

Post-vintage bulk wine review



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Introduction

The purpose of this article is two-fold:

- to provide an overview of the current bulk wine market by analysing some of the main varieties and styles
- to provide an overview of wineries to see how the large, medium and small wineries are currently faring in relation to bulk wine.

Bulk wine market overview

In the aftermath of an abundant 2004 vintage, we have observed a number of trends in the bulk wine market and some of the major ones are detailed below. All prices are ex-works for spot domestic sale with short delivery periods and short payment terms.

Regional (or dry land) reds

The market for regional reds is now quite polarised. Small parcels of excellent quality wines, usually barrel-aged batches

reflective of their regional style, are attracting buyer interest at excellent prices of \$2-\$3 per litre. Some parcels are even fetching as high as \$4 per litre. However, these wines are of the very best quality available and as such reflect only the top 5-15% of available volumes. Moreover, the volume of each individual transaction of such wine is usually fairly small, and this segment of the market is extremely thin.

These prices are not (yet) achievable for 2004 wines and this is mainly due to some unsustainably low spot market prices that prevailed for 2004 dry land red grapes. In other words, potential buyers are not really interested in paying much for 2004s, having just built up inventories using grapes bought during vintage at very low prices.

For the 85-95% balance of regional red wine volumes, prices are extremely soft, and are approaching south-eastern Australia bulk prices. Either these batches are not in the top 5-15% of regional wine quality, or there are simply too many equally good wines available for sale.

Shiraz

Prior to 2004 vintage, Shiraz prices were in the \$1.20-\$1.50 range, however, since vintage there has been some downward pressure on pricing, particularly for older vintage stock. Most of the activity that we have witnessed is for pre-2004 vintage south-eastern Australia wine in the \$0.90-\$1.40 range. Transactions above this range have occurred for small volumes of better quality parcels or below this range for poorer quality wines.

At the time of writing (June 2004), the demand for 2004 south-eastern Australia Shiraz is very weak; traditional domestic buyers are now generally sellers and it is still a little too early for many international buyers to be looking at 2004s. Accordingly, due to few transactions, determining an established market price 2004 south-eastern Australia Shiraz can be tricky. These observations are equally applicable to Cabernet Sauvignon and Merlot (see below).

Cabernet Sauvignon

This seems to be everyone's least favourite variety at present, for both south-eastern Australia and regional appellation wines. Prior to vintage, prices for south-eastern Australia Cabernet Sauvignon were in the \$0.90-\$1.30 range, however, for these same wines, the price range is now more likely to be \$0.60-\$1. As with 2004 Shiraz, there is little current spot market demand for 2004 Cabernet Sauvignon.

Merlot

Even though it is a soft-sounding word, Merlot is hard. Hard on the palate, hard to extract flavour and hard to find a buyer. International demand for this variety is sporadic at best. The price of good Merlot with reasonable depth of flavour mirrors Shiraz pricing, but it is extremely hard to find good Merlot. Average or

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poorer examples are selling for generic dry red programs with pricing \$0.60-\$0.90 per litre typical.

Chardonnay

Despite reasonably generous 2004 inland crops, there is still good demand for south-eastern Australia appellation Chardonnay. Prior to vintage we expected that the broad-based Chardonnay shortage experienced from the short 2003 Chardonnay crop would rectify itself during the course of 2004 vintage. However, we were not correct, and the market is still in slight undersupply.

In addition, the market is finding it extremely difficult to accept Chardonnay tied to reds (which was not uncommon at various times throughout 2003). There were also some quite generous crops of regional Chardonnay from places like McLaren Vale, Limestone Coast and even Western Australia where Chardonnay was acutely short prior to vintage.

Good quality south-eastern Australia 2004 Chardonnay is fetching around \$1.80-\$2.20 per litre, older vintage wine \$1.50-\$2 and 2004 regional Chardonnay sellers are asking \$2.25-\$3 but with little buyer interest at the higher levels. Any transactions of regional wine have been at, or in some cases of lesser quality even below, south-eastern Australia prices.

Sauvignon Blanc

In summary, the 2004 harvest produced some abundant crops of regional whites such as Sauvignon Blanc from the regional Victoria, Limestone Coast and the Adelaide super zone.

Quality is a little variable, however, and as with regional Chardonnay, asking prices are still quite high (low \$2 up to, and even above, \$3 per litre). There is, however, very little buyer interest at the higher price levels. South-eastern Australia Sauvignon Blanc is experiencing good demand from a small number of buyers with prices firming in the \$1.50-\$2 per litre range

Dry white/dry red

Over the past couple of years, many wineries have experimented with turning their excess red grapes into white wine. During 2004 vintage, anecdotal evidence suggests that this had become quite a mainstream practice occurring at a significantly higher level than previous years.

As a result neutral dry white, which was short before vintage, is now reasonably well supplied as Sultana, Chenin Blanc and the like have been replaced by water-white Ruby Cabernet, Cabernet Sauvignon, Grenache and Mataro. The results of such white-from-red programs have been generally pretty good, and it is fair to say that this year's products that we have tasted are the best that we have seen during the past couple of years.

Conversely, but upon analysis not really surprisingly, 2004 vintage dry red at budget pricing between \$0.60-\$1 per litre is relatively hard to find!

Winery overview

Over the past year we have observed quite different reactions to the current well-publicised supply challenge (and opportunity!) from different winery groups within the industry. I would like to share some of these observations with you and they are set out below:

The major wineries

Generally speaking, with a couple of notable exceptions, the big (mostly publicly-owned) wineries have red surpluses and have varied positions on whites. Many, if not all, have taken significant inventory write downs at some stage since the big 2002 vintage. Furthermore, they are actively working through excess stocks using various strategies including bulk sale, increasing buyer's-own brand offerings and reducing contracted grape intake. Naturally, these are the companies that will have the biggest

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impact on the market, since between them they control well over 50% of production assets (and a much higher percentage still of branded sales).

With teams of sophisticated marketers, well-financed large sales forces, and an unemotional attitude to taking pain where market realities dictate, these companies are now extremely focused on their bulk wine stocks and are working very hard to clear excess inventories.

I may be expressing a minority view, however, I think that the large wineries will be extremely successful at this task; probably at a rate faster than they themselves and many other observers expect. If a single major winery (or alternatively a US importer) is successful in developing another significant extreme-value US brand, this process will be further fast tracked. The supply opportunity certainly exists for this to occur.

As Australia's major wine exporters, endeavours in this area will be well assisted by the A\$ falling from recent highs near US\$0.80 that occurred during February this year.

The mid-sized wineries

The next tier down, generally consisting of the medium-sized inland irrigated wineries and/or those with not insignificant brands that are either family-owned or ASX-listed, somewhat surprisingly, have relatively tidy inventories. Most, although not all, carry only modest (and certainly manageable) surpluses of current and older-vintage reds which can be used for business development work, and many plan to buy or are already buyers of bulk wine (both red and white) in order to meet growing export orders at budget price points.

A number of these wineries mopped up good quality surplus red grapes at the end of vintage at bargain-basement prices. These companies have worked very hard since 2002 vintage to be able to meet lower price points and move excess stocks with a

reasonable degree of success. They are in a relatively sound position, mainly through offering budget level grape prices during the past couple of years in order to meet falling price points.

Despite their brands being smaller, less diverse and hence usually less well known than the big companies, many of these companies are travelling reasonably well. They are, however, most likely to come under the most pressure in the current climate of supermarket supply chain rationalisation, since they are at risk of being of insufficient size or strength to be a "must have" supermarket supplier.

The smaller wineries

The final tier consists of the rest and this is where there is still significant pain being experienced. Often undercapitalised, in some cases these companies are unable or unwilling to take inventory write downs, perhaps due to fear of unsettling nervous bankers. Alternatively they are simply finding it very hard to accept the going spot market prices and are unable to successfully meet seemingly ever-falling price points. These companies, as a broad generalisation (which of course risks over-simplification), have probably been the least-successful group in meeting the new marketplace realities for bulk wine.

Sometimes, asking prices for bulk wine from these wineries are not at (or sometimes not even near) market. So these companies are often finding it difficult to shift their bulk surpluses with any measure of success. Although many are much more realistic now than they were, say during 2002, a number have consistently asked \$0.10-\$2 per litre above the prevailing market price. This has resulted in bulging inventories, as they simply followed the spot market down with few sales to show for it. Alternatively, they may have finally been forced to accept a ridiculously low (and value destroying) price just prior to this year's big vintage in order to clear tanks.

Perhaps one of the reasons for this phenomenon is due to conflicting market signals that such wineries may be receiving, as many of these producers are also grape sellers to larger wineries on long-term contract, where prices are usually significantly above current spot prices. Alternatively, they may be receiving insufficient market signals through low investment in sales and marketing capability. In any case, the result has been ballooning bulk wine stocks delivering stressed balance sheets, nervous bankers and equally anxious proprietors.

Happily, the new WET producer rebate contained in the recent 2004-05 Federal budget is a most welcome relief to this group, as it will clearly improve overall winery profitability.

So where are we heading?

The abundant 2004 vintage has brought challenges, and in some cases opportunities, for each of the major industry winery groups summarised above. There is no doubt regional (or dry land) reds are in clear oversupply, however, the oversupply of south-eastern Australia reds is nowhere near as great and Chardonnay at budget prices is slightly short.

In closing, it is useful to draw a parallel with the early 1990s and the short-term oversupply that occurred back then. That oversupply helped bring about a range of opportunities so diverse and of such magnitude that it spawned an entire new level of growth that has increased the depth, maturity and long-term strength of the Australian wine industry. I think our current supply challenge will bring us similar opportunities.

Jim Moularadellis is the principal of Austwine, Australia's No.1 bulk wine broker which transacts 30-40 million litres of bulk wine within Australia and exports over 10 million litres of bulk wine per annum. He is a Certified Practising Accountant and holds an Honours Degree in Law from the University of Adelaide. He can be contacted on +61 (0)8 8431 8344.

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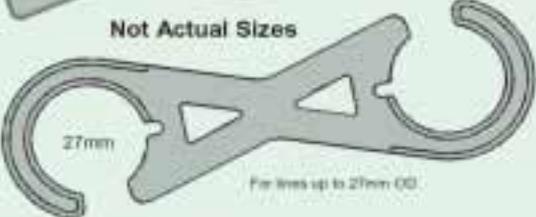


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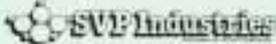
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