

## The Key Report 13<sup>th</sup> January 2003

### **1. Editorial**

Lots of fun, heaps of good wine, plates of exquisite food, now it's back to work. There's little in the way of full on excitement happening at the moment, although as I write this, some mega takeover or collapse is probably taking place. Murphy or sod's law does rule. Anyhow let's be positive: Happy New Year to you all. The opinion in the office is that 2003 will prove very interesting for the Australian wine industry. Perhaps it will be a watershed year or maybe just the phase of emerging from puberty to adulthood. Although the term Australian Wine Industry is freely applied, in reality it should be considered in its various aspects. The big guys and the rest, growers, producers, aspects of tourism and more, not forgetting the wine itself.

We think it's safe to assume that people in the industry realise that Australia is indeed a world player in the wine game. We expect that game to get tougher, even a little dirty this year. How injured or victorious will our players be by next Christmas?

At the small independent producer end, there are too many in the market place, and some will fall by the wayside this year. If your cellar door can make more money by selling jam, dollies or sex toys don't hang around - get the sales going!

We hope not, but something tells us the grower producer relationship is going to be stretched further this year.

Lets play on! TK.

### **2. US Slump**

A review of various articles published in the US over the past three weeks indicates that the Californian wine industry is facing a slump, partly due to increased plantings, partly due to under performing wine consumption and partly due to a worldwide wine glut resulting in cheap imports. According to figures released by A.C. Nielsen, seasonal sales of Californian wine declined in nearly all categories in the last quarter of 2002 - the first time in almost a decade. One newspaper article said, "Meanwhile good, cheap wine from Australia, South America and South Africa is filling stores."

The situation can be paralleled with Australia, but the difference is that we flog a lot more wine to them than they do to us.

### **3. Christmas Day in New York**

An article in the New York Times dated 25<sup>th</sup> December was headed "Wine Prices Drop Sharply, a Good Reason for Cheer" By Amanda Hesser. There is little need to reproduce the article the title says it all. The point to note is that it doesn't only apply to Californian, Oregon or Washington State wine, but imported wine as well. One report was uncannily similar to the Wynns John Riddoch and Michael story in Australia: a Californian Cabernet Sauvignon selling for "\$75 last year, is now \$53." Apart from the list of top wines that are now selling much cheaper, the quote that stood out for me was "I think a lot of people aren't admitting what's happening," Karen King, the wine director at Union Square Cafe in Manhattan, said, "because the minute you admit it, it's true."

The problems are not confined to the pricey end of the market either. Plantings in California have increased from around 310, 000 acres in 1996, to about 570,000 acres in 2001 so there's a lot of every day grog available out there. One retail group has started selling Charles Shaw's Chardonnay, Cabernet Sauvignon and Merlot at US\$1.99 a bottle.

The article says growers will be hit first with nowhere to sell their grapes. Imported wines have increased their market share by 5%, Australia accounting for a fair percentage of this.

### **4. Holy Snappin' Supermarkets!**

Morrisons, a northern England based supermarket chain that has a good reputation for the variety of wines stocked, has just made a £2.5 billion (A\$6 billion) agreed bid for Safeway, the

fourth biggest UK grocery retailer. The news sent most UK supermarket shares lower, the feeling being that it may bring forth a rival bid - the favourite being Wal-Mart.

What does it mean for Australian wine? One less sales outlet (that's 450 Safeway stores). Then again, if your wine is stocked in Morrisons, you have **gained** 450 outlets. But Morrisons will have to rethink their buying strategy as sourcing for almost 600 stores requires greater product than it does for 120. But if Wal-Mart enters the scene, the game plan will change again. Whatever happens, it looks shaky for those medium sized Australian producers that did well meeting the requirements of Morrison.

## **5. Consumers are wary**

America was not the only place that had less than wanted consumer spending over the Christmas period. I am informed that the normal term is "less than expected" but over the years I have found it hard to get a grip on exactly what 'expected' is. Enough is never enough and there is always a reason for it not being so. War in Iraq was the leading contender in 2002.

Exuberant Yule Tide spending was down in Europe. The Confederation of British Industry has reported the worst pre Christmas sales for 10 years in a survey covering the period 4 to 18 December. Dixons and Next, two large retail chains, have declared their disappointment with Christmas sales figures. "Falling consumer confidence" was one statement. Perhaps a more telling statement was the one made by John Clare, CEO of Dixons (the largest electrical retailer in the UK) who says consumers are "now cautious about sales for the next four to five months." Consumers are also being more careful about taking up credit. Reports from France, Germany and Italy are all suggesting the same.

How does that translate to wine buying in the UK? If past experience is anything to go by, wine sales will not grind to a halt, however patterns will alter. In a flat economic period, consumers are often loath to change or experiment, sticking with the tried and tested. In this respect Australia is lucky - it has more than 20% of the market and is seen as an old reliable friend.

Eating out is one of the first things to be cut out or reduced hence less wine sales. Home consumption is adjusted - perhaps a couple of alcohol free nights or maybe those couple of bottles that cost a bit extra for the weekend suddenly don't cost that much extra. At work the screws are tightened on expenses both for the office and client entertainment.

## **6. Lion's fur ball.**

A media release prior to Christmas states: "Lion Nathan Limited and Banksia Wines Limited announced today that Lion intends to make, through its wholly owned subsidiary Lion Nathan Enterprises Pty Limited, a cash offer of \$1.27 per share for all the shares in Banksia that it does not already own." Allied Domecq holds the majority of those wayward shares; unless they come to the party then the status quo will remain, much to Lion's annoyance.

Back in May 2001 when Lion held just over 60% of Montana and Allied around 27%, Banksia was tying up a deal with Montana where the NZ company would assume responsibility for the distribution in key eastern seaboard markets in Australia for Tatachilla. Montana added St Hallet who had just merged with Tatachilla to its New Zealand distribution portfolio. By the end of August 2001 the battle was over - Lion saying it would accept a NZ\$4.80 a share offer from Allied which valued Montana at NZ\$1 billion (\$440 million).

Lion took a pre tax profit from the sale of NZ\$127 million and went looking for wineries to buy in Australia. Within a month it was announced that Lion would launch a takeover offer for all the shares in Banksia Wines Ltd. On 8 October a statement was put out via the Australian Stock Exchange "Allied Domecq PLC confirms that it today acquired shares in Banksia Wines Limited to take its total shareholding in Banksia Wines Limited to 14.97%." The reason given by Allied Domecq was to safeguard the distribution deal Montana had with Banksia wines in NZ. Allied also said it had no plans to launch a rival bid for Banksia.

We asked Lion if they had offered an olive branch to Allied re certain distribution arrangements: "Not at liberty to say" was the response from Lion. Have Allied agreed to take up the offer? "Not yet" they said. There appears little reason for Allied to sell - unless there is an underlying motive on the distribution issue.

#### **7. Who's snappin' up whom?**

It is fascinating to know who owns what or who is owned by whom. We know Lion Nathan has a stake in the Australian wine industry because it bought Banksia and the Petaluma group. Most know that the Japanese Brewer Kirin owns 46% of Lion Nathan.

Perhaps not so well known is that Kirin also has an indirect 4.8% with 7.9% voting rights in Pernod Ricard, and we all know Pernod Ricard owns Orlando-Wyndham (Jacobs Creek), don't we?

#### **8. My, my partner what a juicy morsel you are!**

BRL Hardy's USA joint venture partner Constellation Brands has reported net income up 18% to US\$10m for the third quarter, to reach US\$64m for the year. A good result as it was ahead of analysts' forecasts. If they continue along the same lines, BRL might be seen as fitting in their portfolio, rather than a Joint Venture partner.

#### **9. Wolf jumps Kangaroo (Ridge)**

We didn't cover it at the time and you probably read it in a national or local newspaper:

*"Beringer Blass forms equity partnership with Kangaroo Ridge"*

What is interesting to us is how one bloke - John Geber, managed to trundle around Europe with a few samples and flog over a quarter of a million cases in only the second year of his company's existence. When Beringer Blass, with their multi million dollar army of reps, regional, national and international sales managers, couldn't do it themselves. Nice one John.

"Kangaroo Ridge will give it entry into some tough European markets" says Beringer Blass. Why? It can't be because they don't have access to that style of wine - we all know there is an ocean of it out there. Is it because of their insistence, up until now, of being only a premium wine company but they now realise that to expand into Europe they need entry-level wines? In their wisdom, they have bought off the shelf rather than develop a brand themselves. What they paid wasn't disclosed but obviously worthwhile to Beringer Blass, and to John, no doubt.

#### **10. Did he walk or was he pushed?**

News of executives coming and going is hardly news nowadays. Some guy from a Roller Coaster manufacturing company is offered a big pile of dosh to come and revitalize a wine company... stays for a few months, is deemed unsuitable and offered another pile of dosh to go muck up some other company in another industry.

Mario Micheli was the regional president UK, Europe, Africa and Middle East of Southcorp Wines Europe. Southcorp say he left, a report in Harpers (UK Mag) said he was sacked. So was he pushed or did he walk and why? "To pursue other interests and career aspirations." says the article. It also said that in his three years "he soon installed two of his former Anheuser-Busch colleagues, Peter Jackson and James Lousada and oversaw a refurbishment of the Southcorp premises in Twickenham, southwest London." If he did no more than find a couple of mates a job and splosh a bit of paint around then one can understand his departure.

New man in the job is Jeffrey Wilkinson - a former Rosemount man whose recent role has been Southcorp's General Manager, Operations, New South Wales and Victoria. Could it be the same Jeffrey Wilkinson that looked after us so well at the Yellowglen Cellar Door all those years ago?

#### **11. Who loves you baby?**

Enough doom & gloom, how about this for a media release to make you smile:

"Fans of Petite Sirah, a red grape grown on limited acreage in the North Coast (California) and not known to most wine consumers, have formed a new marketing and promotion group called PS I Love You."

Perhaps the winemakers of Durif in Australia should band together to support fellow Californian vigneron with a group called PS We Love You Too!

## **12. Corks save Cats?**

We just hope you feel guilty, you heartless, animal-slaughtering users of screwcaps. It was the 27<sup>th</sup> December 2002. We blow the dust off the keyboard, crank up the computer and this comes through the wires: "Drinkers are being urged to sup wine and champagne from bottles with cork stoppers to help save the world's rarest big cat. The cork forests of Spain and Portugal - home of the endangered Iberian lynx - are under threat because of the increasing use of synthetic and screw top stoppers."

The release continues "It is often more profitable to destroy the animals' woodland homes and replace them with other less environmentally-friendly forms of forestry and agriculture." So, if we stop buying wine with cork stoppers, they reckon the cork farmers will rip out all their cork trees, and plant wheat or something in which the lynx can't live. Therefore it's our fault, the wine drinkers of the world. No responsibility on the Spanish or Portuguese governments, no questions on how the poor Iberian lynx reduced to just 150. Or are we to assume that the decline has only been in the last say 3 - 5 years? It's all down to bottle stoppers, not swimming floats, floor tiles or 70's three-inch heels.

We feel for the lynx but think it is unfair to lay his predicament at the door of the world's wine industry. As it is time for the bottle closure to move forward, so it is time for the cork industry to look for alternative uses.

As for the closing paragraph "WWF forests campaigner Beatrix Richards said: "Clever propaganda by the manufacturers of screw tops and plastic corks has led many people to think that cork stoppers are bad for the environment when exactly the opposite is true."

To our knowledge all the industry propaganda has been about how bad cork stuffs up an unacceptable percentage of wine, not about the environment.

## **13. Wise words from Aunty ABARE**

Australian Bureau of Agricultural and Resource Economics (ABARE) predicts that wine grape output in 2002-03 will fall 3% to 1.56 million tonnes. "The dry seasonal conditions throughout 2002 will result in the first fall in wine grape production since 1996-97."

More wise words include "Production is projected to increase by 13% to 1.77 million tonnes over the next two years to 2004-05, assuming average seasonal conditions. There will be more red than white. South Australia is going to remain the major wine producing state."

ABARE also said wine grape production would increasingly be driven by wine exports, however they did recognize the fact that international competition was increasing.

## **14. Drought on the Truth**

"Australian yields down by half as drought bites" is the heading of a short article by Josie Butchart on decanter.com 8 January 2003. The article centres on Victoria and says not a great deal harmful or otherwise it's just that title. TK is off to the UK next week and reckons more than one consumer will comment on how bad the Australian 2003 vintage will be. We look forward to more newsbreaking stories from our reporter at large.

## **15. Belly Laughs**

- "Beer belly gene found" is a headline that grabs the attention (of some of us anyway). "Scientists have found that men with a certain gene variation have a tendency to get a flabby stomach. Understanding genetic predisposition to weight gain is an essential step

in arresting the stigma that obesity is always an individual's fault. " So there - it's not my fault or the beer, it's just the way I am built.

- And a couple of announcements from the Australian Stock Exchange:  
Invesco Australia Ltd ceased to be a substantial shareholder in Peter Lehmann Wines on 20/11/2002.  
Invesco Australia Ltd became a substantial shareholder in Peter Lehmann Wines on 26/11/2002 with a relevant interest in the issued share capital of 2,076,885 ordinary shares (5.5664%).  
Is Invesco in or out? Why were they out six days before they were in?
- Loved this snippet from The Weekend Australian just before Christmas: "Police investigating a spate of robberies in Berlin bars say they are having difficulty finding witnesses who were sober enough to describe the robbers."
- David Anderson (Wild Duck Creek), quoted in the December – January edition of Australian Gourmet Traveller Wine Magazine: "People say: 'Holy snappin' arseholes, how do you get that sort of stuff? I don't know how you do it!' But when the grapes are picked at the end of April, they're not shriveling- they bounce into the crusher." Great visuals David.

#### **16. Up, Up and Away**

It was on the TV, radio and in the newspapers, with headlines such as "Australian wine exports surge to record levels". All the right words were there. Record, value, soaring, quality, good and value (again). Positive all the way and why shouldn't it be? The facts: we exported 471 million litres in 2002 - 26% up on 2001. The exports earned almost \$2.3 billion, an increase of 30% (\$531 million.)

#### **17. What's on today – Bird watching, Rock Climbing or Wine Tasting?**

There will undoubtedly be a spin off for wine related tourism, with the news that Federal Tourism Minister Joe Hockey is to present a green paper in favour of a more targeted approach. Some of Mr Hockey's comments include "Instead of targeting Ma and Pa in the US, we have to start targeting George and Barbara." (slightly confusing - we thought George and Barbara were the Ma & Pa of President George Dubya?)

In simple words Mr. Hockey wants to attract more affluent hence higher spending visitors from all parts of the globe. One aspect is "niche markets" ie hobbies "from bird-watching to rock-climbing." We assume wine will enter this category as well.

Interesting to see who spends what. In 1999/2000 total visitors to Australia spent on average, \$4066 each trip. The Chinese spent most, averaging \$6070, followed by the Americans \$5899, Europeans (excluding the Brits) \$5411. Coming bottom of the table, New Zealanders \$1808.