February 2019: M&A in a Changing Wine Market

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US Wine Sales +3%	Off-Premise +2%	DTC Shipments +11%	Winery Jobs +5%

[12 month change]
The past year witnessed multiple deals at all levels of the U.S. wine industry. Premium wine brands and wineries, national wholesale brands and boutique producers received interest from buyers. Mergers and acquisitions are expected to stay strong in 2019 despite wider, potentially troublesome changes in the overall U.S. wine market.

Winery, Vineyard Deals Brisk at all Levels

The advisory firm Zepponi & Co. had a hand in some of the biggest winery transactions of 2018, such as AXA Millésimes' purchase of Outpost Wines in Napa Valley and Foley Family Wines' acquisition of the Acrobat brand from Oregon's King Estate.

The deals were among the dozen worth more than $10 million last year that Santa Rosa, Calif.-based Zepponi tracked, and firm principal Matt Franklin expects activity to remain robust in 2019.

> Mergers and acquisitions are expected to continue at a brisk pace through at least the first half of 2019.
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> Vineyard demand, especially outside of the best-known regions, is likely to decrease but could pick up if land prices start to fall later this year.
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> Large-production, large-volume brands may stay in demand, especially for foreign buyers looking for an entry into the wholesale market.

“We have a pretty full pipeline of opportunities in Napa, Sonoma, Oregon, Washington and Central Coast, and there seems to be buyer interest still,” he said. “We’re expecting that 2019 should be as good as 2018.”

Napa and the Pacific Northwest are both areas of prime interest, thanks to the potential to acquire top-tier wineries producing wines that retail for more than $20 a bottle. Europeans, especially buyers from France, are looking for opportunities in the U.S. Franklin said many see acquisitions as avenues to access the U.S. market as consumer demand for French wines remains strong.

Foreign buyers keen on U.S. wineries

While large companies such as Constellation Brands continue to seek buyers for lower-priced brands, Franklin said they’re a tough sell. Again, the most likely buyers are going to be foreign entities that see them as opportunities to gain a toehold in the U.S. market. “Who is going to buy those?” he asked. “Somebody that needs access to the U.S. wine market and needs volume to have some sort of clout with distributors and is able to acquire those to go ahead and get that clout — but they’re international.”

A good example might be a company like the Carlyle Group, which acquired Accolade Wines last year, a $772 million deal for a host of brands that Constellation spun off to Champ Private Equity in 2011.

Brands that rode the direct-to-consumer (DtC) wave to success and whose owners are now seeking an exit are an emerging area of opportunity, Franklin said. With few hard assets but strong per-bottle pricing, they offer good cash flow to buyers. The challenge is that rapid growth is tough for the brands, which usually produce just 5,000 to 10,000 cases, and a lack of integration makes them a tough sell to foreign buyers looking to enter the U.S. market.

“These things are throwing off nice cash flow, and you could just keep them as a cash-flow investment,” he said. “So that’s an opportunity that’s still out there that no one’s really taken advantage of. And these owners are looking for a pathway to liquidity.”

One U.S. wine company that has been quite active in the mergers and acquisitions market made a significant move abroad.

Bill Foley further expanded his company Foley Family Wines, which is based in Santa Rosa, Calif., with the recently approved purchase of Mt. Difficulty winery in the Central Otago region of New Zealand. The $35 million deal includes more than 170 acres of vineyards, the winery and a second brand Roaring Meg. Because the buyer was a foreign firm, the deal required the approval of New Zealand’s Overseas Investment Office that reviewed the purchase agreement submitted in 2017.

Brand, not land, can attract buyers in 2019

Given the abundance of wine and grapes in the bulk market at the moment, Erik McLaughlin, CEO of Seattle-based advisory firm Metis, feels brands are in a strong position in the current market. “The power of brand is more important than ever, as buyers become pickier about their investment opportunities,” he said. “I think we’ll continue to see strong activity on brand-oriented deals, but land-oriented deals will slow down.”

The comments underscore the direction heralded by 2018 purchases such as the Wine Group’s acquisition of the 7 Deadly Zins as well as the Acrobat transaction, but also point to a deeper issue in the market: the decrease in vineyard prices as the abundance of production dampens buyer interest in securing land.

“Folks who a couple of years ago were concerned about where their grapes were going to come from are now taking a little more of an attitude, ‘Why would I buy a vineyard when I can buy grapes so cheap for now?’” McLaughlin said. “Buyers want a bargain right now, and there’s enough distress situations that, outside of the primo, primo areas that are still garnering a premium, the buyers can be really picky, and they can afford to wait to get the right deal.”

Outlook for future winery, vineyard deals

McLaughlin expects vineyard prices in less-favored areas to decline 10% to 15% from where they were two years ago, but this shouldn’t hurt long-term owners. “They’ll still get more than what they bought the land for 10, 15, 20 years ago, or what they’ve invested in terms of the land and development cost,” he said.

Similarly, buyers with the long-term in mind have opportunities to acquire solid properties, with those in second-tier locations available for less than the cost of developing a new vineyard from scratch.

“If you’re looking for a B-plus site, you can probably buy the existing vineyard for cheaper than you can buy the underlying land and the development cost to create a vineyard on it,” McLaughlin said. “Savvy operators will come in and be able to scoop a vineyard that may have depressed revenues over the next couple of years, but they can get a deal on a vineyard now that they’ll be very, very happy to have a couple of years from now.”

Vineyard and agricultural property appraiser Tony Correia said the industry saw a surge in buying activity from 2012 to about 2017, when some of the major players such as Jackson Family Wines and E. & J. Gallo Winery invested in integrating premium supply. “In those five years, those folks gobbled up a lot of vineyards,” he said.

One of the most impactful was Gallo’s purchase of the 600-acre Stagecoach Vineyard in Napa Valley, announced in 2017. Prior to Gallo’s purchase, the vineyard was supplying 90 wineries of which 30 made a Stagecoach vineyard-designate.

That, in turn, led to smaller, quieter vineyard deals as a major source of premium fruit was now controlled by Gallo, which made other moves, such as buying The Ranch winery in Napa Valley to increase premium and ultrapremium production.

Such buying and selling activity is coming to an end, as Correia suspects the industry is pausing to see how it can process the large 2018 crop and figure out how to increase consumer demand. Correia, however, does not expect to see declines in prices for wineries and vineyards, as he believes there will not be many distress sales in 2019. “We’re just going to see a flattening in the level of activity,” he said. “I don’t see the factors that would push prices down.”

It had seemed in recent years as if one could put Cabernet vines in the ground and expect steady, profitable returns. That is no longer the case, as Correia said the industry appears to have planted more than enough Cabernet and Pinot. “We have a tendency to overplant anything that is profitable,” he said.

He said Paso Robles may already have been overplanted, because many tons of 2018 grapes went unsold or sold at deeply discounted prices. He said that in the Central Coast, where large tracts of land are still available for development, it’s easy to “create a lot of production” quickly and inexpensively. Part of the issue in the Central Coast could be a capacity problem.

Correia said he thinks the U.S. could be heading for a recession, and the industry will see the slowdown first in diminished wine sales followed by a flattening in the demand for wineries and vineyards. “I suspect there’s some deals that will happen in the next six months, but I think you’ll see a definite slowdown.”

An established winery, buying to expand

Securing extra production capacity close to vineyards and a tasting room is what kept Rombauer Vineyards interested in Renwood Winery in the Sierra Nevada foothills town of Plymouth, Calif.

The 60,000-case-per-year winery had been owned by an Argentine investment group that included Alejandro Pedro Bulgheroni, who also owns a Napa Valley estate. The group reportedly paid nearly $7 million for the winery in 2011 in a bankruptcy sale.

Rombauer CEO Bob Knebel said the family-owned winery tried to purchase Renwood then, but the deal just didn't come together. But Rombauer did purchase a 148-acre vineyard nearby to support the winery's fast-growing red wine program. In addition to the powerhouse Chardonnay, Rombauer produces estate Cabernet Sauvignon and Zinfandel that have enjoyed strong sales growth primarily through tasting room sales. "Demand had grown, and our Napa production space couldn't grow any further," Knebel said. "We needed to liberate some capacity."

Because Renwood was near the company's estate vineyard in the foothills, Knebel said, Rombauer reached out to the current owners with a general inquiry, and they serendipitously were open to a sale. Knebel declined to disclose the purchase price, but the sale, expected to close in mid March, also included a 20-acre vineyard and tasting room, which after a light refurbishing should be open this spring selling Rombauer's full portfolio. The purchase did not include the Renwood brand.

At a time when the industry is greatly concerned with finding new consumers as traditional ones grow older, Knebel said, Rombauer is enjoying sales growth driven by consumers of all ages. "We are in a category of luxury wine that is still at affordable price points," he said. "We appeal to a broad cross section of new and experienced enthusiasts looking for quality wines that reflect the beauty and character of the sites the fruit comes from."

Quality is paramount, and it needs to reflect a brand's story and experience. The best way to make that kind of sale is in a tasting room. "This isn't just a marketing exercise," Knebel said. "Our obsession over quality and customer hospitality over the generations has been a pillar of our very careful growth. We see a very broad section of customers with an equally large following in the 21 to 35 (age group) as with aging baby boomers." he said. "There's an entire generation of younger people who have grown up understanding what really good looks like in any category."

High value estates still garner interest

In the Napa Valley and some of the other top wine regions of the U.S., deals are expected to continue among individuals with the means to either enter the industry at the top level or move on to something else after developing a successful estate. One of those recent deals was the sale of Brand Napa Valley.

Ed and Deb Fitts purchased their Pritchard Hill estate in 2005, founding the Brand Napa Valley label four years later, in 2009. According to Ed Fitts, he and his wife had no previous vineyard-management or winemaking experience.

Fitts is the former president and CEO of Dopaco Inc., a company he founded in 1979 that supplies packaging materials to national chains such as McDonald's, Burger King and Wendy's. During this 27-year career, Fitts grew the company from 125 employees with annual sales of $10 million to 1,500 employees working in seven facilities with annual sales of more than $400 million. In 2004, Fitts sold the company with plans for "retiring" to his new role as vineyard manager and winery owner.

Fitts said his original intent was to grow grapes and create a "small-scale" wine label. But when he and his wife realized the potential of the *terroir* at their location on Pritchard Hill, he said, it seemed "only natural" to develop that potential. The Fitts increased production from 200 cases when they launched the brand in 2009 to more than 1,000 cases in 2018. "The vineyards are now producing at their full potential, and it clearly shows in the bottle," Fitts said.

In January, the couple announced they had sold Brand to Jim Bean and Christine O'Sullivan, former Apple executives. "There was nothing more exciting than the natural progression of planting a perfect vineyard, making world-class wine, developing a state-of-the-art cave, winery and tasting room," Fitts said. "The transition to Jim and Christine was also a natural progression, not a sales decision."

According to Fitts, the winery and estate were never officially for sale, so he and his wife never solicited offers from any other potential buyers. He and his wife met Bean and O'Sullivan while hosting them on a tour and tasting at Brand. "We hit it off and learned that they were looking to acquire a small winery," he said. "The rest is history."

Fitts said he's accomplished what he set out to do with the business: "Create a world-class, enduring wine estate." He and his wife have no intention of keeping their hands in the new Brand business. Fitts said he believes that passing the reins to Bean and O'Sullivan, who he describes as "extremely qualified," will take the winery to the next level. He looks forward to focusing on philanthropic projects.

Christine O'Sullivan and Jim Bean have been wine-grape growers in Napa since 2003, owning a total of 65 vineyard acres. They grew interested in the property for its winemaking potential and because of the winery the Fittses had built. That being said, O'Sullivan said she did work with local experts leading up to the purchase, including Reidy Law Group and CMPR, who served as legal counsel and advisors.

O'Sullivan and Bean had been looking at other properties for purchase over the past few years, but would not disclose what those properties were. "When we found Brand, we immediately recognized that this was the rare gem we were looking for," O'Sullivan said.

Moving forward, the new owners said, their goal is to continue the success of their predecessors, continuing to make wines that improve with each successive vintage. As part of that continuity, Brand's winemaker, Philippe Melka, will be staying on board at the winery — a relationship that O'Sullivan said she and Bean have solidified during the amicable acquisition process.

When asked if she had any advice for others looking to invest in or purchase an existing wine label, O'Sullivan said, "As growers, owning a winery is a very natural next step. … It may not be for everyone. This is a very serious business endeavor."

— Andrew Adams, Stacy Briscoe, Peter Mitham

Changes and Disruptions in the U.S. Wine Market

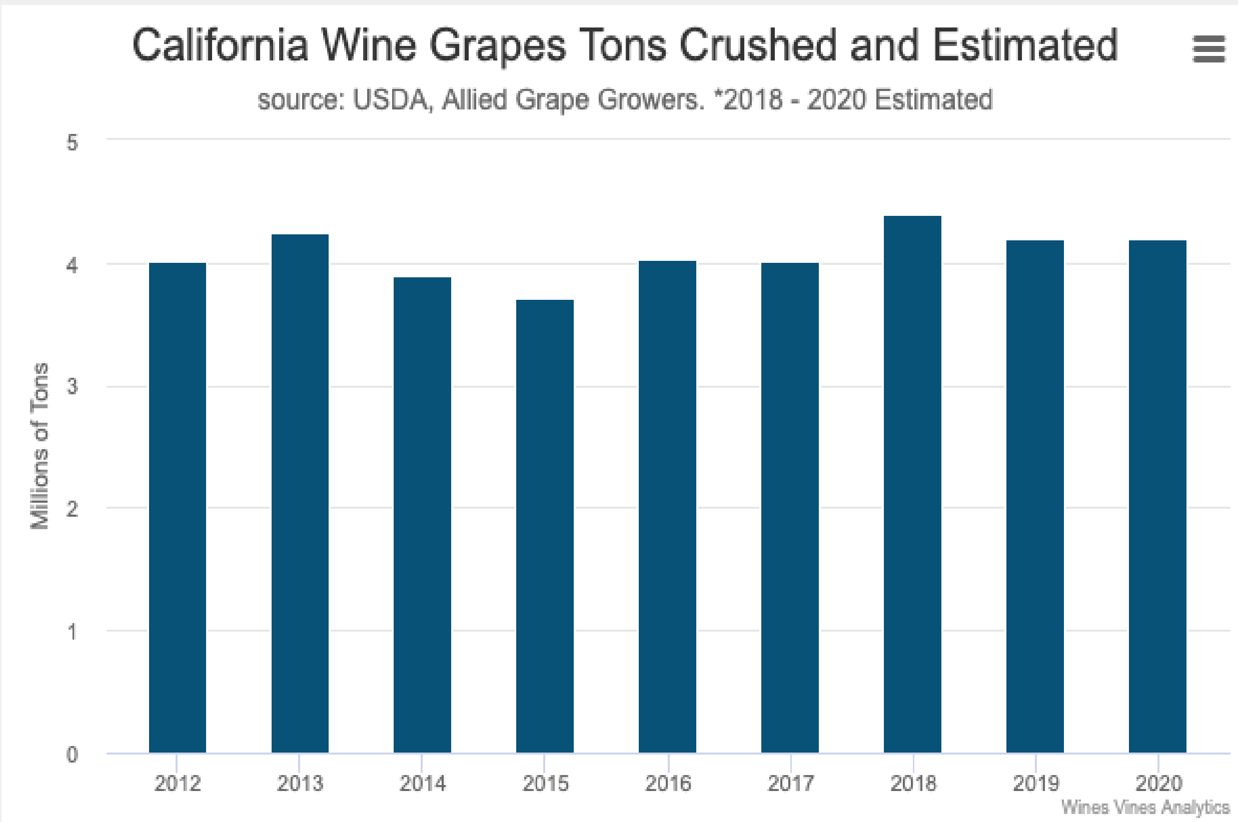
Sacramento, Calif.—The U.S. wine industry came together recently in California's capital city, just as it has for the past 25 years. But by the same time next year, the convention center that housed the 25th annual Unified Wine & Grape Symposium will have been demolished to pave the way for a new one, and the event will be taking place at an interim location.

It's a major disruption to the industry's largest conference, and several speakers at this year's Unified used that change as an analogy to describe what the entire U.S. market is facing.

> California appears to have produced a record crop of 4.4 million tons in 2018.
>
> Many of the industry's top experts point to a "demand problem."
>
> New products in the beverage alcohol sector as well as cannabis infused drinks and alcohol-free beverages are growing more competitive with wine.

After years of steady growth, the market is — depending on whom you ask — either entering a period of oversupply versus diminished demand as part of a regular cycle or poised to face significant challenges as younger consumers fail to embrace wine drinking as their parents and grandparents did and instead opt for craft beer and cocktails, cannabis-infused drinks or alcohol-free beverages.

Following the smoke and fire of 2017 California appears to have enjoyed a record harvest in 2018, estimated by the Allied Grape Growers at possibly 4.4 million tons.



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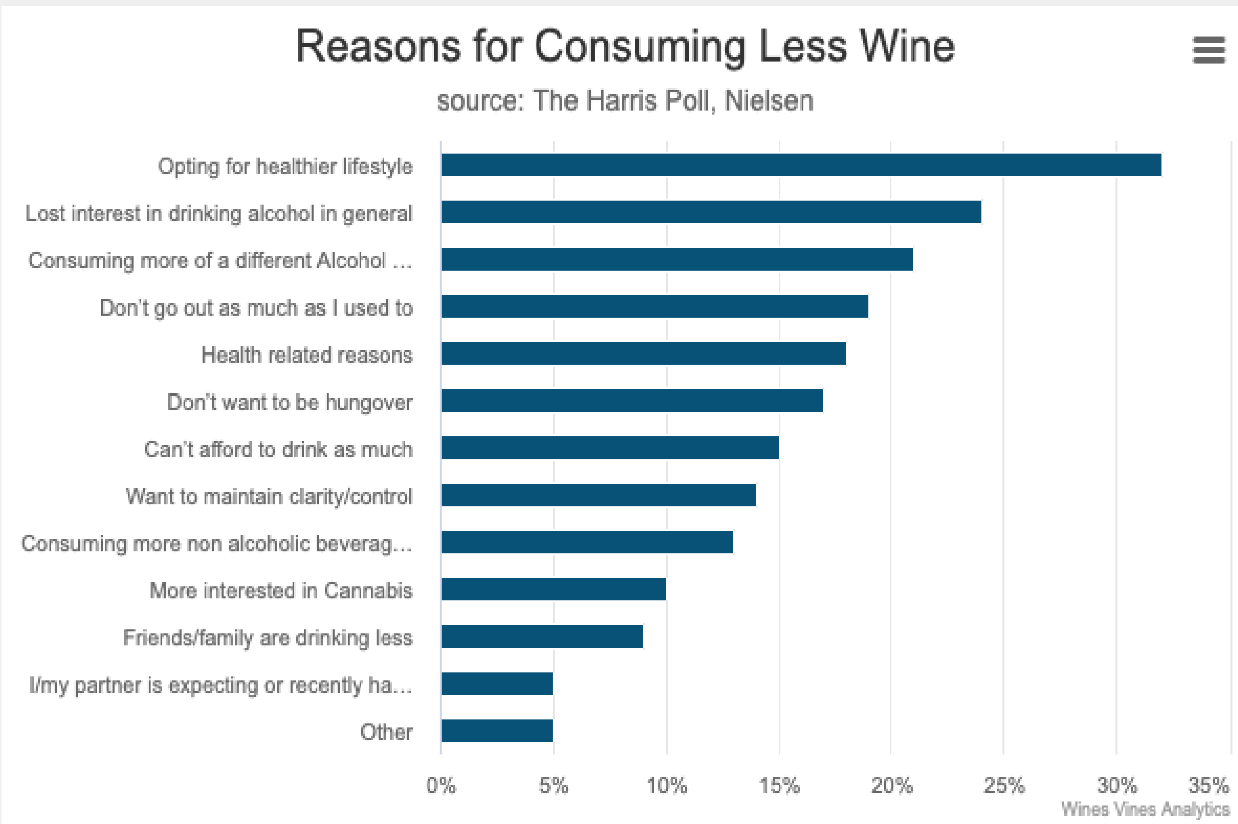
All those grapes come at a time when the industry is facing flat and declining consumption numbers. Danny Brager, senior vice president of Nielsen Beverage Alcohol Practice, spent a surprising amount of time discussing beverages without alcohol during his remarks at the State of the Industry session at Unified.

Growing interest, sales in alcohol-free

Brager said alcohol-free beverage sales increased by $7 billion versus four years ago, and the diversity of such beverages has also greatly increased. Some major companies, such as Coca-Cola, have launched mock beers and cocktails to provide drinkers an option when either they can't drink or choose not to. The fast-growing cannabis industry has also developed a variety of low-calorie, low-dose infused beverages that are being marketed as alternatives to beer or wine.

Facing more competition and not as much consumer enthusiasm, Brager said, the wine industry needs to focus on maintaining its share of consumers' minds, hearts and pocketbooks. "We're in a battle for share, maybe battle is too mild a term, we're in a war for share," he said.



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Alternative packaging has helped wine stay competitive and expanded the consumption of wine to non-traditional "wine" activities and events such as an outdoor music concert or round of golf. Brager said wine-in-a-can sales grew to more than $70 million in 2018, and the package type is clearly not a fad. "Wine has done a really nice job of figuring out how to deliver its product to the mouths of consumers," he said.

DtC shipments remain a bright light, having doubled in the past decade to more than $3 billion in value. Brager said nearly 80% of all beverage alcohol sales online are for wine, but the category as a whole lags far behind other consumer packaged goods.

To succeed in such a diversified market, wine producers will need to "focus intensely" on growth pockets and segments where their wines resonate with consumers. These innovations need to work in tandem with retaining boomer consumers. "Give consumers what they want, where they want it, and innovate," he said.

Take advantage of the changes

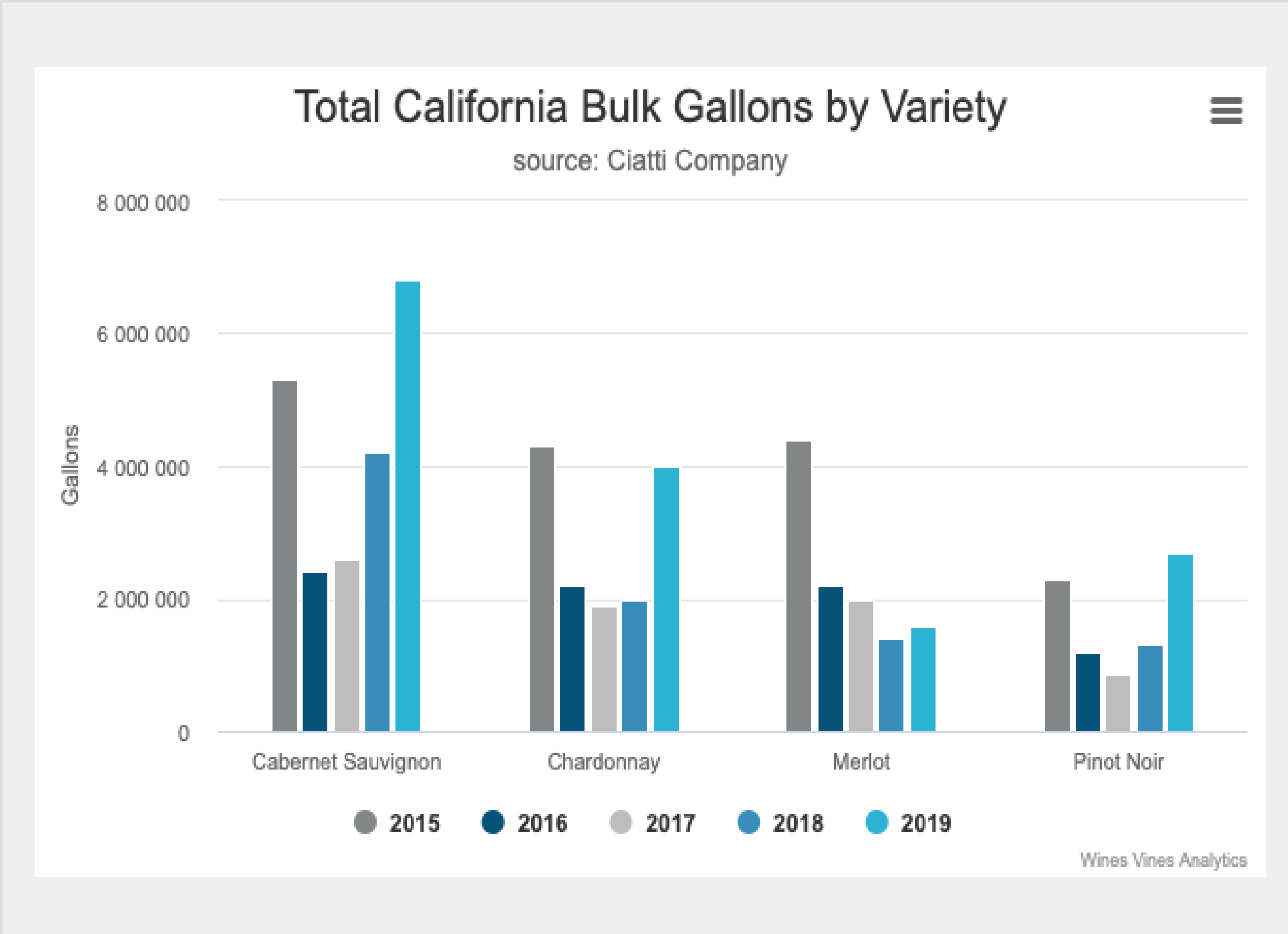
Glenn Proctor, partner and global wine and grape broker for Ciatti Company in Novato, Calif., said the industry is facing a new "market paradigm," and the challenge for everyone making and selling wine is to adapt and find the opportunities the changes will bring.

Ciatti just opened a new office in China, and Proctor said global wine production has rebounded after a dismal 2017 vintage in many key areas. But as global production increased 13%, prices and demand have declined in almost all regions.

The same is happening in the U.S. Proctor said rather than a typical oversupply scenario, the industry really has a demand problem. He noted the bulk market is probably at its slowest since 2010.

The current inventory of Napa County bulk Cabernet Sauvignon has risen to more than 600,000 gallons, while the price has dropped to $28 per gallon. Inventories of key varieties in Sonoma, Lake and Mendocino counties have also increased. Proctor said deals are done now mainly by buyers floating a price and sellers matching it primarily to clear inventory.

Large wine companies that used to move the bulk grape and wine markets are more likely to be sellers these days as they look to offload excess supply. "There are some opportunities for creativity and innovation," Proctor said. "Buyers are looking for deals, and sellers are realizing the new market paradigm."



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A few weeks before Unified, Proctor delivered a similar presentation at a conference hosted by the Sonoma County Winegrowers, where he also discussed grape pricing.

At the group's annual Dollars & Sense forum in Santa Rosa, Calif., Proctor said the power has shifted from the seller to the buyer. "Supply has become a bad word," he said. "With an oversupply grape market, buyers have an expanding list of grape growers to choose from. And with the increase in grape prices, buyers are not necessarily maintaining regional loyalty, looking for more economic grape sources."

Proctor also conducted a survey of Sonoma vintners regarding the current market demand. According to the results, most winemakers are going to buy less of the region's most popular varieties (Chardonnay, Sauvignon Blanc, Zinfandel, Merlot and Pinot Noir). When asked what they expected regarding prices, Chardonnay, Sauvignon Blanc and Merlot are all expected to stay around the same price point, but Cabernet Sauvignon, Pinot Noir and Zinfandel are expected to decrease in price. Perhaps to take advantage of the changing market, the wineries reported they do expect to buy more Cabernet Sauvignon. "Interestingly, vintners plan to buy more Cabernet, but expect to pay less for it."

At the Unified symposium, Allied Grape Growers president Jeff Bitter characterized the coming year as one of adjustment, but on the whole the U.S. and California wine industry remains very stable.

Bitter said California's total acreage is likely to grow by 0.5% to 594,000 acres. Total harvests are projected to stabilize at around 4 million tons through 2021.

Allied Grape Growers works with the state's nurseries on planting material purchases to analyze what coming vintages will bring. The industry continues to lean red: Of the 22 million vines sold in 2018, about seven out of every 10 were red varieties. Cabernet Sauvignon, Pinot Noir and Chardonnay dominate, in that order, and will account for two-thirds of California's new vineyard production. "The reality is there's a lot of vines that went in the ground last year and a lot of those are coastal vines."

Much of the state's vineyard development continues to occur in coastal areas, and any imbalance in the market won't be cured by culling Central Valley vineyards. Bitter said the Central Valley's bearing acreage is going to shrink by 6% to 190,000, after several consecutive years of growers pulling wine-grape vineyards.

Bitter concluded the industry really has more of a demand issue, and it's something that growers can proactively handle. This year may be the right one to pull out an older or virus-compromised vineyard. "It's really time to dig up non-performing vineyards," he said. "Take my advice and dig it up now. Don't prune it."

—*Andrew Adams*, *Stacy Briscoe*

Finding Profits In Excess Supply

Sacramento, Calif. —"Supply is not the problem." Those five words from Glenn Proctor, global wine and grape broker with Ciatti Company, during the State of the Industry session at the Unified Wine & Grape Symposium at the end of January summarized the challenges facing wineries in 2019.

The situation made for strong attendance at Unified sessions examining alternative routes to retail for wineries. On the one hand, private labels, or "strategic brands," offer wineries opportunities to move inventories. On the other, custom-crush facilities allow brands to scale up production without necessarily investing in the brick-and-mortar infrastructure.

Brand innovation

Lisa Ehrlich of Lisa Ehrlich Consulting, who has developed dozens of brands for her clients, picked up on Proctor's comment that the surplus creates "opportunities for creativity and innovation." The development of strategic brands can allow wineries to engage directly with consumers, building connections in a market where consumers are less brand-loyal and more experiential. "They can be a source of marketing, creativity and innovation," she said during the afternoon session on alternative routes to retail.

While she wouldn't recommend it, she has developed brands in as little as six weeks. The short timelines underscore just how responsive labels can be to industry circumstances as well as consumer sentiment.

The consensus among speakers at Unified was that consumers have firmly set their sights on wines above $15 a bottle, while wineries are targeting the $20-$25 range.

Robert Trone, co-owner of Total Wine & More, said bottles retailing for $15-plus are where his company's outlets excel. Total partners with wineries, Trone explained, allowing producers to own the brand while Total provides the distribution platform that helps them move product. "What works for us is providing a wine that has great value and great taste," he said.

Custom winemaking options

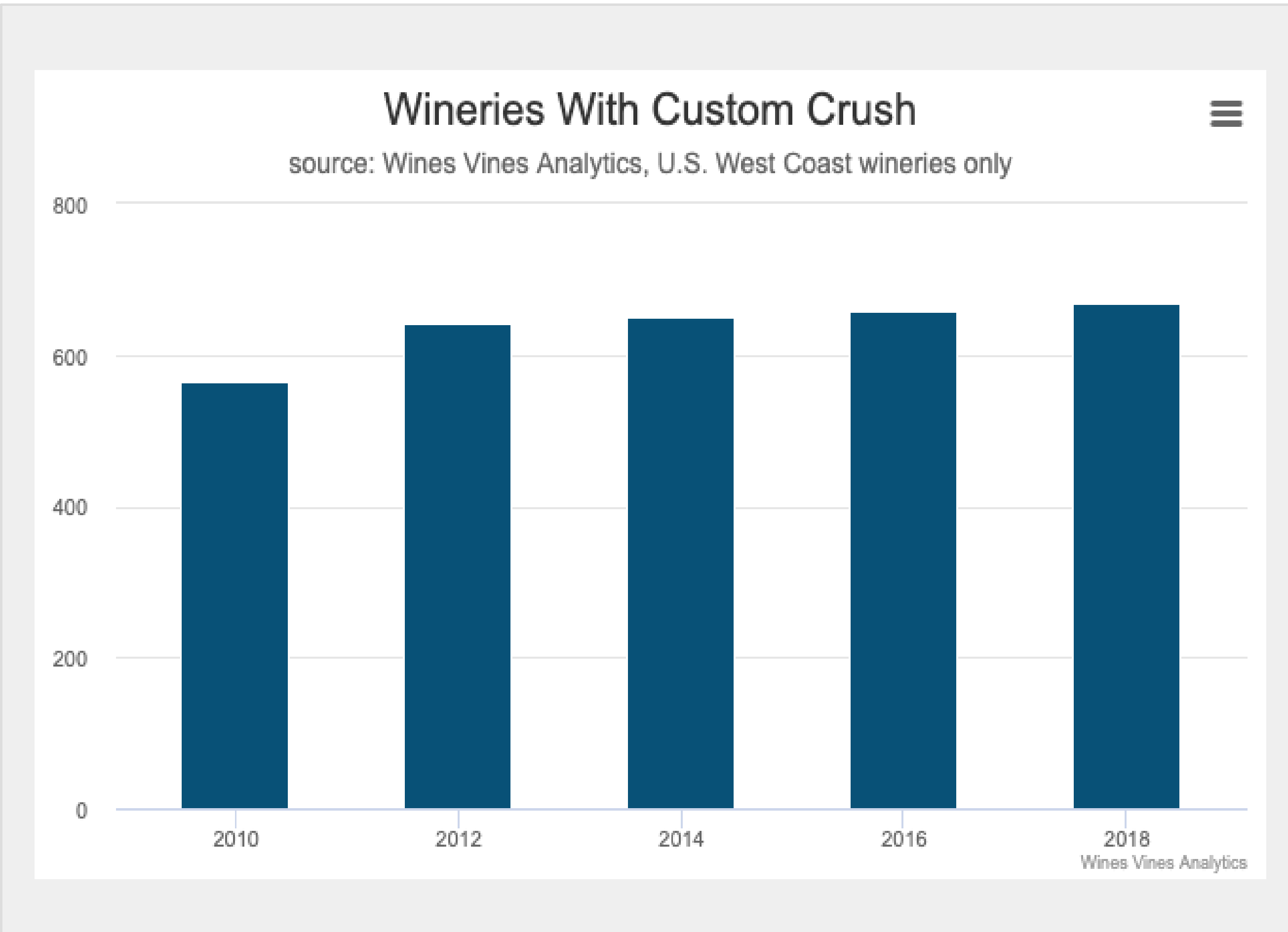
Plata Wine Partners LLC is one of the vintners with which Total works. Plata owns 20,000 acres of California vineyards, from which it has produced a variety of bulk and bottled wines since 2006. Plata CEO Doug Walker told a Unified audience that annual production is in the range of 6.5 million cases. Ownership of its vineyards gives it control over production practices, right down to managing vineyards for the resonance it wants brands to have with buyers. "We allocate these vineyards to the brand," he said.

Plata's growth was entirely through the use of custom-crush facilities, said head winemaker Alison Crowe, who moderated a panel discussion at Unified that explored the opportunities custom-crush facilities offer.

Francis Ford Coppola winemaker Tondi Bolkan explained during the session how the winery's Black Diamond and Sofia labels began life in custom-crush facilities. Outsourcing production of its wines was common at Coppola until 2005, when – with eight facilities in play – it bought Chateau Souverain and was able to consolidate production at the Geyserville, Calif., facility. The purchase also gave it enough capacity to begin offering custom-crush services to others.

Custom-crush facilities and bulk-wine suppliers can often work in tandem to manage inventories and feed brands, Bolkan noted. Companies like Turrentine Brokerage and Ciatti can help connect buyers of bulk grapes and wine with facilities that can process it as well as provide the legal advice that keeps their ventures on track. Coppola itself works with Delicato Family Vineyards to source bulk wine, helping, in turn, to manage Delicato's inventories.

Yet the number of such wineries has not grown at the same pace of as that of wineries in general. According to the Wines Vines Analytics winery database, there were 4,483 wineries in California, Washington and Oregon in 2010. Of those wineries, 13%, or 565, offered custom crush. The number of wineries offering custom crush increased 14% to 642 from 2010 to 2012 but growth slowed to just 1% to 2% in the following years while the total number of wineries grew at a much higher rate. By 2018, wineries offering custom crush accounted for just 11% of the total number of wineries in the western U.S.



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Regardless of which side of the equation parties are on, communication and responsiveness are key.

Winemakers using custom-crush facilities need to be engaged – "Don't ever expect your custom crush to make your wine," warned Alison Smith of Smith Story Wine Cellars – and those supplying brands into the market need to pay attention to what's moving and what's not. Most wines are consumed within 48 hours of purchase. Consumers are going to be looking for the next bottle in tomorrow's market, not yesterday's.

Ehrlich underscored this in blunt advice on the limits of strategic brands among consumers.

Some flourish for an instant, and it's not necessarily a failure when they disappear. She encouraged wineries to be ruthless, knowing when a brand is done and it's time to exit the market.

—Peter Mitham

The Younger Wine Consumer

Much of the apprehension regarding the future of the U.S. wine market is based on younger consumers not following the same consumption patterns as their parents or even their older Generation X siblings.

However, there are young wine consumers, and the Wine Market Council (WMC) has done some research into their drinking and buying habits. The council surveyed more than 2,000 wine drinkers (consuming wine at least every two to three months) and segmented the results by age and gender. Of wine drinkers in their 20s, 61% are female and 39% are male. The gender split among wine consumers in their 30s is 54% female and 46% male, and among all drinkers it's 56% female and 44% male.

WINE CONSUMERS BY AGE AND GENDER

Age=>	20s	30s	40s
Female	61%	54%	53%
Male	39%	46%	47%

Source: Wine Market Council

Based on WMC's survey, younger wine drinkers are also buying at a rate similar to older people and in some instances are willing to spend more. All consumers in their 20s, 30s and 40s reported buying wines priced at less than $10 at the same rate of "at least several times a year."

At price points higher than $15, however, consumers in their 20s and 30s are more likely to buy than those in their 40s. The biggest difference came for wines priced at more than $25, where half of all those surveyed in their 20s had made a purchase but only 35% of consumers in their 40s had.

By variety, younger male drinkers lean toward most reds except blends and Zinfandel, while Moscato and Pinot Grigio skew female.

When asked which varietals or wine types they regularly consume during the year, wine drinkers in their 20s were less likely to pick Cabernet Sauvignon than consumers in their 30s or 40s. Only 32% of those in their 20s said they had purchased Cab regularly versus 42% of consumers in their 40s.

Younger wine drinkers had a slightly greater propensity to buy white wines, and 48% also reported regular Chardonnay purchases, which is more than for people in their 30s and 40s. Wine consumers in their 20s also purchase sparkling wine more often, and that extends to sparkling Moscato and rosé. Nearly half of younger consumers reported buying a slightly sweet rosé or white Zinfandel, which is much higher than the 30% of consumers in their 30s and 40s.

VARIETALS CONSUMED REGULARLY

	20s	30s	40s
Red (net)	**87%**	**88%**	**84%**
Merlot	49%	44%	44%
Cabernet Sauvignon	32%	42%	38%
Pinot Noir	43%	46%	32%
Red Blends	37%	37%	27%
Zinfandel	32%	30%	30%
White (net)	**91%**	**88%**	**86%**
Chardonnay	48%	37%	38%
Moscato	57%	39%	37%
Pinot Grigio/Gris	38%	37%	29%
Sauvignon Blanc	20%	25%	19%
White blends	24%	26%	12%
Sparkling (net)	**73%**	**63%**	**54%**
Sparkling Moscato	37%	27%	23%
Prosecco	26%	28%	18%
French Champagne	27%	26%	17%
Sparkling Rose	34%	23%	17%
Domestic sparkling wine	17%	20%	17%
Cava	4%	8%	3%
Somewhat sweet rose/ blush/white zin	**46%**	**30%**	**30%**
Dry rose	**26%**	**26%**	**12%**

Source: Wine Market Council

But the WMC research also found openness to other alcoholic beverages in young consumers. More than half (52%) said they were open to “other” alcoholic beverages than beer and spirits when not drinking wine. Such products include cider or even new “hard” seltzers or sparkling waters.

This indicates an interest in new experiences and perhaps that they view the entire segment as more than just wine, beer or spirits. These younger consumers, however, do not opt to replace wine with beer as readily as people in their 30s and 40s do.

In early January, Lulie Halstead, chief executive of Wine Intelligence, presented some of her group’s research on millennials at the Dollars & Sense seminar organized by the Sonoma County Winegrowers. Halstead outlined some factors, based on Wine Intelligence research, that could explain the lackluster wine consumption habits of younger people.

Wine knowledge: General wine knowledge is on the decline. The group conducts a test on wine knowledge, and the average score of the typical wine drinker was 30 out of 100 in 2018, versus 33 in 2015. This is, in part, due to the technology age we live in, Halstead said. When consumers have the ability to quickly look up information about a wine at the point of sale, they do not feel the need to retain information about what they purchased. The average millennial score has dropped from 29 in 2015 to 23 last year.

Wine confidence: Because consumers, in general, are less knowledgeable about wine, Halstead said, they are less confident in their purchasing decisions.

Choice: Millennials are becoming, as Halstead described, more “promiscuous” in their alcoholic beverage consumption. They’re more likely to include craft beer, craft cocktails and ciders in their imbibing rotation. And in states where it is legal, that also means cannabis.

Expense: According to Wine Intelligence, the number of consumers (in all age demographics) who view wine as an “expensive drink” has increased from 26% in 2009 to 35% in 2018.

Better packaging: Because wine consumers are now learning about wine and wine brands digitally, and because the largest demographic of potential wine drinkers (millennials) is notably more frugal with their wine-spending dollars, Halstead stressed the increasing importance of label and packaging design. “You have to factor in the expensive perception,” she said. “Consumers want what they’re buying to look good. If they’re spending more money on it, it needs to have the perception of being more premium, more luxury.”

Health: The number of regular wine drinkers who consume wine on an at-least-once-a-week-basis has declined from 57% in 2013 to 45% in 2018, according to Wine Intelligence. Halstead said this is in part due to the U.S. population becoming more aware of their total alcohol consumption; consumers are more frequently turning to non-alcoholic beverages (and now cannabis) as alternatives. Millennials also appear to be more receptive to stories in lifestyle media about eschewing alcohol to pursue a healthier lifestyle.

— *Andrew Adams, Stacy Briscoe*

Wine Industry Metrics: Wine Sales Steady, but Growth Minimal

Wine sales and shipments in January remained steady, but growth was muted in the traditionally slower, post-holiday season. U.S. wine sales in January rose 6% to $3.2 billion, reported bw166, with slower growth of 4% in the latest 12 months. Still, the total market was worth nearly $71 billion. Off-premise sales tracked by Nielsen in the four weeks ended Jan. 26 rose 3% versus a year ago to $851 million. Direct-to-consumer (DtC) shipments were flat at $126 million, according to Wines Vines Analytics/ShipCompliant by Sovos, while hiring activity slipped 3% in the month, yet Winejobs.com's Winery Job Index remained relatively strong at 319.

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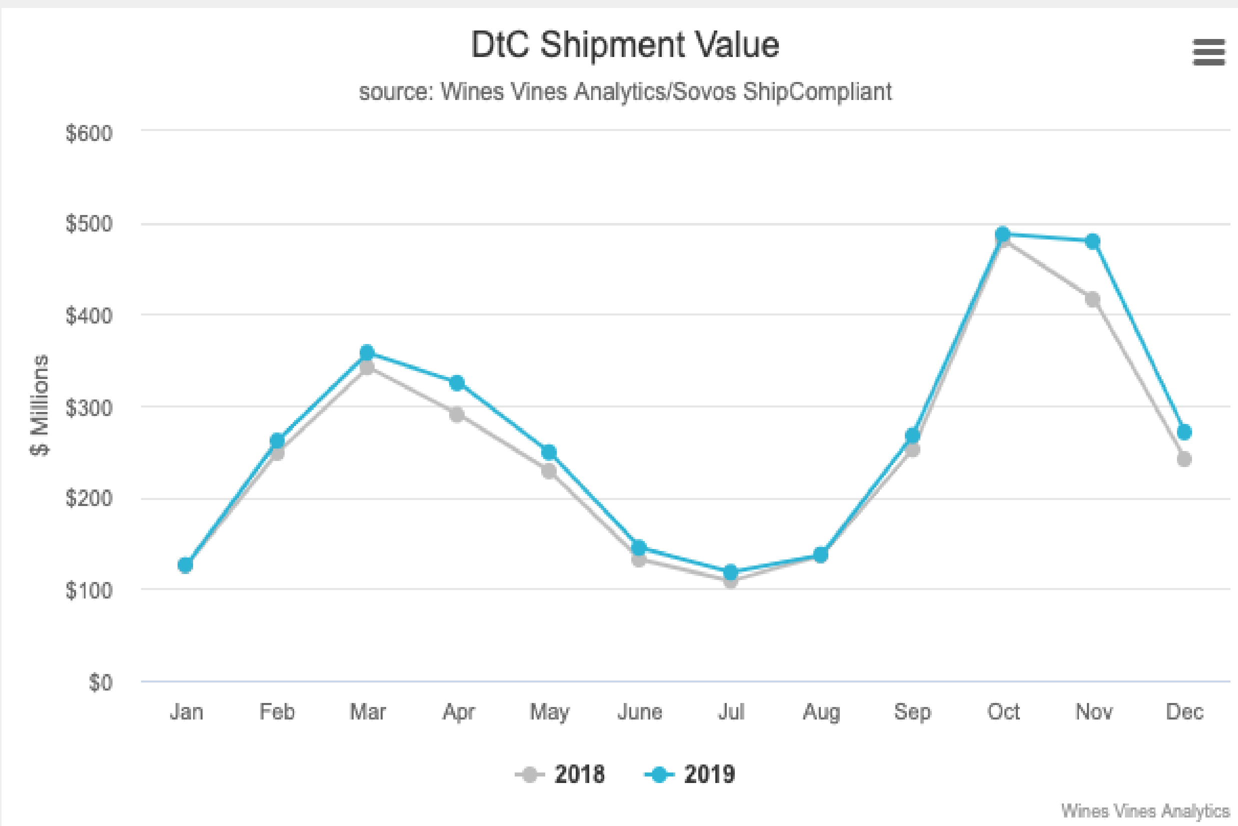
U.S. wine sales rose 6% in January to $3.2 billion, market research firm bw166 reported. Sparkling wine sales were flat at $107 million for the month, giving domestic table wines the lead role with $3 billion in sales. Sales data for the latest 12 months smoothed over seasonal variations, indicating 3% growth in table wine sales and 2% growth in sparkling wine. Together, sales of U.S. wines in the latest 12 months approached $48 billion. Sales of packaged imports increased nearly 8% in the period to almost $23 billion, boosting sales of all wine in the U.S. 4% to nearly $71 billion.

Domestic table and sparkling wine sales at off-premise outlets Nielsen tracks totaled $851 million in the four weeks ended Jan. 26, up 3% from a year earlier. Case sales topped 10 million for the month. Sales in the 52 weeks ended Jan. 26 rose 1% to approach $12 billion, while volumes in the period were flat at 138 million.

Domestic table wine sales in the latest four weeks totaled $772 million, up 3% from a year earlier. This was stronger than the growth posted in the latest 52 weeks, in which sales rose 2% to approach $11 billion. Domestic sparkling wine sales increased 12% in the latest four weeks to $79 million. This was many times stronger than growth in the 52 weeks ended Jan. 26, in which sales rose just 2% to $672 million.



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Direct-to-consumer (DtC) shipments totaled $126 million in January, Wines Vines

Analytics/ShipCompliant by Sovos reported. Volumes rose 3% to 318,455 cases. The greater increase pointed to greater movement of lower-priced bottles. Average bottle price in January fell by less than 3% to $32.97. This contrasted sharply the strong performance seen in December, when average bottle price rose 7% to $36.42. This was the sharpest decline in average bottle price since February 2018, and reflected seasonal softness following the active holiday season.

Overall, figures for the latest 12 months show that average bottle prices continue to rise in most regions. Nationally, average bottle price rose 2% to $39.65. Napa County, which accounts for 28% of all cases shipped, led growth with a 7% increase to $67.27. California beyond Napa, Sonoma and the Central Coast, ranked second in price growth, with the average bottle rising 4% to $28.91. Oregon bottles posted the weakest growth in the period, rising a scant 1% to an average of $39.60.

Sonoma County, where volume growth led the channel in the latest 12 months, saw average bottle price flat versus last year at $29.47. Washington, which ranked third in growth after Oregon, saw its average bottle price drop more than 1% to $32.90.

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Winejobs.com's Winery Job Index slipped 3% in January from a year earlier to 319. The decline mirrored conditions in 2016, but the index remained relatively high versus previous Januaries. DtC positions, including tasting room and retail staff, continued to enjoy strong demand, rising 16% to a subindex reading of 457. Finance and vineyard positions also saw modest increases in activity, while demand for sales and marketing positions fell 20%.

Calera Founder on Selling a Wine Estate Strategically

Josh Jensen, who founded Calera Wine Co. in 1975, sold the San Benito County, Calif., winery, including 83 acres of estate vineyards, inventory and brand, to the Duckhorn Wine Co. (DWC) on Aug. 15, 2017. Jensen, who turns 75 in February, remains as an ambassador for Calera until August 2021 and now has a seat on the DWC board. Jensen has lived for 40 years on the remote, arid vineyard property near Hollister and was packing to move to San Francisco when this interview was conducted in mid-January.

Calera is a singular property and brand, established by Jensen after he worked briefly in Burgundy as a young man, when he picked grapes at Domaine de la Romanée-Conti in 1970. The story of his subsequent search for limestone soil on which to grow Pinot Noir vines in California, the founding of Calera and the establishment of a Mount Harlan AVA in 1990 is well known. Jensen created several single-vineyard Pinot Noirs and Chardonnay, Viognier and a rare Aligoté from his own property, as well as Pinot Noir, Chardonnay and rosé from other Central Coast sources.

Jensen and Duckhorn agreed as part of the deal not to reveal the sale price. San Benito County has assessed for tax purposes the value of six parcels totaling 735 acres now owned by Duckhorn at more than $14 million. The value of the brand, with its international reputation as one of the oldest and highest-quality Pinot Noir specialists in California, plus the inventory, equipment, etc., likely added much more to the price of the acquisition.

Q: When did you first consider selling the winery?

Josh Jensen: Around five years ago, I was ready to think about slowing down, and I talked to my three kids about whether they were interested in running it. I had already begun turning over ownership of the vineyard land to them. They told me essentially, “We don’t want to give up our careers to run the winery. That was your thrill, Dad, and each of us is pursuing our own thrill.” So I thought, yes, I had pursued my dream, the dream of making Pinot Noir here on Mount Harlan, and it would be inconsistent of me to force my dream on them.

Q: How did you start the process that eventually led to the sale?

Jensen: I looked for someone to help me find a buyer. I had met Robert Nicholson of International Wine Associates a couple of decades ago, when I sat next to him on a flight coming back from London. Working with him, we had to prepare the booklet that has all of the information possible about the property and the business. It included everything: wine reviews, financials, the property’s history, acres owned or leased, 10 or more years of our books, and every piece of paper I’ve ever touched regarding the three business entities I had formed to own and operate Calera.

When it comes to real property, we knew that the law firms for the buyers, especially private equity funds like TSG Consumer Partners that owns Duckhorn, would want to see everything. This included my gift tax returns from when I gave ownership of the property to my kids. I was lucky that I had to pay nothing on the gifts, because the valuation of the real estate was so low that when I spread them over three or four years beginning in about 2010, the annual exclusion was enough to exempt me. The issue that came up about the valuation was always Calera’s dry climate. The fight to get water was well known, and appraisers had always thought: “Who wants that headache?” We get 10 inches of rainfall in a good year.

Q: How soon did a buyer turn up?

Jensen: About six months later. I had told IWA, please don’t show this to any of the giants, the biggest wine companies, and Robert said immediately, “You’ll get a lower price if we don’t.” But I’ve put too much of myself into this, and I wanted the name Calera to stay on and the quality to stay at the top. No one knew Calera was for sale unless IWA approached them. It was a secret, and this was imperative psychologically. They took it case by case, and potential buyers had to sign non-disclosure agreements to get the booklet. The first company, when they looked into it, didn’t have the stomach for a vineyard in a drought area. But it was good practice, and it ended after we entered the letter-of-intent phase. They had agreed to a non-refundable deposit, but it was never paid to me and they didn’t lose it.

CALERA WINE CO.

Hollister, Calif.

Founded: 1975

Enterprise: Duckhorn Wine Co.

Annual case production: 45,000 cases

Average bottle price: $35

DtC sales: 18%

Vineyard acreage: 83

Brand: Calera

www.calerawine.com

Q: What happened next?

Jensen: This was in the middle of the drought in 2016. It seemed like a suicidal formula to continue right then. I said to IWA, "I'm going to pull it off the market, and wait for better times." Robert didn't like that at all, but it turned out to be a lucky stroke. We went into a very wet winter in early 2017, people stopped worrying about the drought, and when it did sell to Duckhorn, I got a 30% higher price than the previous offer.

Q: How did the deal with Duckhorn shape up?

Jensen: Duckhorn showed they were completely financially serious from the start. The way they approached it enabled a sweet deal for me and my kids regarding the tax status. We owned the property free and clear. When you sell a commercial property, you have to establish a price for the land, and a price for the buildings and other improvements. That's called allocation. We negotiated with Duckhorn how much of the sale price would be for the vineyard land and other land, and they gave us a very high allocation for the land.

Buyers don't usually want to do that. Buyers typically want a low value on the land because land can't be depreciated, but if you pay for buildings, facilities and machinery, you can depreciate them, and it saves the buyer money. But Duckhorn allowed us to negotiate that, so a substantial part of the sale went to my kids, to whom I had given 97% of the planted acreage. They were then able to use section 1031 of the IRS code to avoid a potentially big tax burden. My son, younger daughter and I formed a real estate company, and my other daughter formed a real estate company in San Francisco. Me and the kids bought a commercial property in Santa Rosa with the money from the sale of the Calera property, so the capital gains tax is deferred until we sell the new property.

Q: Why was Duckhorn a good fit for Calera Wine Co.?

Jensen: They liked the bottom line but also the growth potential. In 2017, we were selling about 30,000 cases, but only 3,000 were Mount Harlan (estate-grown wines) because of no goddamn rain, but there was no limit to how much we could make of the Central Coast wines. We also just finished digging a cave for barrel storage, a little over 1,000 linear feet, a year or two before. It was super-expensive but another lucky break, because it turned out Duckhorn didn't have any wineries with caves, and they thought it was cool. They're looking to finish it out for a great visitor experience.

Q: What advice do you have for other winery owners considering a sale?

Jensen: Expect a non-competition agreement. That is four years in my case. And I recommend to everyone to get a specialist to help you. Yes, you could use a real estate broker, and they are capable of finding a buyer, but there are a zillion special questions about winery properties that a Realtor is not going to know how to handle.

Another thing is that you've got to keep your mouth shut. The pros will tell you there's a right way and a wrong way to find buyers. You don't tell your buddies at the golf course. Don't say a word to anybody. It would give an advantage to the buyer. When I was asked by friends during the time it was for sale if I'd ever sell Calera, I said I haven't given it much thought. Later, when the sale was announced, I apologized to them for lying.

— Jim Gordon

State by State DtC Law Changes

Concord, Calif. — The Direct-to-Consumer Symposium, held Jan. 23 and 24, included a report by Steve Gross, vice president of state relations for Wine Institute and member of the board of directors at Free the Grapes, on wine-shipping regulations across the United States as well as 2019 goals for amending bills and opening up the few remaining states where DtC is still illegal or very limited.

Arizona: The state Department of Liquor Licenses and Control sent out about 100 violation notices to wineries that were holding DtC licenses for shipping more than the six-case-per-person limit allotted to wineries in 2017. In 2018, the limit was increased to nine cases. As of 2019, the allotted amount increased to 12 cases (and will stay at 12 cases from here on out).

Illinois: Fulfillment houses now have to fill out shipping reports. Additionally, 837 cease-and-desist letters were sent in January 2018 (290 to wineries) to companies that were illegally shipping to the state.

Virginia: DtC permit fees increased from $95 to $230; application fees for all licenses increased from $65 to $195. Online filing requirements have done away with the notary requirement for applications.

Hawaii: In Honolulu the permit fee increased from $120 to $180 as of April 2018.

Pennsylvania: The Pennsylvania Liquor Control Board (PLCB) improved its DtC reporting interface — direct wine shippers now have the option to upload data using a PLCB-provided Excel template, rather than manually entering sales data for each direct shipment.

Texas: DtC permit holders shipping 5,000 or more gallons are required to file shipping reports on a monthly basis; those shipping less do so quarterly.

Indiana and Tennessee: New reporting requirements were imposed on common carriers as of July 1, 2018 — this is used to compare against winery shipment reports.

Oklahoma: The DtC shipping bill passed in 2016 was amended to remove regulations disallowing shipments into the state of wines sold by local wholesalers.

Kentucky: An on-site DtC bill was signed by the governor in April 2018. But there are restrictions:

- Consumers must purchase on-site from wineries and distilleries.
- If on-site, the business can ship up to four cases per person, per visit.
- If on-site, consumers can pay for and join a "club" to receive up to one case per month per calendar year.
- A "license" is required for the winery or distillery, but the type is not specified in the bill.
- Due to the lack of clarity and restrictions in the bill, common carriers are not shipping interstate at this point.
- Shipments require a written declaration from the consumer that the ship-to address is in a "wet" area for the winery to obtain "safe harbor" from violation.

Goals for 2019

In addition to writing bills to open Alabama, Utah, Delaware and Mississippi to DtC shipments, Free the Grapes is seeking to update or improve many existing laws regulating wine shipping.

Kentucky: Pass a model DtC bill, amending the current law, that removes the on-site restriction, addresses the wet/dry deliveries declaration required by consumers and addresses common-carrier reporting concerns.

New Jersey and Ohio: These two states are currently closed to wineries that make more than 250,000 gallons annually. Working toward a bill that will remove this provision.

Indiana: Remove the restriction on issuing a DtC shipper's permit to anyone who is part of the three-tier system.

Arkansas and Rhode Island: These two states also have an on-site restrictions. Introduce bills in both states to change the statutes.

Alaska and Minnesota: These two states can ship without a permit or taxes. In Minnesota, there is currently a restriction of two cases per person per year; in Alaska, the case restriction is limited to "a reasonable amount." The new bills will stipulate a defined, logical amount (around 24 cases annually) and include the proper taxes and permits needed.

Oklahoma: Fix the recently discovered prohibition on the use of fulfillment houses. State law previously forbade wineries from using a fulfillment house if shipping into Oklahoma.

Arizona: Resolve the stipulation that says wineries cannot accept an order from Arizona between 2 a.m. and 6 a.m. The bill will edit the law to clarify that wineries can process an order at any time but cannot deliver wine between those hours.

Tennessee: New bill will attempt to double the annual case limit from four to eight cases.

Washington and others: Working to prevent wholesalers' anti-carrier language from being adopted and make it easier for common carriers to deliver and report wine shipments. Local wholesaler groups continue to introduce more stringent statues that would shut down the carriers; the goal is to stop that from happening wherever it occurs.

Avalara Buys out Compli, Other Industry News

Avalara, provider of tax compliance automation software, acquired the operational assets of Compli, which offers compliance services, technology, and software to producers, distributors, and importers of alcoholic beverages in the United States. Avalara was founded in 2004 and provides tax compliance automation software to businesses of various sizes around the world. The company is headquartered in Seattle, Wash., with 12 offices in the U.S., Europe, South America and Asia.

Members of the Compli team will now be Avalara employees. The office headquarters will remain in Paso Robles, Calif., and Boulder, Colo. Compli founder and CEO, Rachel Dumas-Rey will now take on the role of general manager of the beverage alcohol division of Avalara.

Dumas-Rey founded Compli in 1997. She earned a bachelor's degree at California Polytechnic State University, San Luis Obispo and a masters from California State University, San Diego. Before starting Compli she worked for the U.S. Department of Commerce and a software company. Jeff Carroll, who helped create ShipCompliant and worked there for more than a decade, joined Compli in 2017 and later became chief product officer. Carroll is based in Boulder and remains part of the Compli/Avalara team.

"We've always provided vertically integrated regulatory compliance but having Avalara behind us gives us power in the industry — especially with the way the industry is changing," said Dumas-Rey in an interview with *Wine Analytics Report*. "This could not have come at a better time."

Dumas-Rey was referring to various compliance changes that have — or will soon — come to pass in the United States, such as the South Dakota versus Wayfair ruling that allows taxes on purchases made from out-of-state sellers, including those without a physical presence in the taxing state, and the upcoming Supreme Court case involving the Tennessee Wine and Spirits Retailers Association that could alter dynamics of the three-tier system.

Although the alcoholic beverage industry is a new segment for Avalara, Dumas-Rey said the company's strength in research into legislative changes — the depth and speed at which they can acquire information — is one of the major benefits of the merger.

Dumas-Rey said Compli and Avalara had been officially discussing the merger since early summer 2018, but such a deal is something she and her team had been considering for even longer. “We’ve been a customer of Avalara for quite some time. Their sales tax rates are incorporated into our eCompli software,” she said.

When asked about any future plans for the business given the new resources Avalara brings, Dumas-Rey said it’s too early to talk about what the integration will mean down the road. “At this point, we’re going to stay the course with our current plans, our tech roadmap and continue to focus on growing our business.”

— Stacy Brsicoe

Industry News

No preliminary crush report, final delayed

The California Department of Food and Agriculture (CDFA) and USDA’s National Agricultural Statistics Service (NASS) announced that because of the recent shutdown of the U.S. federal government there will be no preliminary 2018 California crush report. The agencies also had to delay the release of the final crush and vineyard acreage reports, both of which are dependent on available funding for the 2019 fiscal year. During the shutdown, the NASS was not able to collect data or issue reports. The 2018 California Grape Crush Report will be released April 10. The 2018 California Grape Acreage Report will be released April 19.

Constellation promotes McGrew, SVP of communications

Constellation Brands in Victor, N.Y., promoted Mike McGrew to senior vice president, corporate communications. McGrew is responsible for providing leadership and strategic direction to the company’s communications teams to support the company’s objectives in beer, wine, spirits and cannabis. McGrew joined Constellation in 2014 as senior director of communications for the company’s beer division.

Guarachi hires vice president of sales

Guarachi Wine Partners in Napa, Calif., promoted Bill Matthes to vice president of national sales. Matthes was previously division vice president of the Eastern U.S. region for the company. In his new role, Matthes’ will focus on sales strategy and long-term growth objectives for all Guarachi Wine Partners brands across California and South America in addition to overseeing the national sales team.

Truett-Hurst hires director of winemaking

Truett-Hurst in Healdsburg, Calif., appointed of Ross Reedy as its new director of winemaking. Reedy will be responsible for all winemaking of the Truett-Hurst and VML brands located Healdsburg, Calif., and production at Sugarloaf Crush facility located in Santa Rosa, Calif.. Reedy began as a cellar assistant in 2012 and studied wine and viticulture at California Polytechnic Institute, San Luis Obispo, graduating in 2005.

New marketing VP at Daou

Daou Vineyards & Winery in Paso Robles, Calif., hired Alexis Walsh as its new senior vice president of marketing. Walsh comes to Daou from Treasury Wine Estates, where she most recently served as vice president of commercial strategy and on-premise. Prior to that, she spent six years at Trinchero Family Estates, where she had roles in brand management and national account on-premise sales. Walsh earned a master's degree from the University of California, Berkeley; and a bachelor's degree in psychology, *cum laude*, from Harvard University.

DeLille Cellars names new director of winemaking

Jason Gorski has been promoted to director of winemaking and viticulture at DeLille Cellars in Redmond, Wash. Gorski previously served as winemaker and assistant winemaker, under the tutelage of founding winemaker Chris Upchurch. With Gorski's promotion, Upchurch remains co-president, partner and founding winemaker. He will continue to be actively involved, supporting Gorski and the winemaking team with harvest and blending, as well as helping to guide the company's goals from an ownership perspective. Upchurch also plans on focusing his efforts on supporting the national sales program and continuing to be present at retail events, according to a press release announcing the changes.