Case Study

The owner of the prestigious Château de Vallois must decide whether to launch an affordable wine. *by Daniela Beyersdorfer and Vincent Dessain*

Preserve The Luxury Or Extend The Brand?

The Experts

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HBR's fictionalized case studies present dilemmas faced by leaders in real companies and offer solutions from experts. This one is based on the HBS Case Study "Marketing Château Margaux" (case no. 507-033), by John Deighton, Vincent Dessain, Leyland Pitt, Daniela Beyersdorfer, and Anders Sjoman. It is available at **hbr.org**.

ILLUSTRATION: LARA TOMLIN

Gaspard de Sauveterre shivered as he stepped out of a side entrance to his château. While the late September days were still warm, he could feel autumn approaching. The 75-year-old owner of Château de Vallois, a famous wine-producing estate in the Bordeaux region of France, felt a familiar thrill. This was the season he and his team had worked toward the whole year; any day now the bell for the harvest, the famous *vendanges,* would ring. He quickened his pace down the long, well-kept alley through the wrought-iron gates to start his ritual morning walk through the vineyards.

He loved these hours when the rising sun bathed the misty landscape in shades of yellow and gray. The quiet, cool air cut through the thoughts that had been swirling in his head since his granddaughter burst into his study yesterday with an audacious proposal.

Claire de Valhubert had grown up on the estate but had moved to Paris following the sudden death of her mother, Gaspard's daughter, seven years ago. After graduating from one of France's elite *grandes écoles* she had worked for a top consulting firm before earning an MBA at Insead. Gaspard had expected her to come for the harvest, of course—she never missed it—but he had been surprised to hear about her plans to join the family business and radically change the centuries-old enterprise.

Claire had explained her idea as simply as possible. In her opinion, younger wine enthusiasts were being priced out of high-end French wines. And although she knew that de Vallois had been steadily profitable since the 1980s, she worried about what might happen if the estate allowed less-expensive, lower-quality winemakers, particularly those from outside the traditional wine-making regions of Europe, to capture and retain the next generation of customers. She wanted de Vallois to enter the "affordable luxury" market, selling

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directly to customers, as some of the other top traditional Bordeaux estates had done.

When Gaspard mentioned the encounter to François de Sauveterre—his son, Claire's uncle, and the château's CEO—later that evening, François' first reaction was to raise a skeptical eyebrow. But he agreed to give his niece a hearing; after all, she had inherited her mother's 25% share of the estate, the same stake he held. Gaspard had the remaining 50%, and although François had taken over day-to-day operations five years ago, the elder de Sauveterre would certainly weigh in on any change in strategy, particularly one as dramatic as Claire's.

A Rare Vintage

Turning into the fields, Gaspard saw Jean-Paul Oudineaux, his estate manager, crouching over a vine and carefully examining its grapes. He had hired Jean-Paul, then a young agricultural engineer, 30 years ago after buying Château de Vallois.

The estate had fallen into a slow decline under its last owner, but together, Gaspard and Jean-Paul had restored it to its former glory. The essential ingredient had always been there: a *terroir* with the ideal soil and microclimate, which, according to the French, determines a wine's character. In a ranking of Bordeaux wine estates that recognizes their long-term track record in quality and reputation, de Vallois had in 1855 been classified as a *Premier Grand Cru Classé* (First Growth), which allowed the estate to command top prices for its wines.

Gaspard and Jean-Paul had overhauled the vineyards, improved the drainage, and subtly adjusted the blend. In time, the château produced perhaps the greatest of Bordeaux's five grands crus classés. It now sold about 150,000 bottles each year of its *Grand Vin du Château de Vallois,* a combination of carefully selected cabernet sauvignon, merlot, petit verdot, and cabernet franc grapes. The estate used the best of the remaining grapes to produce a second wine, the *Puiné,* averaging 200,000 bottles per year. The rest were

> "Vines are like children: They need to be looked after very carefully."

sold to other estates on condition that their origin would not be revealed. It was a good business and had kept his children comfortable, but he sometimes worried whether it would sustain future generations of de Sauveterres.

"I think we are almost there," Jean-Paul called out as Gaspard approached. "Just look at these grapes! This year could be even better than 2005."

Gaspard was not surprised; the weather had been warm and fairly dry all summer. "We could start picking Friday," Jean-Paul continued, "but I'd prefer to wait until after the weekend. The weather forecast is for a few showers and a drop in temperature, and I think that would add a little freshness." Plucking a few grapes himself, Gaspard concurred.

As he felt their tannic sweetness tease his palate, Gaspard asked Jean-Paul if he had seen Claire. Jean-Paul smiled, "No, but I'm sure I will. She hasn't been here the whole summer, so she'll inspect every corner of the place to make up for it."

"Well, you'd better prepare yourself," Gaspard replied. "She wants to make a branded wine and sell it directly."

Jean-Paul sighed. "You know what I'm going to say. Vines are like children: They need to be looked after very carefully. It's the same with selection and blending. Without 100% dedication to excellence, you cannot make outstanding wine. We already do two wines. Isn't that enough?"

Trusting in Tradition

Later that morning, Gaspard picked up a set of ancient keys and descended to the cellars. He entered the vaulted first-year section, in which the best of last year's harvest was aging in neatly aligned oak barrels stamped with the château's emblem. Around 70% of this still-maturing wine had already been sold to specialist merchants called *négociants* under a centuries-old arrangement designed to let noblemen stay out of commerce. The négociants bought the wine a year before bottling and then sold it to distributors and importers. Visitors were always surprised when told they could not purchase a bottle of wine directly from the château.

Prices for fine wine fluctuated widely, depending on the quality of the vintage, the reputation of the producers and négociants, and the expected demand, and they were increasingly influenced by the opinions of expert critics. Château de Vallois collected between €100 and €450 up front for a bottle of Grand Vin, for which a U.S. customer, for example, might pay $999 now for delivery a year later. Some of Gaspard's fellow grand cru classé owners complained about the négociants' margins, but Gaspard accepted them. He knew he could rely on the négociants to buy up Château de Vallois' total output, even in bad years, in order to maintain the relationship. What's more, since growers were paid in advance, the income from the sale made financing production a lot easier.

Gaspard unlocked the door to the private cellar, which housed almost every vintage the estate had produced. As he strolled among the ceiling-high racks, he looked up at the last two bottles from 1848, both covered in dust.

"I thought you'd be here, Papa, " François said, walking in. "I wanted to talk privately. Claire's idea is not going to work. In a good year, we don't have enough grapes for a third de Vallois wine, so we'd have to buy more and make a branded wine. If word got out about that, people could start worrying that we're mixing those grapes in all our wines. Also, there are risks to marketing our wine ourselves. We can charge a high price for it because it's exclusive and customers can only get it through a few, up-market providers. If people think we need to push it, they might not be willing to pay so much."

"Claire has thought about that, too," Gaspard said. "She's thinking of keeping the new wine separate."

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François shook his head. "Well, that's no answer. You know some of the négociants may not like to see producers of grands crus classés adding branded wines. So not only would we have to invest in a distribution channel for which we have neither the experience nor the means, but we'd also be risking the goodwill of the people who sell the wine we're currently making."

Gaspard knew his son was a traditionalist. Although he himself still felt like a stranger in Bordeaux after three decades, François had become well connected through his marriage to the daughter of an important négociant family.

"You know, Cécile's family has been in the business since 1739," François pointed out. "They are as experienced in distributing wine as we are in making it. They take care of all the marketing, insurance, and transport stuff that we'd have to manage otherwise, and they can tell just where to draw the line between exclusivity and scarcity. They know to whom we should be selling and who to avoid. How would we even determine what price to set each year? Granted we might get bigger margins selling directly in a good year, but what are we to do in a bad one?"

A Case for Change

That evening, Gaspard walked up the main staircase and entered the *salon jaune*. The rich polish on the furniture glowed in the soft candlelight, and the crackling fire was piled high with vine branches that scented the air. He took a seat by the hearth and was reaching out to a dish of almonds on a side table when his granddaughter came in.

"Are you all right, *grandpapa?*" Claire asked, looking at him closely. "Am I first for once?"

Gaspard smiled, "It is good to have you back here, my child. Sit down, and tell me what you have been up to today." She was about to answer when François, his wife, and Jean-Paul came in together.

"We just heard the latest forecast and we've agreed to start the harvest on Monday," François announced. The three took their seats and Gaspard handed the almonds around. "I've asked for dinner in the kitchen tonight," he said. "It will be more intimate, and after all, we're *en famille.*"

The château's authentically preserved kitchen, with its enameled ranges and open fireplace, was certainly more intimate than the dining hall, but tonight's table was nevertheless dressed with flowers, starched linen, and fine porcelain. Each place was set with silver and four crystal glasses for the different wines that would accompany each course.

Gaspard could tell that Claire was eager to talk business from the moment she sat down, but she managed to contain herself until the main course. She took a sip of the 2001 Grand Vin that accompanied the soft *agneau de Pauillac* on her plate and turned to Gaspard. "Grandpapa," she began, "I know what you were thinking yesterday: 'Here she comes, her head all filled with business school nonsense.' But I really believe that we aren't realizing even half of what this estate is worth."

> "If we can make such great wine here, why not make a wine for younger people somewhere else?"

Seeing his son frown, Gaspard quickly replied, "Not at all. I may look like a dinosaur, but I am always open to new ideas. I'm sure your uncle agrees."

Sensing encouragement, Claire forged ahead. "I propose that we introduce a branded wine at a price of about €20 to €25 a bottle. Our first wine is way beyond what most people can afford, particularly the older vintages—even a bottle of the 2000 sells for about €1,000. And our second wine, at €100, is still too expensive for the average person, particularly younger people, to buy regularly."

She looked at François: "I know this would work only if we produce at least one million bottles, so we'd have to buy grapes. If you're uncomfortable with that, we could buy more land instead and grow them. We can't claim a Château de Vallois origin on this wine's label, but with Bordeaux grapes or land, we could at least state 'Bordeaux origin.' Good land here is expensive, but we could also buy overseas, like some of our competitors. Why not make a branded wine with California grapes and a label mentioning that our de Vallois team is in charge of it? Why shouldn't we capitalize on our brand? And if we can make such great wine here, why not make a wine for younger people somewhere else?"

She continued, "Of course, to do this we would need our own distribution channel. We know, in fact, many of our customers, particularly the specialized importers, from their château visits. For others we could set up our website to allow them to order directly. Many are already asking for this."

Claire paused to taste her wine and seemed bolstered by its elegant, balanced flavor.

"Finally, I know how we all feel about even the best New World wines—not aging well, too heavy, too fruity, no matter what Robert Parker says. But we can learn a lot from those producers in terms of marketing. They run great advertising campaigns and do market research, which means they can adapt quickly to changing tastes by changing the flavors they offer.

"I'm not suggesting that we meddle with our first wine, but with a branded wine we could be much more flexible, and that would give us a chance to attract younger consumers, get ahead of drinking trends, and make sure that when they're ready for more expensive wines, they'll come to us."

François pushed his plate away. "My dear, please don't take this badly," he began carefully. "I do consider how we can touch young customers and enhance our revenues—every CEO does. But I think you're completely misguided. We might

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not take full advantage of our reputation, but isn't that partly why we have such a good one? And why spend money on a whole marketing and distribution machine for a low-priced wine?"

Jean-Paul stirred uncomfortably. "Who will make this branded wine anyway?" he growled. "I have neither the expertise nor the interest in making fruity wines with other people's grapes."

Gaspard took advantage of the silence that followed to call a halt: "I think that's enough for now. Let's continue this discussion in the boardroom tomorrow."

Time to Harvest?

Gaspard found the boardroom empty when he returned from his walk the next morning. He had woken up early, replaying last night's conversation over and over in his mind.

His son was right to worry. The aura of exclusivity around the first wine could easily be destroyed if people started to think that the estate was tampering with it. But Claire had a point, too: They had gotten too caught up in their routine of creating the perfect grand cru classé. Well, if nothing else, he reflected, she was making them think and would be a good sparring partner for François in the years ahead.

The two were at loggerheads, but Gaspard had not completely retired yet. It would be up to him to cast the deciding vote.

Should Château de Vallois begin producing a more-affordable wine?

See the following two commentaries.

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The Experts Respond

Corinne Mentzelopoulos is the owner and CEO of Château Margaux.

THE DILEMMA presented in this case underscores a constant issue for those of us working in fine and rare wines, such as Château Margaux. Balancing the competing demands of growth and quality is never easy. Nevertheless, I would advise Gaspard de Sauveterre not to add a branded wine at this time, even though the market for fine wine is growing very fast, driven mainly by emerging markets such as China (where the demand is particularly remarkable) and India.

Château de Vallois benefits enormously from its *Premier Grand Cru* status and from the reputation of its *Grand Vin*. Because the grapes must come from the estate's classified plots of land, de Vallois can produce only a very limited number of bottles per year. At the same time, it must try to ensure broad distribution through the *négociants*. François de Sauveterre is right to point out that this restricted availability helps preserve the estate's exclusive image and that any attempt to change the traditional, albeit successful, way of doing things could easily alter the wine's perceived value in the eyes of both the industry and the consumers.

What's more, Jean-Paul Oudineaux already has his hands full maintaining the quality of the estate's intricate, highly complex, production process. The quality of each vintage varies with the climate, and even in an excellent year, planting, plowing, crop thinning, harvesting, blending, aging, and bottling all require very careful management and coordination to produce a truly first-rate wine. Any change in the conditions of the soil or climate—no matter how slight—or variation in the quality of the grapes, for example, will require timely adjustments throughout the year and subtle alterations in the final blend.

In addition, the estate's management has no experience in successfully launching and capitalizing on a brand with a lower price point. They do not know the mass-market segment of the wine business and its distribution channels, and they don't know this new segment's customers because they have always conducted business through the négociants.

Finally, if Jean-Paul were to take responsibility for producing a branded wine, he would necessarily have less time for tending his main responsibility, and the existing wines would likely suffer as a consequence. To avoid that result, the estate would, at the very least, have to recruit a new manager for the branded wine—which might lead the market to believe that the focus of the estate's proven expertise could be diverted from Château de Vallois itself. Besides, launching a new branded wine from scratch would constitute a significant investment.

Any attempt to change the traditional way of doing things could alter the wine's perceived value in the eyes of both the industry and the consumers.

Of course a wine-producing estate, just like any other company, has to protect its financial future. It's wise to periodically question the business model and examine opportunities as well as threats. Even estates that rely heavily on time-proven expertise, like ours, must constantly keep an eye out for new ideas, methods, and equipment that will help them remain at the top. Claire de Valhubert would be a valuable addition to de Vallois' management team in that regard, and Gaspard should certainly encourage her to join the business. But because the de Sauveterres operate in a high-luxury niche, they should refuse to transform the estate into a more industrial business and resist the temptation to add a branded wine for the mass market.

Philippe Sereys de Rothschild is the Vice Chairman of Baron Philippe de Rothschild.

SHOULD THE de Sauveterres explore new opportunities in the branded-wine segment? Absolutely. But they should proceed very carefully. Because first-growth and branded wines involve two entirely different markets, they must be managed completely independently. Nevertheless, many companies in high-end or luxury markets have successfully grown by branching out; my family's firm is one example. We have done so by clearly separating our estate wines (specifically the first growth) from our branded wines. In the current worldwide wine market, protecting the unquestionable quality and image of the first growths is paramount.

It is only natural for François to worry about eroding the de Vallois brand, since his responsibility is to make the best possible first-growth wine for the highly selective top end of the market. He should remain fully focused on that production and not lead the new venture, though he could oversee the work of the separate, branded-wine team to make sure that the new product is of very good quality.

Moreover, the prices for first growths have skyrocketed in recent years, partly because of the growing number of wine connoisseurs around the world and emerging wine markets, such as China and India. If we want to keep younger wine drinkers buying and consuming good-quality wines at affordable prices—and attract future high-quality-wine drinkers as well—then companies like ours, with superior reputations, must make good-quality branded wines available at competitive prices. They can be made under the umbrella of the original group, but the production and distribution chains must be clearly separated. One option is to create two discrete business units within the group.

If the family does decide to develop the branded wine, it will need to put in place a distinct marketing and distribution strategy. Given the estate's traditional first-growth positioning, the de Sauveterres will have to emphasize that the move will not compromise the *Grand Vin*. They could position their campaign, for example, as pursuing a mission to create a wine with the best relationship of quality to price so that members of the younger generation will start off drinking good products and then upgrade to more-expensive, luxury wines later on.

Companies with superior reputations must offer good-quality branded wines at competitive prices.

Marketing the new branded wine directly would give the de Sauveterres a better understanding of the wine market in general and how it might evolve. It would also help them learn about distribution, which could be useful if they want to continue growing their business in the future.

For the sake of harmony, I would advise Gaspard to encourage Claire to join the business; any family member who wants to do so should be allowed to find a position. However, she must build up and carve out her own area of responsibility, which in this case could be the branded wine.

Wine is an interesting product, and personal preferences can vary greatly. I often sample and enjoy wines from all over the world. And though, like the de Sauveterres, I prefer the fine old Bordeaux wines with length and full body, that does not mean that the more immediately seductive, New World wines are not worth making or that I shouldn't make them.

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CHÂTEAU DE VALLOIS is suffering from a classic family business problem. Each member feels that he or she has the right to pull the business in his or her direction. Instead, they need a board of directors with a nonfamily majority, one that will create a complete business plan, not just agree or disagree on marketing a new wine.
Tony Gregory, *CEO, CODA Business Management*

I WOULDN'T go from exclusivity to a wide market. Instead, create an even more exclusive wine, perhaps 5% of total production (but with higher margins), sold directly from the chateau, as a brand extension. Such a small quantity would neither require more grapes nor harm the *négociants'* business. Even better, the prestige of the whole de Vallois brand would increase because of the new wine's scarcity.
Alen Gojceta, *midmarket sales manager, IBM Croatia*

GASPARD SHOULD venture into the affordable wine category but via a subsidiary, with a professional CEO and managers. Claire is enthusiastic but not sufficiently mature as a businessperson; she could play a more suitable role, such as strategist. The venture should focus on younger and first-time buyers, as well as restaurants that cater to such clientele, in markets such as America, Latin America, southern Europe, and Asia.
Vivek Kochikar, *associate vice president and principal researcher, Infosys Technologies*

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