



CIATTI
GLOBAL WINE & GRAPE BROKERS



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**Ciatti Global Wine
& Grape Brokers**

201 Alameda del Prado, Suite 101
Novato, CA 94949
Phone (415) 458-5150



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As 2019 begins, we at Ciatti wish all of our friends, clients and business associates a very happy and prosperous year ahead. We thank you for your continued support.

The wine world is now back in full swing after the holidays and this month's report reviews the past year on California's bulk market and assesses what the new one may bring. Please turn to page 2 for more.

It is hoped the state's record winegrape harvest in 2018 will open up some exciting grape and wine options for buyers with an eye for opportunity, sensing now is the time to innovate, build new lines and generally inject some dynamism into the wine retail market. If you are a supplier with grapes or bulk wines that you think may interest such buyers, do get in touch with us. And if you are a buyer, a reminder that we have installed a new tasting area in our new offices at 201 Alameda del Prado #101, Novato, where you can sample bulk and bottled wines, so give us a call and we will gladly book you in.

Ciatti is here to help you navigate the market in 2019 and beyond, whatever's coming down the track. Keep reading our *California* and *Global* reports for the latest market insights, and we once again wish you a Happy New Year!

Robert Selby

Hot Opps Box

There are potential opportunities available on all varietals – grapes and bulk wine – including from premium appellations. We are seeing Cabernet available from most premium markets in the North Coast. Cabernet from 2016 and 2017 is also available. There are also opportunities on Pinot Noir from the North Coast and Central Coast, including Russian River, at attractive pricing. Zinfandel continues to be available from most areas of the state. Samples of 2018 wines are feeding through now so get in touch.

Events

Ciatti brokers will be speaking at these upcoming events:

- **January 17:** Sonoma County Winegrowers Dollars & Sense seminar and trade show Luther Burbank Center for the Arts, Santa Rosa
- **January 30:** Unified Wine & Grape Symposium, Sacramento Convention Center

2018: The Year That Was

Activity on the Californian winegrape market was somewhat sluggish coming into 2018 off the back of two successive average-sized harvests in 2016 and 2017 (both of approximately 4 million tons) and the highest percentage of contracted fruit, on multi-year contracts, that Ciatti had ever seen. Bulk wine sales were also sluggish as the premiumization trend – the increase in consumer demand for wines priced at \$9+ per bottle which had been the market’s main driver in recent times – was noticeably slowing. The perception crystallized that US wine on the domestic retail market faces growing competition from craft beer, spirits and – on the West Coast – cannabis (recreational use of which has been legal in California since 1 January 2018) and to a lesser extent from imported packaged wines such as Provencal rosé, Prosecco and New Zealand Sauvignon Blanc.

In addition, the weakness of pound sterling leading up to, and following, the Brexit referendum on 23 June 2016 subsequently subdued demand from the UK, one of Californian wine’s most important export markets. The graph here shows the sterling/dollar exchange for the past five years: sterling weakened gradually in the months ahead of the vote, then plunged almost overnight from £1.40/dollar to £1.32/dollar after it. In September/October 2016 sterling took a further dive, into the £1.20s/dollar, where it has been for periods of time since.



Source: XE Currency Converter

Despite talk of better than expected US retail sales for domestic wine in the final quarter of 2017, the first quarter of 2018 was markedly sluggish for bulk wine buying activity. Inquiries from sellers outnumbered those from buyers and significant inventory was available on the market, more than in the equivalent period of 2017. A disconnect was becoming more noticeable between the prices being asked by suppliers for their wine or grapes – still rising in many cases and at historic highs on some – and the reality of the market, where many program owners faced a thankless combination of an input margin squeeze and retail sales slowdown. This accelerated the shift from specific Coastal appellations to the ‘California’ appellation on labels, something which enables program owners to source more amenably-priced wines from alternative Coastal appellations, Lodi or the northern interior.

The Chardonnay market in particular was seeing two mutually-supporting dynamics: Coastal brands were moving to source in the northern interior in order to ameliorate cost; northern interior ‘California’ brands were moving in the opposite direction to boost quality. The latter move highlighted that potential opportunities on the Coast could be opening due to such movement away from the region. These opportunities were quickly being snapped-up on Chardonnay, the most in-demand varietal on both wine and grapes in the first quarter of 2018 due to three successive lighter-than-average harvests (output in North Coast districts 1-5, for example, was down 19.7%, 4.4 million gallons, in 2017 from 2016). But on Cabernet, which in 2017 had experienced a second-successive record-breaking yield (+5.9% to 599,833 tons), and saw continued plantings, the opportunities lingered.

By mid-2018 the conversation had shifted squarely from one of ‘premiumization’ to one of ‘margin management’. The growing focus was now on creating brands marketed around a distinctive brand identity and the quality of the wine inside,

See next page for more on 2018: The Year That Was.

not necessarily a particular wine appellation. These brands would retail closer to the midmarket: for example, at \$13-16/ bottle. At the same time, positioned just under that price category, at perhaps \$9-12/bottle, good quality brands were starting to be launched that 100% source from Lodi/the northern interior, lifting the market at the lower end.

This mid-market is already getting crowded. Gomberg-Fredrikson data for the first six months of 2018 showed that food store sales in wine's \$9-12 category – now the biggest category by market share as brands seek to congregate there – were up only 1.9%. Sales in the \$12-15 category were up 7.6% but this price point still only accounts for 6.9% of the total market. The biggest volume growth – 13.1% - was in fact seen in the 3-liter box category (priced at \$4-7), reminding the industry that consumer demand is there for innovative wine products that offer an attractive price-quality ratio. Would the size of the 2018 harvest allow for the ability – and compound the need – to innovate?

March brought welcome, persistent rainfall that helped replenish water reserves, as well as snows in the Sierra Nevada that boosted snowpack levels. The cooler than normal temperatures – particularly pronounced in the North Coast and in the Paso Robles area of the Central Coast – continued into April, so that by May it was clear the growing season was running slightly behind schedule. It was difficult to assess the set situation as May turned to June; even in Lodi and the northern interior set was running 7-14 days behind the five-year average. June and July finally brought heat, but temperatures were not excessive and mornings and nights remained relatively cool – perfect weather for veraison, so that, with little if any disease pressure, the crop began sizing-up. By July, Allied Grape Growers was estimating the 2018 winegrape crop could be as large as 4.25 million tons, a state record.

With a big harvest expected to add to an already significant inventory, Ciatti was fielding requests from companies seeking to move bulk wine in order to clear tank space, but the continuing disconnect between suppliers' price expectations and the realities of the marketplace ensured activity proceeded sluggishly. The bulk wine market also remained muted, with some wineries that are traditionally buyers seeking instead to sell in order to adjust their inventory. To varying extents depending on area, activity for Chardonnay, Pinot Noir and Merlot grapes remained approximately in-line with the prior year's. The Cabernet market was slightly less active across all areas, while the Zinfandel market was noticeably slower. Of the main varietals, only Central Coast and Lodi/northern interior Sauvignon Blanc, and Central Coast Merlot, were seeing more activity than 12 months earlier. A presentation at June's Vineyard Economics Symposium in Sonoma raised the question of how high the final shelf price would need to be to accommodate the steep grape prices being quoted in the market, and if there is consumer demand for wine at that price point – they were discussing Cabernet, but it could as well apply to the overall market.

The second half of August and September brought cooler than normal temperatures to California's growing areas, slowing development of optimum brix and sugar levels so that many growers held off from picking – all the while, the crop was sizing-up. The harvest grew elongated into October and November: some North Coast wineries were crushing into late November. In the Coast, winery capacity, already limited due to the large pre-existing inventory, became stretched; some wineries closed their doors to more fruit, leaving growers to deal with their overages as they saw fit. Despite a few challenges, weather-wise, most of California's vines remained very healthy throughout the season, producing excellent quality grapes in – as it turns out – bountiful quantities. It is estimated that the 2018 winegrape harvest came in at 4.3+ million tons, the largest in California's history, though – due to vine removals in recent years and the trend towards premium Coastal areas – the Central Valley's 2018 harvest volume was not a record-breaker.

With the large pre-existing inventory, a record-breaking Californian crop and a slow market, the million-dollar question as 2018 drew to a close was: will suppliers grow more sensitive to the realities of the marketplace as it is now, not what it once was, and ensure they don't price themselves out of finding a home for their grapes or wine? Globally, with bulk wine supply now long, power has moved into the hands of the buyer, and in California it's no different. Suppliers need to be amenable on price to ensure the industry has the ability to sell its way out of a high inventory, low activity market situation. By the end of 2018 Ciatti could offer opportunities on all varietals – as grapes and bulk wine – from premium appellations, including 2016, 2017 and 2018 Cabernet from premium North Coast appellations, and Pinot Noir from the North Coast and Central Coast, including Russian River.

2019: Looking Ahead

We are already seeing bulk wines from the 2018 crop hit the market and a little price softening here and there is attracting interest from négociants and entrepreneurial buyers eyeing the opportunity to start and build innovative new lines for the retail market (including on 2018 Pinot Noir, Sauvignon Blanc and Chardonnay), as well as those seeking opportunities on private label and control brands. Ciatti would like to hear from suppliers who feel they may have wines to interest such buyers, and for buyers to contact us or come down and visit us at our new offices at 201 Alameda del Prado #101, Novato, where potential buyers can sample bulk and bottled wines.

If Coastal appellation wines soften a little in price, it may encourage some brands that moved away to the 'California' appellation to return, or for the quality 'California' blends to be reinforced by greater percentages of premium Coastal wines going into them.

Due to the new marketplace realities, we expect the level of contracted fruit in California to gradually decline as – over time – grape contracts come up for renewal and are renegotiated to cover fewer tons. These contracts may also be agreed at lower pricing, so that average prices soften over time – though slowly, as many grapes are under multiple-year contracts. By the end of this year we expect to see fewer grapes and bulk wines under longer-term contracts, and the spot market potentially able to offer pricing below the market average. Again, this greater market flexibility should suit the opportunistic buyer.

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Contact Us

Chris Welch

T. +415 298-8316
E. chris@ciatti.com

John Ciatti

T. +707 264-0762
E. johnw@ciatti.com

Johnny Leonardo

T. +415 717-4438
E. johnny@ciatti.com

Glenn Proctor

T. +707 337-0609
E. glenn@ciatti.com

John White

T. +415 250-0685
E. johnw@ciatti.com

Todd Azevedo

T. +415 265-6943
E. todd@ciatti.com

Greg Livengood

T. +415 497-5032
E. greg@ciatti.com

Steve Dorfman

T. +707 321-3843
E. steve@ciatti.com

Dennis Schrapp

T. +905 354-7878
E. dennis@ciatticanada.com

Jed Lucey

T. +415 630-2431
E. jed@ciatti.com

Mark Ishimaru

T. +415 630-2548
E. mark@ciatti.com

Molly Richardson

T. +415 630-2146
E. molly@ciatti.com

John Fearless CO. Craft Hops & Provisions

CEO - Rob Bolch
Sales - Geoff Eiter
Purveyor of Quality Used Oak Barrels -
Raymond Willmers
T. + 1 800 288 5056
E. rob@johnfearless.com
E. geoff@johnfearless.com
E. raymond@johnfearless.com
www.johnfearless.com

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