



Perception, Reality & the Last Laugh

Two teams of hikers, each crossing a glacier, approached a crevasse. One team saw the crevasse in time and stopped. The other team did not see the deep hole in the ice until the leader had fallen into it, at which time it became rather dramatically perceptible. Different perceptions obviously result in different actions. Perception, in this instance, changed action but perception did not change reality: the crevasse was really there whether noticed or not. Human systems, however, can be more complicated because perception can actually change the reality, at least to some degree.

Consider a thought experiment in the bulk wine market. Imagine 100 sellers of bulk wine and 100 buyers. The amount the sellers want to sell happens to be exactly the amount the buyers need. In the first scenario, however, all of the players think (falsely) that the market is short of supply. Because of this perception, buyers are eager to purchase as soon as possible and they snap up any wines offered, often paying full asking price in order to secure the purchase. Sellers take this as absolute proof that the market is short and they are convinced that prices will increase over time. Most of them wait to put up wines for sale. Buyers get increasingly anxious as few wines are listed and they bid up prices, confirming the sellers' perception of a short market and rising prices. By the time most sellers list their wines, buyers are ready to pounce on whatever they can get their hands on in order to finish blends prior to harvest.

In the second scenario, the market is again perfectly balanced but this time buyers and sellers perceive the market as long. Sellers are worried that they might not be able to sell their wine and so they rush to get the wines listed as soon as possible after harvest. Many wines come on the market but buyers figure that the longer they wait, the lower the prices and the better the selection. Few wines sell and sellers drop their asking prices. A few buyers cherry pick the best lots and three or four make low-ball offers. Most buyers wait and sellers get increasingly desperate. By the time buyers are ready to make their move, the sellers will take just about any offer, especially if they need to empty tanks prior to harvest.

The same amount of wine changes hands in both of these scenarios. Exactly the same balance between supply and demand was made to act like a short market or a long market, depending entirely on perception. But perception can do even more than that. Perception can – for a while –



But perception can do even more than that. Perception can – for a while – make a short market behave like a long market and visa versa.

make a short market behave like a long market and visa versa. In this case, however, reality gets the last laugh. If most players think there is a shortage of supply even when there is really a

developing excess, buyers will rush to buy and sellers will be slow to sell and the market will act like a short market, confirming the initial perception. This can only last for awhile, however. Before long, more sellers will emerge and buyers will fulfill their needs and step out of the market. Sooner or later, the excess of supply will become evident and perception will come into line with reality, often with a violent correction. The same short-term mix-up and eventual correction will happen with a short market that is perceived by the overwhelming majority to be long. Sellers will be anxious to sell, buyers will delay buying and the distressing symptoms of a long market will appear. Eventually, heel-dragging buyers will make their move – only to discover that many other buyers are making the same move at the same time and they all want the same lots of wine.

How does this apply to the current market? Unfortunately, there is no way to get an absolutely objective view of the total balance of supply and demand (although our publication, *The Turrentine Outlook*, does provide the most comprehensive overview). The market is certainly behaving like there is a significant excess. Grape sales in general are very slow even as summer begins and crush draws near. The bulk market is also slow for most varieties. Sellers are very anxious to sell. A few buyers are cherry-picking the best quality lots but most buyers are pretty quiet. What no one knows for sure, however, is what volumes and price-points of wine our old friends, Connie & Conrad Consumer, are going to want. More than any other factor, the ultimate direction of the market during the next year will be determined by this unknown consumer demand. If past patterns prevail, at some point, Connie and Conrad may feel that the worst of the recession is over and that they can splurge at least on little things, like good wine. This may not happen for six months or twelve months or eighteen months or twenty-four months. When it does happen, however, it will catch the wine business short. Consider the following factors:

1. Banks are still under pressure to enforce lending standards and credit remains tight. This forces everyone from restaurateurs and retailers to wholesalers and wineries to keep inventories unusually thin. This often leaves growers stuck with inventory because there is no one else upon whom they can push it back. An improvement in consumer sales would help ease the credit-crunch and cause the supply chain to replenish.
2. We are not likely to see the same big imports of Australian Chardonnay this year as there was last year. The 2010 Chardonnay crop was down in Australia and the Aussie dollar is stronger against the U.S. dollar than it was at the time of the big influx, increasing the cost of importing Australian wine. Supplies of the main varieties from other global producers most competitive with California are not way out of balance.
3. Rain, wind and cloudy weather in California during bloom for many earlier varieties in many regions may have reduced the expectations for a big 2010 crop – and could also affect bud fruitfulness for 2011.
4. There are ample quantities of 2009 reds on the bulk market. In tough markets, however, sellers do not always invest in oak and other finishing that costs real, out-of-pocket dollars. When winemakers finally get the green light from finance to purchase 2009 red wines, they may not have time to finish the wines before bottling. In the midst of an excess of supply, there could be a shortage of red wine that is actually usable as just-in-time inventory.

The grape and bulk wine markets are likely to be tough until consumer sales have established a clear trend towards both increasing consumption and increasing price-points. And nobody knows for sure when that will happen. In times like these, growers and wineries need to remain flexible, doing what is necessary for short-term survival but also keeping an eye on future opportunities. You could compare the challenges to a hike across a glacier. For safety in perilous conditions, it helps to consult with a guide who has explored much of the glacier and knows where the crevasses are and how to find the best passages around them. Give us a call to identify the opportunities for your unique situation over the next few months, and years, in a constantly changing supply and demand equation.

Bulk Market Review

Chardonnay

Chardonnay wine in bulk shows some movement, with recent sales from all regions. Supply, however, is significantly above current demand. Great bargains abound for Chardonnay from all regions of Sonoma County, Napa Valley, Monterey County, Santa Barbara County, and the Interior regions. Buyers have been selecting the better quality lots and recent sales of Sonoma County wines have been in the \$6-\$12 per gallon range, Napa Valley in the \$7-\$13 range, Central Coast \$4-\$8. We have recently sold truckload quantities of California appellation Chardonnay in the \$4-\$5 range. The Winemakers Federation of Australia has estimated that their 2010 Chardonnay crop decreased from 2009 by 24%, to 315,000 tons. Australian bulk prices have been firming up, mainly driven by the mid-sized companies for domestic or export needs, but there are still excesses on the market and prices are below sustainable levels.

Pinot Noir

We are seeing more Pinot Noir on the market than we have seen in many years, but we have had active buyers throughout the season. Early in the year, the supply of California appellation Pinot Noir was limited but 2009 was a big harvest in the Interior and more gallons have continued to come on the market. The high end of the market has been suffering from the effects of the recession and many brands have tried to reduce inventories through bulk market sales. There has been some opportunistic buying from wineries starting new brands or extending blends for brands that appeal to cost-conscious consumers. Volumes are still available for new opportunities. Recent sales for Sonoma County Pinot Noir wines have been in the \$10-\$15 per gallon range, Central Coast in the \$10-\$13 range and California appellation in the \$6-\$7.75 range.

Cabernet Sauvignon

Cabernet Sauvignon is more in demand than any other varietal. The aging requirements of Cabernet Sauvignon forces wineries to carry more inventory, which is tough in these times of tight credit. Buyers would like to purchase 2008 vintage wines that can be bottled and marketed soon. But 2008 was a light crop and little volume is left in bulk. Buyers are reluctantly looking at the ample supply of 2009 Cabernet Sauvignon, but are slow to close deals. Recent sales of 2008 Napa Valley Cabernet Sauvignon have been in the range of \$16-\$27 per gallon and Sonoma County 2008 and 2009 in the range of \$10-\$15 per gallon. Sales of 2009 Central Coast Cabernet Sauvignon have been in the range of \$6.25-\$7. Supply of 2009 California Cabernet Sauvignon is more limited and sales have been in the range of \$5.75-\$6.25 per gallon.

Grapes 2010

Audra Cooper, our newest North Coast grape broker, reports that early season winery expectations were for yields ranging from average to slightly above average. Expectations, however, could be lowered with the cool weather, wind, and rain that took place during May and happened during some Chardonnay and Pinot Noir bloom. Most white varieties are in bloom and many red varieties are just starting. Growers are reporting that we are anywhere from ten days to two weeks behind an average growing season. Demand for grapes in the North Coast remains soft at best for Chardonnay, Pinot Noir, and Cabernet Sauvignon. For other North Coast varieties the market is very quiet with minimal to no interest, especially at the high end. There are plenty of grape purchase opportunities currently available; supply exceeds demand for all major varieties throughout the North Coast. Prices so far have been similar to the depressed market of 2009.

Matt Turrentine, our southern Central Coast grape broker, reports there is a copious supply of all major varieties in San Luis Obispo and Santa Barbara Counties. Demand has been soft, with some interest in Paso Cabernet Sauvignon and Santa Barbara Pinot Noir and Chardonnay. The crop appears to be at least average for all major varieties. Erica Moyer, grape broker for Monterey County, reports good growing conditions and tough market conditions. Although a cool May has the crop about ten days behind normal and the continued rain has increased disease pressure, above average rainfall and little frost concern is expected to result in an average to above average crop. We have been selling Pinot Noir and have a little interest in Cabernet Sauvignon and Merlot. Chardonnay has been very slow.

In the Interior, Erica Moyer reports that the market has been following a pattern similar to 2009. Southern Interior supply for all varieties tightened up earlier than in the Northern Interior, including more demand for Southern Interior Chardonnay and Zinfandel. Currently there is a very limited amount of supply available with multiple buyers interested. In the Northern Interior, the crop projections – based upon bud counts of mostly two clusters per shoot – project an average harvest. The vineyards seem to be about ten days behind normal due to the cool April and May. Adverse weather during bloom for early varieties may have an impact on set and bud differentiation for 2011. Supply is tight for Cabernet Sauvignon and Merlot. There are multiple buyers active in the market with reasonable offering prices and multi-year contracts. For Chardonnay and Zinfandel (for red or white Zinfandel) there is limited demand and plentiful supply.

Please make sure your grape and/or bulk wine broker at Turrentine Brokerage has the latest information on your situation in this constantly changing market.

Napa Valley Vineyard Owners Seminar

Bill Turrentine will be on a panel speaking at the 2010 Napa Valley Vineyard Owners' Seminar June 15th. The panel will address *The Decision to Replant - Ideas and Questions to Consider*. More information is available at www.napagrowers.org.

Market Opportunities

Grapes :

- Available: Cabernet Sauvignon Alexander Valley, hillside 80 tons
- Available: Cabernet Sauvignon Dry Creek Valley (Double Gold 2010 Sonoma Harvest Fair)
- Available: Malbec from Napa Valley and Lake County in small lots or truckload quantities
- Available: Zinfandel Russian River Valley, 125 year old vines
- Available: Alicante Bouschet and Zinfandel, Sonoma County, 100 year old vines
- Available: Mourvedre, old vine, Sonoma County
- Available: Oakdale, CA (District 12) CS, MER, PV 2010 Planting
- Available: Cabernet Sauvignon Atlas Peak
- Available: Merlot Oak Knoll, clone 181
- Available: Petit Verdot Rutherford
- Available: Pinot Noir Monterey County, various lot sizes available

Bulk Wine:

- Available: Cabernet Sauvignon 2009 wine in bulk, 18 Alexander Valley lots, 8 Lodi lots, 19 Mendocino lots, 50+ various Napa Valley appellation lots and 40 various Paso Robles lots
- Available: Pinot Noir 2009 wine in bulk, 10 Mendocino lots, 9 Santa Maria Valley lots, Sonoma County lots, Napa Valley lots
- Available: Various Rhone varieties, 3 Marsanne lots, 6 Roussanne lots, and 28 Viognier lots
- Available: Riesling 2009 vintage, 23 various lots from the Central Coast and North Coast appellations, and 5 lots from Washington
- Available: Albarino 2009 wine in bulk, 5 different lots