressively cultivated new clients through personal relationships throughout all Europe<sup>i</sup>.**

**However, the champagne industry did not become stalled with difficulties or even a pool of diminishing consumers like the nobility. They invested in new processing techniques, transportation and communication networks so as to expand their sales to the new social groups emerging in the late 1800s in Europe and North America (Guy, 2003).**

**Champagne value emerged as part of the new mass consumer culture generated at the end of the 19<sup>th</sup> century. Luxury prestige wines became part of the culture and national consciousness of France and, as the centre of the new bourgeois, to the whole world. Guy (2003) suggested that champagne was central to a process of rapid change, which included the beginnings of the modern revolution in consumption, in the late 1800s. Champagne was used to delineate social boundaries and its consumption became a basic ritual for membership within certain social**



groups. As an integral part of numerous traditions and rituals, champagnes became a centrepiece of bourgeois society. Champagne's investiture with cultural capital resulted from both its linkage to France's reputation as the pre-eminent capital of the bourgeois world and the wine's own evolving importance as international market of social distinction. Sales grew from 5.9 million bottles in 1850 to 28 million in 1900<sup>ii</sup>.

While some activities for the creation of value are related to whole processes or activities at organizational level, it is important to understand the role of social networks that are externally directed to detect the needs of customers in some circumstances. In that sense, the social position of the champagne houses in different social networks in diverse countries and social classes allow them to capture and understand changes in customers' needs. The idea of client relationship was central to champagne marketing before any other wine region and branding the wines using the family name of the founder was broadly used as a tool to maintain the relationship with clients (Guy, 2003). The use of the family name was even more important than the appellation 'champagne' as a form of personal assurance of the quality and uniqueness of the product within a distinctive bottle.





**However, champagne houses were not alone in creating value through history. The evolving social positioning of Champagne as a region was demonstrated in different ways. For example, Reims cathedral was the place where many French kings were enthroned; Epernay was a royal city with the patronage of Louis XIV. Another example is the set of photographs of some members of the English royal family with the founder of Laurent-Perrier.**

**Other actors have also been important creating value at different levels. In the following section, I will review the work of cellar masters or oenologists in maintaining quality and facilitating the work of négociants.**

Quality guarantee based on expertise and terroir

Champagne offers to consumers a sense of continuity in taste and quality, which was an important innovation when wines usually differ from vintage to vintage. However, the ability to offer continuity comes from the tradition in the art of assemblage, which resides in one very interesting actor: the cellar master or oenologist. Cellar masters work for years with the same house (like the example of Pommery). There are a number of factors



for this situation but the assemblage of reserve wine dating from many years ago may be one of the causes.

**Another aspect is that the art of assemblage is transmitted only by apprenticeship. The different interviews offered a common perspective: the knowledge existing in Champagne about the key factor for success, the style of the sparkling wine, is highly tacit. For example, oenologists have to blend many different wines, in some cases from many years ago, in order to obtain a constant quality over time. The art of assemblage is very specialized and only in performing the task can it be learned. For example, Pierre Cheval of Champagne Gatinois, a small grape grower and champagne producer, has engaged his son in blending wines for five years and expects he will need yet more time before transmitting the business to his son. The cellar master of Dom Pérignon, who has been in the company for 18 years, has also been working with an apprentice for many years. The long delay in learning the production process is also an important isolating mechanism that avoids the slippage of value and creates a barrier to labour turnover. Cellar masters remain with the same company for many years.**

Cellar masters or oenologists also create value by acting creatively to make their job more novel, launching diverse versions of wine. For example, Pommery's cellar master



works with four more people who are responsible for each champagne brand style. An important innovation launched by Pommery in 1999 was POP. A new version of POP is launched every year (which includes a new label and a different wine) with diverse themes like ‘of the world’, ‘collector’, ‘silver’, ‘gold’, ‘blue’ and ‘maxi’. Other new products are seasonal champagnes (Springtime, Summertime, Falltime, Wintertime). Even though they are quite innovative, Pommery still maintains its traditional styles like Brut Royal, Rosé and Grand Cru Millennium.

Real creativity coupled with genuine innovation

Innovations to create value are welcome but under an umbrella determined by the traditions established in the region. One interviewee suggested that people and history is what matters in the region. Strong traditions generated by generations living in the same area and producing the same product were key determinants for the adoption of some innovations generated by some actors and adopted later by the rest of the region.

Champagne was a result of innovation and it maintains this traditional approach even today. Dom Pérignon’s purported ‘famous discovery’ was an incredible innovation for the region when its main consuming market, Paris, switched towards burgundy and



bordeaux wines in the 1700s. The Dom Pérignon myth was later employed to distance champagne from the innovations that turned sparkling wine production worldwide into a huge scale industry (Guy, 2003).

Blending allowed the Champagne region to be innovative. For example, at Champagne Laurent Perrier they claim that initially champagne was assembled from pinot noir and pinot meunier, but a cellar master subsequently added up to 45% of chardonnay in order to improve the elegance, freshness and finesse. However, there is not a common formulation for champagne. Each producer (large or small) has its own style determined by the proportions employed of each grape in the blend. Before this innovation, champagne was drunk at the end of the meal as a dessert wine. This change in taste allowed champagne to reposition itself from consumption at the end of the meal to the beginning of the meal as an aperitif - or even to be part of a meal. This innovation opened a new market for champagne.

**Interestingly, the art of blending originated from the complexity of grape production due to weather variability. Champagne is the northernmost wine region which suffers sometimes a late freeze in May. As was maintained by Laurent Perrier, this variability in grape quality led to the development of assemblage to**



**maintain wine quality and made the cellar master's sensitivity to reserve wines important in order to maintain a constant quality from different wines and years. While there is variability in grape quality each year, the main value created by the cellar master is to maintain the concept of the product every year. However, tradition is accompanied by investment in R&D with, for example, the development of proprietary yeasts adapted to different type of grapes. Innovations in production techniques have also been very common. For example, the style of vinification changed when they abandoned the oak barrels for the concrete tanks employed by beer brewers (Laurent Perrier visit). Later on, they introduced the stainless steel. Another innovation in the production process was the introduction of gyroallettes, an automatic process for riddling champagne bottles in large quantity, mainly employed by mass market champagne producers. However, many houses still maintain their process of riddling manually inside large underground tunnels for many reasons: different bottle shapes, tradition or exclusiveness. Similarly, in spite of the problems in grape growing, grape yield grew from 165 kilograms per hectare in 1910 to 15000 kilograms in 2007 due to better grape management over years.**

Other innovations like new bottles and packaging were common in the history of champagne. The development by Pommery of POP has already been noted. This is a



small bottle of champagne (200 ml), with the different and new labels every year. This innovation opened a completely new market segment in the youth market as it was sold through night clubs and discotheques. However, some new types of champagne, like Rosé, took many years to become established but still offered new opportunities to the region.

**Regional innovation is also supported by other actors, like one of the main banks in the area, the Crédit agricole. The bank is a regional investor with its own equity as it is a shareholder in some houses, :most notably aiding the Taittinger family to repurchase their family house. However, its participation does not stop there since it funds research in the cluster for 82 million€ in water, vineyard and environmental scientific research, as well as supporting academic chairs and programmes.**

At the level of society, the process of value creation can be conceived in terms of programs and incentives for entrepreneurship and innovation intended to encourage new entrepreneurial ventures to innovate and expand their value to society and its members. In Champagne, value creation also occurs through entrepreneurial actions encouraging the new generation of vigneron, the sons of the current landowners, to become small champagne producers. This process is still at small scale because 80% of the properties



of small grape growers are rented for a percentage of the production, and most of grape producers sell their grapes directly to the main champagne houses instead of producing their own champagne by their own facilities or through local cooperatives.

This new generation of entrepreneurial vigneron has been supported by the SGV. Among different actions of the SGV to encourage entrepreneurs is the launch of an umbrella brand in 2001 'Champagne des Vignerons' - a generic umbrella brand created in 2001 for 4,800 grape growers affiliated to SGV. The SGV wants to build and develop brand awareness around growers; unifies members around strong values and targets marketing segments with this brand. Among the values implied in the brand are quality and tradition as well as the representation of the terroir. However, this marketing action is only targeted to France where most grower sales are made, but where more than 50% of current customers are older than 50 years. The new entrepreneurial vigneron tend to produce more than 100,000 bottles per year, understand the concept of marketing and position their champagnes in different distribution channels in France and abroad through diverse strategies: restaurants, newsletters to hundreds of previous customers, and to distributors. Moreover, they are aware of the danger of commoditisation and work strongly to differentiate their champagne. One of the entrepreneurial vigneron said 'each village has its own personality and quality'..



In other cases, innovations came from the arrival of new entrants, like Taittinger in the 20<sup>th</sup> century. Even though Mr. Taittinger bought a 1734's champagne house, he brought innovations to the business model like the exploitation of historical assets like abbeys or chateaux. However, Mr. Taittinger did not remain as an outsider since he incorporated to his business model a social and political role and commitment in Champagne. Reputation and location matters to be successful in the region. In one visit, our interviewee said 'the secret of Champagne - we have to live here'.

However, new entrants do not fit well most of the time. Recently, large companies have bought traditional champagne houses, but the arrival of new management teams or the existence of headquarters outside the region has generated concern among the region. In one visit, the comment was made that 'the mergers (of local houses) with other companies are not good because they (the new managers) live out in Paris.' This situation highlights the importance of social networks in the Champagne region.

International recognition flanked with an expensive marketing budget

**The position of champagne is different in France from the rest of the world. In France, champagne is perceived as the essence of France in every class so the**





market segments consuming champagne include middle class. However, they do not consume only branded champagne but they are linked to small producers through traditional relationships, in some cases lasting generations as Mr. Cheval said. Mr Taittinger said that the positioning of champagne is ‘an affordable luxury’ so everyone can enjoy it at least once a year. Another interviewee said that champagne is ‘an affordable luxury because is easy to buy since you can separated into small units (bottles), and, in case of crisis, you can buy 2 bottles but may not change your car’. The industry employs good advertising to position the wine: Royal Patronage and participation in key events like car races: the Wine of Champagne is a celebratory wine.

Most of the small producers target local markets and France, and champagne houses mainly operate export markets like Britain, USA, Germany and Japan. This is very interesting in terms of value creation and value appropriation since champagne houses have to invest additional resources, like branding and distribution channels<sup>iii</sup>, to create value and appropriate it, small producers only invest in the production of grapes since most of the champagne is produced cooperatively and sold from their own cellars. Prices reflect these differences between investment and market segments.



However, there are some challenges for champagne in international markets. As noted in chapter 4 (see figure 04.6) champagne is particularly susceptible to economic downturns. There are many newer sparkling wines on the market especially from New World countries, as well as sparkling wines produced by champagne houses in those countries. The promise of growth in the large markets of China, Russia and India won't make up for reductions in major markets, which are declining, since they are still small markets.

Champagne has been a very successful area generating value in the long term through learning processes, highly innovative firms and strong social networks. However, the creation of value has to be accompanied by good appropriation strategies, otherwise the economic actors in the region will not have the high standard of living that they currently have.

## VALUE APPROPRIATION

In the strategy literature, two key concepts operate across all levels of analysis to determine which actor captures the value that is created: *competition and isolating*



***mechanisms* (Peteraf, 1993). The creation of novel products often produces a situation where there is limited supply and high demand. Competition will follow, as other suppliers of the product seek to replicate the value created and participate in the profits. A consequence of competition (increased supply) is that exchange value (price) will decline to the point where supply equals demand. Competitors may also be unable to retain value as end users benefit from the lower prices brought by increased competition. Isolating mechanisms implies that competition is limited and supply is not above demand. Isolating mechanisms can be knowledge, or physical or legal barriers which prevent replication of the value-creating product by a competitor. In essence, isolating mechanisms operate to limit value slippage, thus enabling sources of value creation to capture the majority of the value created. The existence of an isolating mechanism raises the potential bargaining power of the creator of value to retain this value, although the nature of the isolating mechanisms may be quite different.**

**In the case of champagne, there is a key legal barrier determined by the AOC laws that control a wine's content and linkage with a delimited territory and the best indicator of success in the appropriation of value is the price obtained for champagne. I will review both ideas in this section.**



Price

**Value creation requires more than simply understanding what the customer or society is willing to pay for (Lepak, Smith, & Taylor, 2007). Instead the firm must recognize the existence of multiple targets – whether intended as such or not - that exist in concert and not in isolation. Champagne, as a region, has numerous ways of creating value for different customers that want a luxury product: large houses aiming at highly selective customers, large co-operatives targeting the mass market, or small-scale vigneronns who target the French market through relationships lasting generations. However, the variety of offerings may not sustainable if everyone feels that the appropriation of the value created is not fair. In the case of champagne, there is a delicate balance between value creation, the wine, and value appropriation, the price of the champagne. The higher the value created, the higher the price obtained as figure 10.1 shows.**

**TAKE IN FIGURE 10.1 ABOUT HERE**

**While the most important value generators are the champagne houses, which sell 66% of the wine and command the higher prices, there are gentlemen agreements**



with grape growers to buy their grapes at a fair price. One champagne house buys grapes directly from up to the 4th generation of grape growers in 17 villages using contracts lasting between 5 to 18 years. A manager of another champagne house said ‘there is no competition in grape growers but a gentlemen agreement, and if a grower changes there are huge penalties’, another manager said, regarding the fairness of grape buying deals, ‘we have to live here’. The social fabric, which was generated by history and tradition, determines the categorization of the different actors into faithful or unfaithful. Therefore, social capital acts as an important restriction to free riding behaviour for either houses or growers wanting to improve their appropriation of value. The price paid for grape is 5.50€ per kilo, which is one of the highest in the wine industry.

While champagne houses have all the resources, brand and distribution channels, to be able to appropriate the value from the French market, they target markets abroad. External markets are inaccessible in large scale for most of the vigneron unless they heavily discount their prices or ask someone else to manage their sales, which may erode the value of the champagne brand. Strong social capital has been built through resource investment by houses. One interviewee said ‘Growers understand that the situation of privilege (in terms of grape value and income



obtained) comes from the work of houses. For example, [when] phylloxera destroyed the vineyards, (champagne) houses subsidised the growers to plant new vines.’

Controlled origin appellation

The land devoted to grape growing under the champagne appellation has grown over years. However, the capacity of the region to grow grapes under the appellation has reached a limit in the last few years. As outlined in previous chapters, there is an extension of the AOC planned by 2015 but growers may be opposed to the revision and extension since new villages will be added to the AOC and the revision will add lot of new people with the right to grow grapes, thus diluting the economic position of existing growers.

The history of the development of the AOC has shown the importance of the learning process which has occurred in the area amid conflicts between houses and vigneron. These conflicts occurred due to misunderstandings of the process of value creation and free riding by some actors.



The region of Champagne grew very strongly during the 1800s altering the social fabric and economic relations of the wine community in the years leading up to the phylloxera crisis (Guy, 2003). By the time phylloxera made its entrance into the Marne region, vigneronns were fully dependent on the négociants for the sale of their grapes. However, radical fluctuations in the wine market showed vigneronns the problems of economic hardship. The control of champagne was contested between vigneronns and maisons as vigneronns' feared that house brands would be more important than 'terroir' (the vigneronns' unique resource); in the process village names like Ay or Sillery became replaced by a single territorial name - champagne - and there was a need to set boundaries in order to guarantee the consumers' confidence in the product which was plagued with fraud from unscrupulous merchants.

Within Champagne, the fraud that required government attention consisted of three related issues: counterfeiting of names of manufacturers or brands; using the denomination 'champagne' as a generic label for sparkling wine; or labelling a wine 'champagne' when the grapes had been harvested or the wine manufactured outside of the region (Guy, 2003). The first two issues, which were fundamental concerns of champagne négociants, were strongly pursued by the French government using



international laws regarding industrial property and French judiciary. While regional manufacturers obtained recognition of champagne as a denomination by the state, the boundaries of the region were ambiguous. The ambiguity was very useful for free riding négociants that committed fraud (although it was not illegal at that time). Fraud included wine fabrication with grapes grown in other French areas; or bringing wines from Lorraine, Burgundy, Anjou, or even Germany (Guy, 2003).

For the vignerons, champagne derived its quality and prestige not from the firms in Reims or Epernay that bottled the final product but from the land and the Champenois vignerons who cultivated it (Guy, 2003). Vignerons intended to develop a powerful tool, through the delimitation of the Champagne boundaries for punishing unscrupulous merchants who sacrificed the rural community for their profits. On the other hand Négociants considered that the best guarantee of authenticity for the public is to be the interests of them in maintaining the quality of their wine and the prestige of their brands (Guy, 2003). With consumer preference for the authentic brands, the law of supply and demand would eliminate unscrupulous producers. The resulting stresses, which produced the riots of 1911, have already been outlined (see chapters 1 and 5). Significant in all of this is the analysis of Guy (2003, page 157) who said ‘what emerges is a picture not of harmony





and consent but of conflict and compromise; a glimpse of a dynamic rural society struggling to define the boundaries of its community and the position of that community within the French nation. Hidden was the friction of a community in transition...part of a long and recurring battle to define roles within the regional economy and the community.’ And she added ‘the cause that propelled them (vignerons) into the streets in 1911 was quite simple: to protect the connection between champagne, the wine, and Champagne, the land and its terroir’ (2003, pp161).

The battle over the control (appropriation) of the economic and cultural heritage of champagne (and more importantly over the value created) was based on different definitions over the issues and boundaries of the community. There are always tensions between economic actors in the appropriation of value. These tensions have come to be managed through institutions such as CIVC, one of the key lessons from champagne for the rest of the regions. Thus, the next sections deals in more detail about the CIVC.



ACHIEVING A BALANCE BETWEEN VALUE CREATION AND VALUE

APPROPRIATION: THE ROLE OF THE CIVC

**In contrast to other wine regions, both growers and producers had achieved a balance between the creation of value and its appropriation through a third institution - the CIVC, with balance guaranteed by the co-presidents and a board of Directors composed by five directors from the SGV and five directors from the UMC. The board usually meets eight times per year, and one of the key meetings is to decide the harvest dates as well as other issues related to the harvest. The CIVC can sanction a producer if its product is not under the rules of the AOC and can declassify a producer from the AOC label but CIVC does not control the operations of the houses outside Champagne.**

**Even though the institution seems to have a political role, its daily operations run by a set of commissions and professional managers are fairly independent and highly technical. The members of the CIVC have long-term appointments. The institution has a number of specialist commissions related to technical matters, Communication and the champagne appellation, the equipment of the vine-growing area, champagne and health and after-sale quality. It employs more than 200**



technicians and is composed of a vineyard department which defines the dates from planting to shipping, and export department which assists: they help companies and vigneron to export, a trade department which registers the labels/brands under the AOC and an 'economic observatory'. Nowadays, the organisation has a number of functions which include the following:

- Registration of transactions between vigneron and houses
- Provision of statistical information and economic analysis to the level of a balanced scorecard for the chairs of the CIVC
- Performance of market surveys to evaluate quality and quantity
- At harvest time (jointly with AOC), the establishment of:
  - Yield per hectare
  - Pressing limits
  - Minimum alcohol level potential
  - Quality of the wine reserve
  - Dates of vintage

An important activity, close to the role of asset management in firms, is to register each land parcel in the region. By 2000 CIVC had mapped the whole region in 50 sq m size parcels within the AOC Champagne. the CIVC also has regulatory missions closer to asset management such as:



- **Recording vineyard ownership from vines planted to shipping of finished product**
- **Delivering professional licences to négociants**
- **Developing certificates of origin for exports**
- **Modifying the status of champagne négociants**

**The CIVC does not only have activities related to controlling the adequate balance between demand and supply or the assets in the region, CIVC is also responsible for innovations to improve standards in the region, including:**

- **Raising of environmental standards to support a green strategy using less herbicides and pesticides**
- **Reduction of pressing yields to improve quality of must.**
- **Increasing time in cellars after bottling**
- **Development of a particular yeast created for the region**

**The area related to innovation is formed by a Technical Research and Development section with more than 45 engineers and technician, a Viticultural and Oenological Department, which uses experimental vineyards (30 hectares.) and cellars, laboratories and vinification equipment, as well as collaboration agreements with universities in applied research.**



Finally, the CIVC is responsible for building the image of champagne in France and other major markets by controlling the way of promoting the image through websites such as [www.champagne.fr](http://www.champagne.fr) or [www.champagne.com](http://www.champagne.com), providing educational brochures, maps, DVDs, etc., as well as contacting the press for neutral information and the protection of the appellation in the World Trade Organization and bilateral agreements with countries. Since champagne is not a generic noun, CIVC is responsible for promoting abroad laws and regulations regarding the name, systematic surveillance and legal action against wrong use of the brand.

#### FINAL REFLECTIONS AND CHALLENGES

Champagne is a success story not only in terms of market positioning but in terms of achieving a balance between value creation and value appropriation. It is uncommon to see a balance between the process of value creation generated mostly by firms with distribution networks and the appropriation of the value from suppliers to these firms. This balance has to be obtained amid a highly complex business which includes the following characteristics:

- Large investment in real estate.



- **Technical aspects of production:**
  - **wines' purchase concentrated in 15 days,**
  - **assemblage of a large number of wines to obtain consistency,**
  - **purchase of bottles from diverse suppliers,**
  - **riddling and finishing the wine.**
- **Grape supply (89% from grape growers) determined by complex relationships (mostly social rather than commercial) affected by competition from other houses.**
- **Wines from different villages and different years.**
- **Long ageing process: two to ten years which implies high levels of inventory.**
- **The costs are half of the selling price and production costing is very complex.**
- **Long delays between decisions and impact: the vintage from good a year like 1997 was on the market in 2005-06.**
- **Labour: restrictive legislation, salaried employees, and conflicting trade unions (three syndicats).**
- **Both agricultural and industrial activity.**
- **Both supermarket and independent retail channels.**
- **Both long and short distribution channels.**



- **Both distribution subsidiaries and importers: sales in 120 countries.**
- **Fast moving consumer good = high turnover stock.**
- **Long time to market for innovation - three to ten years.**
- **The product is both wine (guardian of values) and luxury (high price, image, people).**
- **High level of social activities: there is a direct involvement in business function like buying grapes from growers due to social relationship**

Sustaining Competitive Advantage

**Champagne, as a region, has managed to achieve the four cornerstones of sustained competitive advantage, which positions and sustains the region as a leader in the wine industry:**

***Heterogeneity* refers to the presence of superior productive factors that are in limited supply:**

- **Champagne has a unique ‘terroir’ compared to other wine regions in the world.**  
**The combination of northern location and chalk produces high-acid grapes that make the unique taste of champagne combined with a cultural heritage that is impossible to imitate.**



- **Since there is no common formulation for champagne, each producer (large or small) has its own style determined by the proportions employed by each grape (pinot noir, pinot meunier and chardonnay) in the assemblage. This is an important aspect that may assure champagne's survival as champagne is not one homogeneous product but many heterogeneous products catering to different tastes and markets. There is a very fragmented supply with 5000 individual brands under the champagne umbrella.**

*Ex post limits to competition* is related to the forces that limit competition for the rents obtained from superior productive factors.

- **Champagne has obtained legal protection for its regional brand: AOC 'Champagne'**
- **Champagne has developed the large firms responsible for marketing sparkling wine: Moet & Chandon, Vranken-Pommery, etc. which create barriers to the development of stronger competitors in sparkling wine outside the region.**

*Imperfect mobility* refers to the factors that are somewhat specialized and which relate to the specific needs whose opportunity costs are lower than the value of the product in the current strategy.

- **The opportunity costs for employing the land located in Champagne in other types of productions are clearly lower than its usage in grape growing for**





sparkling wine. Therefore, the grape growers have an incentive to continue producing high quality grapes and negotiate with houses for grape supply.

- The costs of opportunity for the brands developed by champagne's houses are clearly lower when they are used in generic sparkling wine. Therefore, champagne's houses do not currently have an incentive to replace the sparkling wine production in Champagne with that from other regions.
- The historic relation of the region with royalty provides the region with a non-imitable intangible resource which enhances its reputation as a luxury product/wine drinkable in very special occasions.

*Ex ante limits to competition* refers to the limitation to competition for the establishment of a competitive position using the same resource:

- The existence of a centralized regulator for land transfers called SAFER means a limitation to local houses and foreign firms buying land in Champagne.
- The social networks existing inside the region are effective deterrence to free riding competitive behaviour.

These four cornerstones have not been achieved instantly but it was a long process of trial-and-error and reaction to opportunities and threats as this chapter has shown. The achievement of these four cornerstones is related to the development of



**a capability in the region, which is difficult to imitate elsewhere, the management of a delicate balance between value creation and value appropriation. This is one of the key lessons of champagne - the necessity to articulate institutions at regional level that are able to protect and nurture the capability of maintaining balanced relations among different actors localized in the same geographical region.**

### Challenges

**Champagne is not exempt challenges. The challenges are actions or events that may erode the pillar of its current success. This includes the fact that champagne houses lately have started being managed from outside Champagne. There may be issues of social capital and networks, especially with the relationships with vigneron and other maisons, affecting the region in the future. Since most of these firms are listed on the stock exchange, they need to show steady financial results and this may affect social relations.**

**Further, there are two possible competing strategies for champagne producers: volume and value. Each may be attractive to co-operatives or houses (although the former may tend to go for volume and the latter for value). However, the adoption**



of one strategy by one group of actors will have an impact on those who chose the alternative course of action.

There is concern of the lack of enough supply in the short term which generates pressure on value appropriation actions between vigneron and champagne houses. Increase in grape supply by adding 40 new villages under the AOC but it will take 10 years to reach productive stages.

The new generation of people may change the culture in the management in the medium term: prosperity vs. *mévente*.

Global warming may affect the style of wines in the long term.

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<sup>i</sup> Guy (2003) described many of the earliest champagne families' successes as the stuff of legend.

These families became legends in the world of fine wines like Moët and Clicquot.

<sup>ii</sup> Currently, Moët alone sells 28 million bottles of non-vintage champagne, and total sales from the region is around 300 million bottles p.a..

<sup>iii</sup> For example, Laurent Perrier, which is number three in terms of value and was created in 1812, has five subsidiaries established in USA, UK (No.1 export market), Belgium, Swiss and Germany to sell the product mainly to restaurants and cafes.