Wine Investment in South Africa

David March

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Dissertation submitted to the Cape Wine Academy in partial fulfilment of the requirements for the diploma of Cape Wine Master

I, David Allan March, declare that this research report is my own, unaided work. It is submitted in partial fulfilment of the requirements for the diploma of Cape Wine Master to the Cape Wine Academy. It has not been submitted before for qualification of examination in this or any other educational organisation.

Signed

Dated

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Abstract

Wine Investment in South Africa

'the acquisition of wine for gain….as a means of making money or financing consumption'
(Robinson, et al, 1994)

It is seventeen years since Micheal Fridjhon stated in Wine Magazine that the South African market was too small to provide opportunities for wine investment (Fridjhon,1994). Asked whether that is still the case in 2011, Fridjhon replied that it is;

> 'There is insufficient demand, lack of agreement on what would be the icons, concerns over quality of storage and no real transactional environment' (Fridjhon, 2011)

This report will consider whether the situation has really not changed.

Despite the small potential market for investment there have been attempts to establish a trading platform in South Africa and the basis of an en primeur system, yet many schemes have perished and at present, only one winery is offering wine futures (Kanonkop; but some others are offering a variation on this) and only a few businesses offer investment purchases together with storage and trade. Only two specialised wine auctions exist in SA and one of those is not open to the public (Nederberg auction) and the other (CWG auction) is dominated by trade buyers leaving little opportunity for the individual investor.

In the meantime, Europe, America and Asia have established themselves as the centres of the wine trade and demand seems as strong as ever. Fortunes have been made and are being made from trading wine. Prices are outpacing other forms of investment.

Presently, wine investment in SA involves purchasing foreign wines, mainly Bordeaux and storing them abroad or with a merchant in SA. Few, if any SA wines are considered investible and there is no real market to trade purchases here; sales will be through the merchants who will demand a fee for the service. There is little opportunity for an individual to trade wines themselves, firstly as a licence is required to do so and secondly as there isn't a marketplace to advertise such sales.

Anyone reading copious amounts of newsprint and market reports could assume that investors are making serious profits. So too are the producers, auction houses, storage facilities, importers, fund managers, merchants; and from each the governments are reaping the rewards via Duties and Taxes. Is South Africa missing an opportunity?

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Section 1

Chapter 1

1.1 Introduction

Investing and trading in some wines, based on demand exceeding supply, has proved a profitable exercise for hundreds of years in Europe. More than ever today, wine has proven to be a highly tradable commodity and the trading hub has spread to the USA and Asia, in particular Hong Kong. Indeed, wine has outperformed many other commodities for investor returns for decades. In 'flat' economies and even in recessions, wine has offered returns which match or better many other forms of investment. In 2004, during a stable but unexciting economic period in Europe the en primeur campaign in Bordeaux saw prices fall by some 20%. Château Lafite, for example, set its release price at €80 (R800) but even this was a 33% gain on its 2002 release price of €60 (R600); a growth over 24 months many investors would be happy with. Having purchased 2004 Lafite at €100 (R1000, ex négociants etc) you would need to spend an average of €600 (R6000) to purchase that wine in bond today (Berry Bros & Rudd, 2011) – and that would be for a vintage that many recommended avoiding for investment. Over the seven years since purchase that represents an annual return of 70%.

Fine wine from Bordeaux has been a more lucrative investment over the past 12 months than gold, crude oil or shares, according to the Liv-ex Fine Wine Exchange (see 3.2) and reported on Decanter.com 4th January 2011. Prices for the top five Bordeaux châteaux across ten different vintages had risen by 57% during 2010, compared to a 35% rise in the value of gold over the same period, while crude oil had risen by only 20%. For the top Châteaux the returns have achieved 15% compound interest annually over the last 25 years according to the Financial Times in the UK (Financial Times UK, 2008).

Yet South Africa has not developed any significant investment trading environment. There have been initiatives; some schemes have offered wine futures or cellaring opportunities with a view to future trade profit or buyer discounts, but there does not appear to be a platform for wine as a trading commodity as exists in Europe, the US or Asia. Seventeen years ago Michael Fridjhon stated in Wine Magazine that the South African market was too small to provide opportunities for wine investment (Fridjhon, 1994), this report will examine whether the situation has changed and whether South Africa could support such activity and how investment in SA wine might occur.

1.2 Scope of Assignment

Wine investment can take the form of purchase, part purchase, ownership of shares in a wine farm or winery or purchase of wine in order to resell for a profit. This report will examine the last of these; **the investment in wine as a product.** It will not include investing in any infrastructure, grape growing or winemaking business. More specifically, this report focuses on '**Investing in SA wines**.'

The purpose of this report is to review the history of wine investment internationally and in South Africa, examine the current market and opportunities to invest in wine, and discuss possible investment potential and future trends.

Information and data will be sought from producers, industry observers, and secondary trade establishments such as auction houses via interview, research and review.

For the purposes of international price and cost purposes, most prices have been converted into SA Rand. To simplify a fluctuating exchange rate, a mid price was taken during March 2011. All examples were converted at;

R11	=	GBP1 (£)	R0.9	=	HK$1
R10	=	€1	R7	=	US$1

All wines are based on 75cl content and in full cases of 12 bottles.

All prices are estimates and rounded out for ease of comparison.

1.3 Contribution of Assignment

A wine investment market in South Africa would generate considerable financial activity. With more than $3bn (R21bn) realised by trading in wine around the world (Wasserman, 2010; Miles, 2009) the potential to be part of that is enticing, creating jobs, individual wealth, new businesses and revenues for the State. Trading in wine could bring direct overseas investment and offer individuals and businesses opportunities to realise profit and improve lives. SA wines traded internationally might act as ambassadors for the country, much as Napa Valley wines do for California. With tradable icon wines recognised in markets around the world there is an incentive for improvements throughout the wine industry and familiarity with 'brand SA' boosting sales at all price points everywhere.

This report seeks to promote the investment in wine, especially South African wine and stimulate interest in creating a trading market in South Africa.

1.4 Outline of Assignment

This report will examine the history and international background of wine investment in Chapter 2, its origins in Bordeaux and the en primeur system. It will look at recent developments such as the expansion of investment in the US and Asia in Chapter 3 and relate investment to economic fluctuations. Statistics will show how wine has become a tradable commodity and the returns it has provided for investors. The types of wine investment with a comparison of costs and administration will be reviewed in Chapter 4. Chapter 5 will look at the shifting of the main trading hubs and the role of industry observers and critics. The possible barriers to investing in wine, both in South Africa and elsewhere, are outlined in Chapter 6. Section 2 concentrates on South Africa, looking at its wine culture in Chapter 7 and in Chapter 8 examines the history, nature of and problems associated with wine investment in South Africa. Section 3 looks at future trends and the way forward. It will speculate whether SA has sufficient high value imported and indigenous wine (and demand) to create a bigger trading platform. It will also consider market conditions, wine styles (longevity), scarcity and whether SA could view wine as a speculative investment area in the same way as Europe, the US and Asia does. A conclusion and summary is given in Section 4.

1.5 Key Findings

Very little literature exists specifically about investing in wine in South Africa. Despite a wealth of articles and websites devoted to various funds and auction sale figures in Europe, America, and more recently Asia, there is little if any reference to South Africa or its wines. Industry commentators, in South Africa and abroad, seem not to consider SA wines investible (at present) and most find the idea of SA as an investment trading hub unlikely.

There are few investors using wine as an investment asset in SA and those that do probably are not including SA wines in their portfolio. Without a trading platform demanded by investors there is no secondary market. Many respondents felt that having a secondary market could benefit everyone; presenting exciting business opportunities as well as access to rare wine.

The paradox is that most commentators are cognisant of the quality and longevity of SA fine wines and see no reason for them not to join other New World wines being traded alongside Burgundy, Rhone and Bordeaux. Indeed, many found their (relatively) low prices – even at the very top end – most attractive as potential high growth assets and certainly felt they had an advantage in this respect.

The barriers that seem to exist which prevent some from investing in SA wine are largely the same for the rest of the world. What distinguishes South Africa seems to be a lack of awareness and confidence in the SA wine market and its wines and a lack of opportunity to buy, store and trade.

1.6 Key Message

The message clearly supported by most was that there is real potential for investment in SA wines and that there is no reason why a small, but successful secondary market could not exist in SA, though most commentators felt this was some way off. The message was that SA wines at the top end are equal to the best in the world and that in time the world would accept this and they would become highly tradable, realising profits for those with foresight.

There is also an opportunity for South Africa to play to its strengths in establishing icon wines in areas where it is already forging a considerable reputation. Those areas include Bordeaux blends, Port style wines, MCC wines, Shiraz, and Cape blends.

Chapter 2 Investment history

2.1 The international background to wine trading and investment

Europe has a long history of wine trading, and if the nature of wine investment is to make profit from buying and selling wine then also a long history of wine investment, with Bordeaux at its epicentre. Bordeaux châteaux never delt directly with customers (and to some extent still don't) but would sell their wines through Brokers or 'Courtiers'. It was the courtier's job to receive samples of unfinished wine and entice as many négociants as necessary to buy their châteaux allocation, often charging around 2% for their service (Kissack, 2011). The négociants would either finish making the wine (many châteaux did not own expensive winemaking equipment) or buy it finished in barrel prior to possible blending, ageing and bottling under their own name. Often, négociants had to blend several parcels in order to meet their stock requirements, frequently the case in Burgundy. Only relatively recently (1935) have Appellation d'Origine Contrôlée (AOC, now the Appellation d'Origine Protégée) regulations prevented blending if the wine is stated as coming from one particular château and many châteaux, in order to avoid poor quality blends appearing on the market under their name, introduced bottling under their own label prior to delivery to négociants, to avoid this. 'Mis en bouteille au château' was an attempt to show the consumer that the wine was authentic and unadulterated. Négociants would then add some

15% to the price and sell the wine to their network of worldwide agents, importers, wholesalers and restaurants (Kissack, 2011).

2.2 Wine futures

Bordeaux producers knew that their wine was greatly improved by prolonged maturation in barrel, but this might mean several years before any financial return could be realised. Anxious to realise early income the idea of selling wine in barrel (some six months after harvest and before bottling) was born; with immediate ownership but only future delivery guaranteed. In fact, the practice of selling wine whilst still on the vine was practiced in Roman times (Robinson et al, 1999). This ‘futures’ or ‘en primeur’ option suited both parties despite more risk on the buyer’s part as they were paying for wine which they then stored and offered for sale, even if it was from a poor vintage;

> ‘when we don't have the demand we have to handle the stock for ourselves, so that's the reason why this is a risky business, really’ (Tapie, 2007).

Négociants that decline some or all of such a vintage may well be ignored by the Châteaux next vintage;

> ‘we [négociants] are really an investor because we have to buy. Because if we don't buy...we do not secure a position for the next vintage’ (Tapie, 2007).

Fortunes were made by speculators buying vintages in the mid nineteenth century and again in the 1960’s and 1970’s, but the 1997 campaign showed the risk taken by négociants as they were left with wine worth far less in the market place than they had paid for it (Claridge, 2010).

The en primeur system gives producers immediate income - and Châteaux enjoy having a guaranteed market for their wines in poorer vintages (Styles, 2008) and can reassure potential customers that they had got the earliest and best possible price from their négociant who in turn had got the best and earliest price from the producer. This way it was possible for négociants to make a profit if the wine was bought early and demand for it subsequently increased beyond the normal 10% - 15% fee that they would take from any deal to wholesalers, importers or retailers.

The 1855 classification of Bordeaux châteaux was based on the market value of each château’s wine and the en primeur system ensured that négociants and brokers would clamour to purchase as early as possible (provided the vintage was reasonable and quality promising) long before the wine was even released, in order to get the best price, relying on the knowledge that there would never be enough wine to go round from the key châteaux to meet future market demand. The 1855 classification meant that each château had a geographic limitation and production was thus finite so creating scarcity and fuelling demand. Châteaux en primeur sales might be successful provided;

*The château was one of some fifty or so that could stimulate market interest and sell largely on reputation.

*The wine at barrel tasting had to suggest sufficient quality and inherent promise to satisfy future customers.

* Brokers and négociants had to predict potential profit based on the Château's release price.

*There had to be potential customers willing to pay.

There has been little change to the en primeur system for more than 150 years. It still requires going through a retailer / wholesaler who goes through an agent / négociant (often the same) who buys from a courtier / broker, to purchase wines on release.

The en primeur system has worked so well for some châteaux that today most wait for the judgement of the market, in particular notable critics, before setting their release price – often basing that price not on costs but on quality appraisals and an estimate of what the market can withstand (Losh, 2007). Further, many châteaux release in a series of tranches, or batches, designed to fuel demand and consequently increase prices each time. Those who hesitate to pay what might appear to be an expensive release price find more times than not that the second or third 'tranche' will make the first release a bargain. For example, the 2000 Château Latour was €175 (R1,750) a bottle on release, €273 (R2,730) on second tranche one year later and €455 (R4,550) on its third tranche; an increase of nearly 150%. Even buying at third tranche looks appealing now, as recently (March 2011) Latour 2000 sold at Sotheby's London auction for more than £1,000 (R11,000) a bottle. A successful vintage – and en primeur campaign - such as 2005, can increase demand for earlier vintages, such as 2000, whose prices may look more reasonable in comparison.

The income of a winery such as Château Latour from its Grand Vin and its second wine, Les Forts de Latour, with an average annual production of 18,000 cases of the Grand Vin and 11,000 cases of Les Forts and at release prices of €5,400 (R54,000) and €1,068 (R10,680) respectively in 2009, before costs, was around €108,978,000 or R1,198,758,000. Actual income was probably higher than this, because this assumes all wine was sold on release, whereas much of the stock was held back for second and third tranches, where the price had risen to well over €7,800 (R78,000) for the Grand Vin. Attempts by South African wineries to establish an en primeur system is discussed in Chapter 8.

Chapter 3 Investment growth

3.1 The growth of investment in wine

It was inevitable that the potential profits realised by successful wine investment should attract not just the collector or connoisseur but also the financial speculator. In difficult economic times traditional investment methods, via stocks, bonds or commodities offer most volatility and often suffer most. Many traditional financial investors are looking at wine as means of diversifying their portfolios. Burton and Jacobson (2001) argue that returns on wines are higher than for other collectibles and match those of stocks. Evidence recently has shown wine investments going beyond the returns from stocks. Investment companies such as Sanlam recognise the potential of wine investment;

> 'The fact that the performance of wine is uncorrelated to stocks and bonds has made investing in it all the more popular. Pundits put the correlation between fine wine and equities at around 0.03 – which essentially means there's no correlation at all. That is good news, as markets remain in volatile territory, and interest rates globally stay close to zero – making wine an excellent hedge against your stock portfolio' (Sanlam, 2011).

The more volatile the market or unsteady the economy the greater the tendency to spread portfolio risk, thus making wine investment a viable alternative.

> 'Collecting wine is no longer a privilege of just the super wealthy now that special investment funds have sprouted amid a search for alternative assets to traditional stocks and bonds' (Reuters, 2010).

With Asia showing such interest in wine, as a trading commodity and as a lifestyle marque there has been tremendous growth in the West as investors eye up potential profits via the East. Asian investment has been considerable, often as instant portfolios are purchased for tens of thousands of dollars. New markets are still emerging; Brazil and India could provide the next growth spurt as their growing middle class seek ways to make their money work for them.

There is also another advantage in wine investment, one with a long tradition in clubs, Universities and corporations and now growing in popularity amongst individuals. Buying more than is required and selling the excess for a profit in the future enables one to acquire a cellar of great wines at a smaller – if any – outlay. With the right wines over a period of time one could almost create a 'free' cellar. For example, buying 12 bottles of en primeur Château Latour 2000 at €250 (R2,500) each (total R30,000) in 2001 and selling 4 bottles at auction in 2010 for €876 (R8,766) each (Decanter, 2011), would realise €3,156 (R31,560 after seller's premium) giving the owner not only all of his money back with €156 (R1,560) profit but also eight bottles of Latour to drink for free.

3.2 The 2008-present economic recession

The economic recession of 2008-present resulted in poor performance ratios in all areas, including previously high returning equity plans, pensions, stocks and shares. Even the property market entered negative growth in much of Europe. But wine prices remained steady (see Table 1). Stephen Williams of The Antique Wine Company (2011) sums it up;

> 'For most of 2008, the fine wine market managed to remain immune to the wider financial crisis. But then after Lehman Brothers, the 'dash for cash' changed everything. Whilst most wine enthusiasts held on to their cellar, nervous investors started taking profits, restaurants sold wine to raise money and a number of fine wine funds began deleveraging. With so much stock coming onto the market…. prices inevitably fell.'

Prices and demand for wine did fall, but blue chip wines weathered the storm. Perhaps the most compelling argument for wine investment came in the middle of the difficult 2008 trading environment. The 1982 Château Lafleur from Pomerol, not one of the top ranked wines, was sold on opening at €109 (R1,090) a case in 1983. In 2008 it was selling at auction for a remarkable €30,800 (R308,000) a case; a growth of some €1,230 (R12,300) or 1,000% every year. Compare that with how gold has suffered through the recession – in 1983 it sold for \$450 (R3,150) an ounce, today for \$1,419 (R9,933) an ounce in Europe (March 2011) a growth of only 10% per annum. There are many other examples of astounding price increases for individual wines during this difficult economic period. In 2006 1982 Château Lafite sold for €5,500 (R55,000). With the recession effects still reverberating around the world, a case sold recently for €43,000 (R430,000); including commission, an increase of R75,000 a year (Sothebys, 2011). The '82 Lafite is a remarkable investment, estimated at being worth eight times its weight in silver (Schmitt, 2010). One does not need to wait 15 years to see spectacular growth, however. A specialist trading platform – the London International Vintners Exchange, or Liv-ex, was established in London in 1999 to track such growth. Recent data showed the 2008 vintage of Lafite went from €3,300 (R33,000) to €11,100 (R111,000) in a single year – and that was before it was even bottled (Liv-ex, 2010a).

The massive cash input into wine investment from the Asian market, particularly the Chinese, over the last few years has helped keep wine as a commodity buoyant and attractive. The Acker, Merrall & Condit March 2011 auction in Hong Kong, for example, saw one case of Jayer's Richebourg 1978 sell for HK$1,647,000 (R1.4m or R123,173 a bottle). The millions of dollars traded has ensured the continued respectability and desirability of the product as well as keeping returns healthy. It also, according to Johann Krige, "bailed out the Bordeaux system and saved en primeur from collapse" (Krige, 2011 Appendix E). The recovery has been rapid and impressive; Zachy's Wine Auctions raised more than $9m (R65m) in their very first auction of 2011 in Hong Kong (Zachy's, 2011).

Williams concludes with a view of the 'strong global demand' shown since 2010;

> 'Anyone brave enough to buy has picked up some great fine wine parcels at very advantageous prices. Equally, for new investors looking to get into the game, the last few months have been a golden opportunity' (Williams, 2011).

Williams' company issued the following data (Table 1) to show how investment in wine had ridden out the recession. Data shows their top 50, 100 and 500 wines' performance against standard asset exchanges. The top 50 wines ended 2010 with good returns (Yield To Date) showing a *sevenfold points increase over the UK stock exchange* (AWC, 2011).

	Value	M/M %	Y/Y %	YTD %
Live-ex Fine Wine 50 (GBP)	401	+2.6	+56.6	+52.5
Live-ex Fine Wine 100 (GBP)	336	+2.1	+40.6	+36.6
Live-ex Fine Wine 500 (GBP)	257	+3.6	+19.5	+19.0
FTSE 100 (GBP)	5,900	+6.7	+9.0	+7.3
S&P 500 (USD)	1,258	+6.5	+12.8	+11.0
Nikkei 225 (JPY)	10,229	+2.9	-3.0	-3.0
Gold (GBP)	910	+6.2	+33.8	+31.0

The Antique Wine Company Newsletter, January 2011 M/M month on month; Y/Y year on year

Table 1. Key Investment Data – Ending 31st December 2010. © AWCompany (Liv-ex 2010)

Alternatively, Liv-ex issues a simple, monthly updated report (Table 2) which shows how fine wine has performed against key measures. The disasters in Japan in April 2011 are reflected in the Nikkei levels, and there is clear identification of the remarkable success of wine as an asset when held against, for example, the UK interest rate of 0.5% (May 2011).

Hence the growth of dozens of investment firms in Europe, the US and increasingly in Asia now offering clients' portfolios of wines to buy into, most offering professional storage facilities for client's wines and a brokerage service. Huge storage facilities exist on most continents merely to hold stocks of wine under perfect long term conditions with ownership

Cellar/Index	Value Index	3month change %	12month change %
Liv-ex 100 (top100performers)	359	+3.7	+26.5
Liv-ex 500 (top 500 performers)	276	+5.8	+23.0
FTSE 100	5,977	-0.1	+3.7
S&P 500	1,340	+5.4	+13.3
Nikkei 225	9,859	-6.3	-12.7

Table 2. Liv-ex May 2011 report showing wine asset progress against other markets. ©Liv-ex

often traded 'on paper' without leaving the premises, such as the London City Bond (LCB). Most investment companies offer tracking facilities for clients to monitor their wines as well as regular financial market reports. An example of an interim market report is shown in Table 3 below. This gives the performance over a longer period of selections of Liv-ex's portfolios, for example, the Fine Wine 50 would consist of the top 50 performing blue chip wines. Note the static performance of stocks and shares as represented by the FTSE 100 over the difficult last few years.

Indices	Level	MOM %	YTD %	1yr %	5yr %
Liv-ex Fine Wine 50	437	4.4	9.0	60.0	283.1
Liv-ex Fine Wine 100	358	3.3	6.3	41.1	191.9
Liv-ex Claret Chip	445	3.9	7.5	53.0	262.9
Liv-ex Investables	360	3.8	7.7	44.3	202.0
FTSE 100	5,994	2.2	1.6	11.9	3.5
S&P 500	1,327	3.2	5.5	20.2	3.6
Gold	867	4.3	-4.7	18.0	170.1

Table 3. An interim market report from Liv-ex. March 2011. With Month on Month and Year to Date figures

Investment companies offer clients with little or no knowledge of wine or the wine market the opportunity to invest with very little effort. The inexperience of many companies, many of less than 20 years standing, does make investment risky, however, as many investors would prefer to see a long history of successful trading and returns before parting with large sums of money. The Wine Investment Fund, though relatively young itself (2003), has tracked the returns of fine wines over a seven year period shown in Table 4 below, where a much more consistent pattern emerges based on a performance index and where wine appears almost twice as profitable than gold.

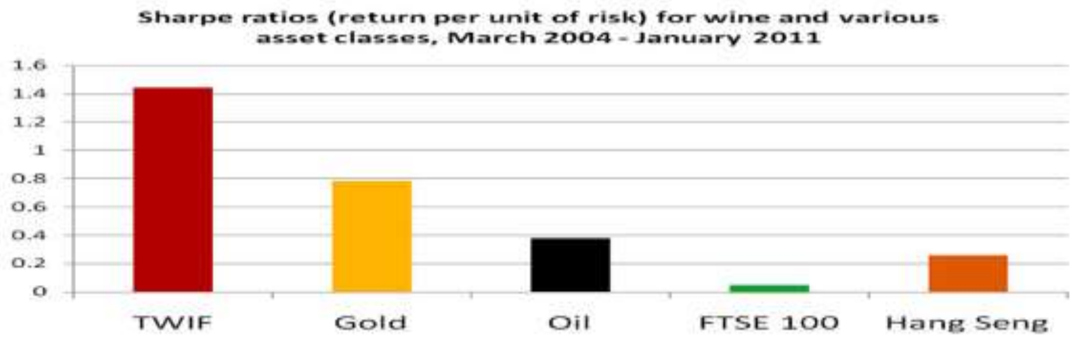

Table 4. The Wine Investment Fund return analysis over 7 years. For every unit of risk, fine wine has returned 1.4 units, Oil 0.4 units

Using the Château Latour 2000 example, an investor selling on his wine in bond (thus avoiding duty but paying brokerage fees) for, say, €350 (R3,500) a bottle – a considerable bargain for most purchasers – would have realised a 100% income return in three years, way beyond the average compound 6-10% many saving institutions could have offered.

Wine	Vintage	RPJ Score (pts)	Market Price (Dec '09)	Market Price (Dec '10)	% Change
Lafite Rothschild	2008	98-100	£2,700	£14,000	418.5
Mouton Rothschild	2008	94-96	£2,700	£8,500	214.8
Carraudes de Lafite	2008	91-93	£1,275	£3,400	166.6
Petit Mouton	2008	89-91	£480	£1,350	181.3
Duhart Milon Rothschild	2006	92	£380	£1,075	182.8

Table 5. www.wineinvestment.org 2010 annual review of selected Châteaux performance and sale prices over a period of 3 years. Note that Asian buyers were influenced by the lucky number 8 appearing on the label and that a Chinese artist designed the Château Mouton label. The RPJ (Robert Parker) scores are discussed later.

Table 5 above shows an even more impressive return for Château Lafite 2008, previously mentioned. All examples pre suppose that the market value is the price the seller can achieve, though, which is not always the case for some wines.

The interest in wine as a lifestyle commodity, with fine wine joining the luxury goods market, and the potential profits on offer, together with greater information available to all via wine journalists and critics has fuelled a secondary industry of its own; one of wine investment where wine has become a traded commodity like pork bellies.

Chapter 4 Investment methods for SA investors

4.1 Types of Wine Investment

Other than buying a wine farm or winery (or even these days shares or ownership of rows of vines) which are not part of the remit for this report, investment in wine consists of buying the finished – or near finished – product and selling on for a profit. There are two main ways of doing this;

1 Buying and trading by yourself.

Here the investor completes all parts of the chain himself. Wine is purchased either;

a) En primeur - not from the Château in the case of Bordeaux, but through an agent / négociant and ships and trades himself.
b) Wines from elsewhere eg Italy or Spain purchased after release if available from the producer, stored and sold on from Europe.
c) Wines from elsewhere eg Italy or Spain purchased after release if available from the producer and shipped to SA, stored and traded.

2 Buying through a third party

d) Through a wine broker / retailer such as 'The Reciprocal Wine Trading Co. (Pty) Ltd.', 'The International Wine Company', 'Winecellar' or 'Caroline's Fine Wines', four established SA dealers offering retail and investment opportunities.
e) Through an Investment Company that includes wine as an asset.
f) Through a secondary trading house, such as an auction house.
g) Through an on-line auction house.

The difficulty, costs and potential profit from these methods varies. Consider each in turn;

1a) *En Primeur, through an agent / merchant, ships and trades privately*. The investor pays the price set by the agent / négociant in Europe who has added their fees to the release price. The investor gets a price only 10% - 15% above the release price but the likelihood of getting an allocation, unless you are a very rich client with a proven track record of not only paying on time but of taking everything put aside for you, is very slim. **Consider that the total allocation of Domaine de la Romanée-Conti for the whole of South Africa's wine trade in 2010 was just 4 bottles** (Peens, 2011 Appendix F). Most agents / négociants don't deal with the public, only with trade houses, corporations, the on-trade or wholesalers. Establishing yourself as a valuable customer will take some time and a lot of money – and you would be expected to purchase weaker vintages which will affect your future returns.

Then the investor either has to leave the wine abroad and pay for storage or pay shipping costs and on arrival in SA pay Duty and VAT, then delivery if required.

NB All examples calculated as per notes under 'Scope of Assignment'

prices converted to Rand for ease of comparison

Château Mouton-Rothschild 2009

Wine on release	R3,333 per bottle
Purchase price inc nég fees etc	R3,600

The investor might then ship to SA and pay Duty and VAT at 14%;

Shipping / Duty / insurance costs	R30–R50 per bottle
Landing costs in SA	R40
VAT which cannot be reclaimed unless VAT registered	R6,100

NB. Assuming the total is fewer than 20 cases to avoid Import Duties, or Duties can be avoided with wines traded in bond via application of form EUR1 (R275 application fee) This is an 'Import Exemption Certificate' from the department of Agriculture.

Also, the allowance of 20 cases of wine 'for personal consumption' under duties regulations – which might be restrictive for the serious investor – can be exceeded if permission is sought from the Department of Agriculture upon payment of R19 per litre. An additional R171 per case above the allowance might be an important charge to consider when estimating potential returns.

Thus 1 case delivered to investor in SA R4,150 per bottle / R49,820 p case

Some 14% more than the initial purchase price

Or the investor might sell the wine without storing or importing it; either finding a buyer himself or through the agent;

Thus 1 case brokered personally or by agent abroad (inc short term storage, broker fee c10-15%, deeds of ownership etc) R3,900 / R4,480 (if brokered) per bottle / R46,800 / R53,820 (if brokered) per case

Some 10%- 22% more than the initial purchase price

The difference of some R200 – R300 per bottle for these two methods has to be weighed against the complexities of both these methods which require a trusting relationship with the agents or a thorough working knowledge of importation and shipping requirements. Both involve regular contact, lots of paperwork and are subject to human failings and natural disaster. Still, after all costs are considered it does mean owning a case of 2009 Mouton for under R50,000 which when compared with today's (Feb 2011) price at SA retailor 'Wine Cellar' of R84,970 in bond looks a healthy return over one year. Of course, the investor would have to sell the wine to realise any profit and other than **requiring a licence** to do so (or trade through the broker) could not guarantee achieving such a price.

1b) *Buying wine already in bottle and selling from Europe*. Provided the wines are available – and the whole point of investment wines is that they are not easily available – the investor purchases then arranges storage with the agent or at a professional storage facility, such as London City Bond. As with selling en primeur abroad the investor avoids duties, VAT and shipping costs, but incurs storage and broker fees unless he brokers deals himself.

Wine on release in bottle eg Vega Sicilia Unico 2000	R800 per bottle
Collection / storage / insurance	c R165 p/case p/annum
Broker fee 10% - 15%inc deeds etc (assume 10%)	cR80 per bottle
Thus 1 case bought from winery and stored in EU for 1 year	*R10,740per case/ R895 per bottle*

Some 12% more than the initial purchase price

Fees are often reduced the greater the quantity stored or traded, so economies can be made with bigger purchases.

1c) *Buying wine already in bottle direct from the winery and shipping*. Provided the wines are available, and that the winery will deal with parcelling and shipping or the investor instructs a shipping agent to collect the wines and transport. The costs here involve;

Wine on release in bottle	eg Vega Sicilia Unico 2000	R800 per bottle
Shipping / insurance costs*		R250 per case
Import Duties**		R2,400 per case
Landing costs in SA		R40 per case
VAT on sale of***		R1,300 per case

Collection or Delivery from winery to Port and in SA not included

* reduced with larger orders

** avoidable if fewer than 20 cases total

*** avoidable if sold through Broker in SA (though Broker will adjust fee), or if very small amount, 'personal sale'.

Thus 1 case bought from winery and shipped R840 (no Import Duties or VAT) /R1,132 per bottle(Duties and VAT) R10,080 / R13,590 per case

Some 5% / 40% more than the initial purchase price

The investor requires a licence should he decide to ship and trade in SA in any sizeable quantity and avoiding Import Duties and VAT is unrealistic and probably unethical for any serious investment plan. The 5% charge minimum here is probably in reality unachievable.

2d) *Buying through a retailer or broker* is probably the safest way to trade. Reputations are built on sound buying advice, proven track records and professional relationships. Wine retailers such as 'Wine Cellar,' and 'Caroline's Fine Wines' in Cape Town, 'The Reciprocal Wine Trading Co. (PTY) ltd.' and 'The International Wine Company' in Johannesburg, or e retailer 'Cybercellar' are closely involved with the wine trade and understand the market. They pride themselves on recommending investment wines for clients and understand the risks involved. Investors are still liable to be recommended and sold poorer vintages or less desirable wines, however, as brokers and retailers are still businesses and have to sell what they may have been forced to buy under the allocation system. Honest brokers would inform their clients of realistic market expectations and work closely with clients to achieve satisfactory results for all. The investor could choose to have his wine stored by the broker / retailer either in Europe ('Wine Cellar' has its en primeur stored at LCB in London) or at their facilities in SA or may choose to store it themselves. Trade may also occur through the broker, who will charge around 15% for this service, which would avoid the need for the investor to obtain a licence. Duties may be avoided if traded in bond. Double VAT may be charged on the same wine, though, as it is due on purchase by the investor, then charged by the broker upon trading as the investor is probably not VAT registered so the brokerage is unable to claim VAT back from the investor who is selling through them (Peens, 2011 Appendix F).

Château Mouton Rothschild 2009 en primeur through 'Wine Cellar' Cape Town

Purchase price	R7,081 per bottle / R84,970 per case
NB. Only 3 bottles available – their allocation	
Storage in LCB	R50 per case / per month (trade price)
Storage at 'Wine Cellar' SA	R70 per case / per month
Brokerage fee at 15%	R12,745 per case

Thus 1 case bought through importer, stored 1 year before brokered sale

R8,193 per bottle / R98,314 per case

Some 15% more than the initial purchase price

2e) *Buying through an investment company*. Many large international companies have added fine wine to their considered asset classes and have included wine experts among their staff. The Antique Wine Company (UK) has more than 20,000 high net worth clients in 70 countries. It states its service as;

- 'We provide guidance and advice on building your tailor made wine portfolio. We help a wide variety of clients from all over the world, with differing tastes, budgets and timescales.
- Unrivalled access to the world's finest wines.
- Priority is placed on investing in wines that suit the taste of each client but which are also of premium quality.
- Monitoring and reporting on the performance of your investment portfolio.
- The assistance of a dedicated Client Account Manager on hand to provide expert advice and answer any queries you may have.
- Unrivalled access to a global network of Clients when liquidating part or all of your portfolio.
- No subscription, redemption or performance fees against your portfolio.'

Wine Asset Managers is another UK based company whose mandate is of achieving 'long term double digit annual returns'. Investment companies take most if not all of the decision making off the investor who could request certain wines for their portfolio after advice (a 'tailored portfolio') or could allow the company to make all purchase and sale decisions and thus have little or no say in how funds are spent or what is traded. Many companies charge around 1.5% a year for their services, a ‘management charge’, often with an initial ‘subscription fee’ of some 5% and initial investment can be quite high; the Wine Investment Fund, for example, has a minimum investment of £10,000 (R110,000) and £500,000 (R5.5million) for institutional investors. Premier Vintners recommend an initial minimum of £5,000 (R55,000). In addition, some funds charge a ‘performance fee’ which is deducted from any profits realised on the maturation of the fund’s term, which is usually 5 years. Luxembourg based company ‘Wine Growth Fund’ has a minimum entry purchase of R1.2m, an annual management fee of 2.5% and a performance fee. The Wine Investment Fund charges 20% on returns realised.

Using the Wine Investment Fund figures, it is possible to assess the returns on a typical investment, achieving say, 10% p.a., again converted to Rand for ease of comparison;

Initial investment		R110,000	
Minus subscription fee 5%		R5,500	
Amount invested year 1		R104,500	
Year 1 growth (compound 10%)	R113,225	-1.5%management fee	R1,724
Year 2 growth	R122,680	“	R1,867
Year 3 growth	R132,923	“	R2,024
Year 4 growth	R144,023	“	R2,193
Year 5 growth	R156,048	“	R2,376
Investment return year 5	R156,048		
Minus 20% performance fee	R9,209		
Net investment return	R146,839		

Thus, over a 5 year investment at a conservative growth of 10% compound per annum, the investor would pay R24,893 in fees and realise a net profit of some 33% or 6.6% a year.

For a healthier growth of 15% compound per annum (a stated industry average) the investor would pay R34,220 in fees and realise a net profit of some 61% or 12% a year.

The Wine Investment Fund admits, ‘each portfolio needs to generate approximately 1.2% compound growth per month (14.4% per annum) to achieve target net of fees and expenses’.

For the top châteaux, returns have averaged 18%, which would see the investor pay some R42,750 in fees and realise a net profit of 81% or 16.2% a year.

These are solid returns but note that costs paid by the investor over 5 years vary between 22% and 39% of the initial investment and some charges eg management fees, would still be due if the portfolio was not achieving such positive returns.

Many investment companies have exceeded the above figures, some quite spectacularly, at least on paper. Albany Portfolio Management, a partner of Albany Vintners in the UK and only established in 2009, reports that their customers' portfolios appreciated by an average of 58.9% in 2010, based on Liv-ex price reports. An examination of their 2010 market report shows exceptional price increases for several wines – most noticeably Château Le Pin '01 whose annual compound growth was over 220%. Table 6 shows selected wines from an investment portfolio of some £184,000

Performance data: 12 months March 2009-Feb 2010 (£)							
Wine	From	Opening[1]	Market[2]	%	Months	Monthly	Annualised
		APM Price	Price Now	Change		Growth %	Growth %
						(compound)	(compound)
Ausone 99	Jan '10	3,700	3,772	1.9	2	0.97	12.3
Ausone 08	Jul '09	7,200	7,794	8.3	8	1.00	12.7
Cheval Blanc 00	Nov '09	6,600	8,207	2.4	4	5.60	92.2
Lafite 01	Oct '09	3,800	5,020	32.1	5	5.73	95.1
Lafite 04	Nov '09	3,850	4,984	29.5	4	6.67	117.0
Lafite 08	Jun '09	3,250	5,390	65.8	9	5.78	96.3
Latour 96	Mar '09	5,000	6,030	20.6	12	1.57	20.6
Le Pin 00	Aug '09	23,000	26,287	14.3	5	2.71	37.8
Le Pin 01	Nov '09	14,000	20,671	47.6	4	10.23	221.8
Le Pin 04	Aug '09	7,800	14,001	79.5	7	8.72	172.2
Margaux 90	Nov '09	7,700	9,208	19.6	4	4.57	71.0
Mouton 08	Aug '09	1,850	2,641	42.8	7	5.22	84.1
Petrus 08	Sep '09	18,000	21,840	21.3	6	3.28	47.3

[1] excludes management fee

[2] average prices reported on liv-ex

Table 6. Albany Portfolio Management 2010 price and growth review of selected wines

(just over R2m) of some two dozen wines (not all shown) showing an increase of 56.8% in prices over the year. Of course, this does not mean a return of 56.8% for the investor as costs have to be deducted and the wine has to be sold to realise income.

Investment companies see wines as offering various risk levels. First Growth Bordeaux would be lowest risk; top Burgundy, Champagne and Old World classics such as Sassicaia and Vega Sicilia of medium risk and New World California and Australia, such as Screaming Eagle, Harlan and Penfold's Grange as high risk. Their investment would reflect this and be part of their risk-return analysis.

Wine does not typically suit a risk-return analysis, though, as it can be drunk and enjoyed (but at the same time destroyed) and is a 'wasting chattel'. This is why wine does not attract Capital Gains Tax in the UK as its ageing implies its ultimate demise. The investor would expect frequent trading by the investment fund to avoid owning wines past their useful life and of little value. Such constant monitoring of portfolios takes a good deal of knowledge and effort from the investor and is an important consideration in weighing return values. Investment companies will also be able to source rare wines more easily than the individual could because of their increased spending power and access to the market. Nonetheless, investment companies might not offer the market buffer expected;

> 'We advise against entering the wine market through investment funds. Such funds have large positions in highly illiquid assets. As such, if they had to get out of the market and to sell their positions quickly, they might incur large losses' (Masset and Henderson, 2009).

2f) *Buying and trading through the secondary trade such as auction houses*. There are numerous auction houses offering wine sales throughout Europe, the US and Asia. Sotheby's worldwide totalled sales of $45m (R317m) in 2008 and Christie's, also worldwide, totalled sales of $70m (R495m) in 2010. Buying through an auction house means bidding on wines which have already attracted tranche fees, broker's fees, négociant's fees and the premium paid by the seller when they purchased the wine.

The wine is put on sale with a guideline price – usually based on Liv-ex's Mid Price - which reflects its standing in the market and the bidder is unlikely to achieve anything near its release price. An example of a catalogue entry from a past sale at Sotheby's is shown in Figure 1 below. Note the brief provenance assurance, the guideline price and the detailed description of the wine's condition. An explanation of bottle ullage is given in 6.1.6.

Of course, poorer vintages, economic downturns or falling out of fashion can drastically reduce the asking price of wines and canny investors might well acquire wines at ‘bargain’ prices. This requires the investor to have considerable knowledge of the market and of vintages and individual wines and to have the time to attend frequently.

Charges are applied by the auction houses for buyers and sellers. A typical buyer’s premium (the auction house’s costs, insurance and profits) for wine are normally around 15% (Christie’s and Sotheby’s in the UK) of the hammer price. In the USA, France and Hong Kong this becomes 20% (Christie’s) or 21% in New York (Sotheby’s) and 25% in Hong Kong (Sotheby’s). Bonhams (UK) charges 15% on the first £5,500 (R55,000) then 10% on any amount above that, plus 1.5% insurance on the total.

Lots 640-644 LYING IN GREENFORD, MIDDLESEX Offered Duty Paid only

Le Pin 1989 Pomerol

u. bn, (ullage description) label badly damp stained and damaged, appears to have come loose and been applied,fragile and barely attached,bought at Sotheby’s June 1999, lot 485 Dreamy, heady stuff, marrying great fruit with elegance. SS.

640 1 bt (cn) per lot: £700-900 per lot: US$1,100-1,450

Château Pétrus 2001 Pomerol

1 label damp stained and bin damaged, 3 very lightly damp stained, 2 labels each have a very small nick, rest good This was always bound to be a winner, given the quality of Pomerol in this vintage which is increasingly evident with each tasting. Everything is in this – it is a very big wine. Exotic and yet pure, truffley and yet classic, this is beautifully delineated Pétrus and an incredible, and worthy, comparison with the 2000. The rich, thick texture will see it through the decades with supreme ease. SS.

641 9 bts (cn) per lot: £6,800-8,800 per lot: US$11,000-14,000

La Tâche 2001 Domaine de la Romanée Conti Côte de Nuits, Grand Cru

Labels have several very small marks but generally good appearance A sweet, intoxicating nose, full of breed. Overpowering scent, just waiting to be unleashed. Plums and roses. Super-charged flavour of violets and ripe Pinot Noir on the finest of soils. One can almost bite the fruit. Damsons and liquorice finish. In character, more earthy and less piercingly keen than RomanéeConti. Then, at 8 years old, real, intense candied violets on the nose. Almost honied – a first for me in La Tâche. A lovely, rosy muskiness and a certain briariness. Then all the raspberries come out. A total mouthful of raspberry and cherry fruit. Wonderfully vivacious. A Rubens-like aftertaste. So pure and sleek and yet wonderfully exciting and direct. SS. 644 3 bts (cn) per lot: £2,200-3,200 per lot: US$3,400-5,000

Figure 1. An extract from Sotheby’s wine auction catalogue showing guide price, provenance and condition. (Sotheby’s 2011) An explanation of ullage is given in Figure 2.

In addition, buyers will pay Sales Tax on any charges in the USA (around 8%) and VAT on any charges in the UK (20%). Sellers’ premiums are also due, (Acker, Merrall & Condit have no seller's fee) which neither Christie's, Bonham's or Sotheby's make readily available, but can be assumed to be between 2% - 15% (Sotheby's will admit to 2% - 10%).

Thus, a case of Cheval Blanc 2004 purchased in August 2010 at auction in the UK might be;

Hammer price		R31,394	R2,616 per bottle
Buyer's premium	15%	R4,709	
VAT on charges	20%	R941	
Total paid		R37,044	

Thus, 1 case bought at auction in UK *R3,087 per bottle / R37,044 per case*

Some 18% more than the initial hammer price

The investor then has to store and broker in Europe with similar fees to the examples above, or ship to SA and pay shipping costs and duties.

Buying the same wine in New York would be;

Hammer price		R31,394	ie	R2,616 per bottle
Buyer's premium	20%	R6,278		
State Sales Tax	8%	R502		
Total paid		R38,174		

Thus, 1 case bought at auction in New York *R3,181 per bottle / R38,174 per case*

Some 21% more than the initial hammer price

Storage, brokerage and shipping costs are applicable.

It is possible to evaluate why wine auctions around the world, but especially in Hong Kong, have managed to make such huge profits for the auction houses. Consider selling a case of wine through Sotheby's Hong Kong which realises HK$11,100 (R10,000) hammer price. The seller will lose [converted] R1,000 of that as a 'seller's premium'. The buyer will then pay 25% 'buyer's premium' of R2,500, meaning that the auction house has made R3,500 from a R10,000 sale.

Very few wine auctions take place in South Africa and those that do are on a much smaller scale. Boland Auctions in Paarl, for example, have held wine auctions for charities and schools where prices are skewed because people are buying to raise funds. On this basis they are successful and wine lots are usually all sold. Norma

Ratcliffe, though, believes that, ‘there is no way forward for SA wines at auctions’ (Ratcliffe, 2011 Appendix G).

2g) *Buying and trading On-line*. The rise of e-trading has made on-line auctions readily available to investors around the world. Based in the USA, ‘WineBid.com’ has more than 62,000 registered bidders and offers storage and shipping facilities (though not to South Africa). One might assume that the costs of using this service are much lower than traditional auction houses, but ‘WineBid.com’, for example, has a 14% buyer’s premium, 1% insurance premium, similar seller’s premium and adds US Sales Tax to purchases. Then there are storage charges at R72 per case, per month and shipping charges to add and of course charges on arrival in SA if the wine is not traded via the same online auction. Hence, the same case of Cheval Blanc 2004 bought for the same price via ‘WineBid.com’ might cost;

Hammer price		R31,394	R2,616 per bottle
Buyer’s premium	14%	R4,395	
Insurance	1%	R313	
State Sales Tax	8%	R602	
Total paid		R36,704	R3,058 per bottle

Thus, 1 case bought ‘on-line’ in USA *R3,058per bottle / R36,705 per case*

Some 17% more than the initial hammer price

The investor would then pay for storage, adding R864 a year per case, and seller’s fees of 5% - 15% if resold on-line, or shipping / duties costs to SA.

‘Cybercellar.com’ are an SA on-line company that has gone a long way to simplifying costs for the potential investor and has some of the lowest charges in the market. Investors buy the wine from ‘Cybercellar’s’ on-line portfolio, who have added their normal retail mark up in advertised prices. Wines can be stored with them at no extra charge and traded through them at a 10% seller’s premium. This could seriously challenge competitors in the market place, but ‘Cybercellar’ only deals with South African wines which, still, make ‘great returns’ for their clients (Phillips, 2011).

Regular dealing, or dealing in larger lots, can bring discounts; ‘AuctionVine.com’ offer a sliding scale of buyer’s fees beginning at a relatively low 12% (with an additional handling fee of R29 per case). It can be seen that the investor pays heavily for his ‘virtual attendance’ at auction, but it does mean being able to purchase wine being sold by a Chinese collector through a New York based website whilst sitting in Pretoria.

With both auction methods there is often a misconception that the investor might be achieving a low priced purchase or that the seller is achieving the best possible price. Auctions can in fact drive up the prices of lots for the buyer and fail to bring expected returns for the seller. In a recent study, Liv-ex found that auction bidders often paid up to 22% over the Liv-ex Mid Price which they might have expected to pay. It also found that sellers often achieved up to 10% less than the Mid Price. Their conclusion was that, even without paying any seller's commission they would realise 10% on their sale by instead selling direct to a London merchant (Liv-ex, 2011b).

4.2 Summary of Investment methods

Today's investment market for wine is truly global, which makes comparing sale prices achieved by brokers or auction houses possible as prices are immediately visible to all anywhere in the world, whether in New York, Hong Kong or Sydney. This also creates some homogeneity in wine prices around the world, though this is contested (Kourtis, Markellos, and Psychoyios, 2010). Since selling wine – through any method above – is dependent on the market at that moment and will realise roughly similar prices anywhere, the main *variable in investment returns* – other than slightly different returns from investment funds through timely buying and selling - *is* ***costs***. Because of this it is possible to compare various investment methods based on the cost of investing.

On a purely cost basis all the methods used above fall within a spread of 10% to 40%. The 'cheapest' methods appears to be buying en primeur or bottled from the Château's broker and trading in Europe or buying through a broker in SA and storing and trading through them. Very simply and assuming the figures quoted, a comparison of costs (as a proportion of the initial investment) would look;

1a) buying en primeur in Europe and trading / shipping yourself or brokering in Europe.

Between 10% and 20%, with an average of **14%.**

1b) buying bottled from the producer, storing and trading in Europe yourself or via broker.

Between 10% and 14%, with an average of **12%.**

1c) buying bottled from the producer and shipping to SA to trade.

Between 5% and **40%** (see notes under 1c).

2d) buying through an SA importer / retailer. Around **15%.**

2e) buying through an investment company. Between **22%** and **39%.**

2f) buying through an auction house in Europe / US / Asia.

Between **18%** and **21%,** but this excludes storage abroad, transport to and from auctions etc or shipping to SA.

2g) buying through an on-line auction house. Around **17%.**

This comparison of costs does not imply that the cheapest method is best, much will depend upon potential profit levels; costs of 39% are acceptable if profits achieve 60%, for example. There are other considerations when making comparisons;

a) Length of investment

Average returns quoted by the industry are 15% per annum. Several investment methods above have end costs around 15% of the investment, there would appear a good chance of making little or no profit within the first year or two. The investor is gambling upon a rising market with their asset achieving exponentially higher growth. A key factor in this is time; the investor may need to hold the asset several years before any real growth is made, depending upon how much was paid for the wine and what costs will be incurred. Wine does not appear to be a commodity with a fast return.

b) Bigger purchases can reduce costs

Economies of scale are available. Larger purchases and larger lots traded can bring reduced costs where brokers, investment companies, storage facilities, shippers and auction houses offer reduced rates with higher volumes. Similarly, investment companies will enjoy better economies of scale than single investors and thus show better returns, going some way to offsetting their charges.

c) Achieving market price

All methods are dependent upon the seller, broker or investment company achieving the top market price for their wines which cannot be guaranteed at auction or in a volatile economy. The over-paying and under-returning prices achieved through auction, often, are important considerations when comparing costs and returns of all methods of investment.

d) Knowledge of the market

All the methods of investment other than through recommendations of a broker or handing over control to an investment fund require the investor to have knowledge of wines and the wine market and a good deal of time to devote to investing. As Phillippe Masset and Caroline Henderson said;

> ‘One should only invest in wines if one has a real interest in wines. This is because such an investment requires having a very good knowledge of this complex market,

which does not function the same way other financial markets do' (Masset and Henderson, 2009).

Ultimately, the choice may depend on how much control the investor wants to have over decision making, how much time and knowledge of the market the investor has and how high a proportion of profits he will sacrifice as fees. It depends on whether the investor is prepared to deal directly with foreign merchants, to organise contracts and payments with overseas wineries, storage depots, transport businesses, foreign brokerages or auction houses. It also depends on whether the investor wants to see and feel his investment, as methods which see wine stored abroad, only traded on paper or with an investment fund will mean never actually realising the joy of holding a bottle of something very special.

Chapter 5 Investment trends

5.1 New trading hubs

Huge demand in the USA and more recently in Asia has created a trading market worth more than $3bn (R21bn) a year (Wasserman, 2010; Miles, 2009). Asia was quick to see the market potential. Its own wine consumption is estimated to grow by 25% in the next five years and according to Vinexpo. China will be the biggest producer in the world by 2050. Not only will China be amongst the top producers, but the rapid increase in its relatively wealthy middle class, growing by some millions every year, who view wine collecting much like owning a Louis Vuitton handbag, is a promising sign for wine investors. The Asian imported wine and spirits market is already worth some $7bn (R49bn) a year, with imported brands – particularly Bordeaux – increasing in share. By 2017 wine imports alone will be worth $1.4bn (Kevany, 2011). A tacit recognition of Asia's growing international influence was made by Vinexpo, who moved their exhibition to Hong Kong. Within two years of abolishing a 40% tax (Sales Tax and also Duty Allowance) on wine, Hong Kong became the wine trading hub of the world, trading more in its auctions than London and New York combined. Indeed, despite recovering from recession, Hong Kong raised HK$195m (R173m) in the first three sales of 2011 (Liv-ex, 2011a). Asian influence and buying power is substantial and worldwide; of the £1.9m (R21m) raised in Christie's June 2010 auction in London, 50% went to Asian buyers. Other growth markets include India and Brazil.

5.2 'Parkerisation'

There is no doubt that wine speculators have relied heavily on the evaluations of Robert Parker Jr before making an investment in wine and that this has both increased his influence worldwide and hugely increased the prices and status of particular wines. Dan Hyde on 'ThisisMoney.co.za April 2010 says;

> 'Parker gives wines a score out of 100. Anything bearing a Parker score of 90-plus is likely to be an investment worth considering'.

An analysis of wines scored at 100 by Parker as investment propositions over 20 years show an accumulated return of 249%, or 12% annually, thus outperforming the Dow Jones index over the same period.

Conversely, a poor rating by Parker has had a similarly profound effect on any wine. Bordeaux has even withheld its release prices of wines until Parker has made judgement upon them. This phenomenon has probably not suited many Châteaux, whose wine was previously traded on reputation and vintage alone and is now dependent upon an American palate.

Despite Parker's many critics, there is no doubting his influence on the desirability and price of the very top wines. An investor would be foolish to ignore his assessments. As Provenance Fine Wines say;

> 'It really is impossible to underplay the significance and influence of Parker on the world of fine wine investment' (Provenancefinewines, 2011).

Emile den Dulk of De Toren's doesn't resent Parker's influence and has invited his SA contributor (see 8.2.4) to taste his wines in barrel. Den Dulk believes in positively promoting his wines on the world stage and Parker is a way to do this (den Dulk, 2011 Appendix A).

5.3 Corporate and On-Trade buyers

The secondary trade market has always been dominated by trade buyers, whether merchants or importers, but in the late twentieth century others began to enter the market. Perhaps the biggest buyers are the financial houses buying for their investment fund clients. There are also large, often international businesses who accept the asset potential of wine and invest capital as they would if buying stocks or shares, just as the owners of one of the greatest art collections in existence is a Japanese Insurance company.

Now too, but not in SA, the on-trade often purchase their restaurant or hotel wines at auction or direct from importer and eliminate the costs of going through third parties. Today, many of the bidders at auction are there on behalf of their establishment and many have large budgets to spend. The presence of so many corporate buyers has caused some friction with individual buyers who feel squeezed out of the market and unless they have the wealth of

Andrew Lloyd Webber who recently sold only ‘some’ of his collection (8,800 bottles) of wines for £3.5m (R38m) often feel that they cannot compete with the deep pockets of businesses. SA Wine Magazine ran a series of correspondence between disgruntled buyers and Alan Pick of one of SA’s biggest trade buyers, ‘The Butcher Shop & Grill’. Pick called the public who acquire small volume lots at the Cape Winemakers Guild auction ‘rats and mice’ and an inconvenience to the commercial buyer. This elicited passionate responses from readers who felt not only slighted but worried that such attitudes would make individual bidders even more obsolete (Wine Magazine, 2007).

Chapter 6 Investment risks

6.1 Investment risks / Caveat Emptor

There are a number of considerations an investor in fine wines should be aware of.

6.1.1 Buying En Primeur

The advantages of buying en primeur include;

1) Securing top wines from good vintages.
2) Having your wine in uncommon formats such as halves or magnums if requested.
3) Obtaining the earliest and usually lowest price.
4) Access to correct storage facilities via retailers.

However, there are other considerations. Négociants are essentially gamblers, not just in making future profit but that the wine will reach them safely and in good condition. Having done the deal it is not unknown (and quite legal) for châteaux to add up to 15% press wine to the cuvée and even up to 15% from a previous vintage. This could significantly change the wine and make future sales, for the négociant and the investor, much less predictable. Secondly, wines bought en primeur might be available cheaper later. It is possible that in a falling market or after negative reviews the same wine will appear on retail shelves at a price lower than the en primeur price. Thirdly, much can happen between purchase and the investor’s storage facility; the négociant could become insolvent or renege on the deal, natural disasters could destroy or affect the wine in barrel or en route, such as the tragic roof collapse at the London City Bond storage in December 2010;

> ‘Staff at the warehouse tried to salvage as much stock as possible, but their task was made all the more difficult due to the fact any stock which wasn’t destroyed in the accident was then exposed to potentially damaging sub-zero temperatures’ (Your Thurrock Magazine, 2010).

6.1.2 Securing a release price

Highest profits can really only be achieved if wine is purchased on release and that requires a third – and even fourth – party. According to 'Premier Vintners.co.uk',

> 'For the most part, when dealing with brokers, you have already missed the boat, or at least the first big uplift.'

Each step will see those involved add their costs and profit margins to the deal. Individual investors in Bordeaux cannot purchase wine at the Château's release price, the price is;

The Château's release price

+ *Broker's fee in selling wine to various négociants around 2%*

+ *Négociants fee to various worldwide agents / importers / wholesalers a further 10%-15%*

+ *Agents / importer's fees / Retailer's fees / profit margin around 20% - 40%*

+ *Import Duties / VAT / Delivery*

The release price is the base price and between 30% to 60% added along the chain. Thus, Berry Bros. & Rudd (UK) sold the 2008 Châteaux Margaux at £136 a bottle (R1,500 in bond – see below) though the release price was around €110 (R1,100 a bottle).

6.1.3 In Bond 'hidden costs'

Wine prices in many countries may also be subject to Taxation via Duties and VAT on collection if they are held 'In Bond' by the selling agent, which most are as it reduces their costs (by passing them on to the customer).

In the UK, purchasers will pay Excise Duties of £20.25 per case (more elsewhere in Europe) then VAT at 20% per case. Buying a case in bond of 2005 Château Margaux from Berry Bros & Rudd (UK) will cost £8,800 plus £20 Duty plus £1,760 VAT, with free delivery, making the total £10,580 (R116,380). So what was £290 a bottle on release, immediately became £350 to the customer if bought in 2006 and in 2011 becomes £880 (R9680) per bottle (Berry Bros. & Rudd, 2011).

In South Africa purchasers of the same wine will either buy through a European based company then pay shipping costs, import duty and VAT, or through a SA based importer / retailer such as 'Wine Cellar' who will include those costs in the final invoice. 'Wine Cellar' estimate the customer should add 25% - 30% in Duties and shipping costs to their en primeur offerings, which already include the price they (' Wine Cellar') have had to pay to the selling agent in Europe. For example, 'Wine Cellar' are currently (Feb 2011) offering

2009 en primeur Château Mouton Rothschild in South Africa at R7,081 (€708) per bottle before Duty and VAT for a wine which had a release price of R3,300 (€330). The difference is not just profit margin, storage and import costs, but also négociants / agents fees in Europe and the 'cash hurdle rate' (see below) incurred by 'Wine Cellar' in paying for their wine in 2010 but only selling the wine a year later (hence losing potential interest accrued, some R190 at base rate over the year for one bottle based on price paid by 'Wine Cellar' had this money been invested elsewhere). The increased price also reflects the increased 'value' of the wine built up in the interim stimulated by tranche releases (see 2.2 wine futures) via evaluations, competitions and increased demand. In short, paying for the wine's history.

6.1.4 Vintage dependency

A key factor is vintage; poor vintages deflate prices, demand and potential profit. Most investors would probably not want to invest in poor vintages, yet the allocation system means that often if you don't take your allocation you may forfeit future allocations or at least not get your full choice. This may be more true for négociants, but they buy on behalf of customers and would not be pleased to be left holding unsold wine as was the case for some with the 2007 vintage – a vintage many had also drastically overpaid for off the back of the strong 2005 and 2006 vintages.

A study by Liv-ex of its top performing Châteaux between 2000 and 2007 saw two thirds of wines increase in price between the initial release and being available to buy in bottle.

> 'Unsurprisingly, high-quality vintages - and 2005 in particular - delivered better results than those from lesser years. For the First Growths buying at en primeur almost guarantees investors are getting the best price. For the other châteaux it's not quite as clear cut: only wines from the best vintages (and those lauded by the critics) showed substantial price increases following their initial London release' (Liv-ex report, 2010).

Investment vintages over the last fifty years would include:

Bordeaux; 1961, 1982, 1986, 1989, 1990, 1996, 2000, 2005, 2009, 2010

Burgundy; 1985, 1990, 1995, 1996, 1999, 2002, 2005, 2009

Rhone; 1983, 1985, 1988, 1989, 1990, 1999, 2003, 2005, 2007, 2009

Italy; 1982, 1985, 1990, 1997, 1998, 1999, 2004, 2006, 2009

Spain; 1981, 1982, 1994, 1995, 1996, 2003, 2005, 2009

South Africa 1995, 1997, 2003, 2007, 2009

Other vintages should be considered as the high prices caused by a great vintage makes slightly less good vintages, such as 2001 in Bordeaux, better value. A portfolio with a mix of vintages including a number of top older wines would be sensible.

6.1.5 Return Risk Volatility

Large investment returns from wine cannot be guaranteed. Every investment house with integrity carries very clear 'caveat emptor' warnings. The legally prescribed wording appearing on investment company pages in the UK reads;

'Please note that past performance is no guarantee of future performance, that the value of investments may fall as well as rise and that you may not get back the amount originally invested.'

Wine is a commodity like any other, controlled by market forces and susceptible to economic pressures, vintage conditions and fashion. Risks arise partly because output prices cannot be determined prior to production and can vary widely (Krasker, 1979). This is because producers are vulnerable to the forces mentioned above and because there is some international variation between wine prices and consequently wine's attractiveness as an investment around the globe. In a recent paper it is argued that such price variations, rather than increase investment risk, offer,

> ..'significant international diversification benefits for investors in Italian, Australian and Portuguese fine wines' (Kourtis, Markellos and Psychoyios, 2010).

Kourtis, Markellos and Psychoyios apply several price index ratios and conclude that diversification is vital and that areas outside classic Bordeaux and Burgundy offer the greatest risk protection. It might be surmised that South Africa offers similar wine quality and market potential to the countries studied. Author Apostolos Kourtis agrees that including SA 'seems like a good idea for future extension... it is certainly an interesting direction' (Kourtis, 2011). Diversification in only French wines seems to offer little protection, and since the 'risk profile of wine as an alternative investment remains largely unknown' (Kourtis, Markellos, and Psychoyios, 2010) it seems sensible to include wines from other than traditional regions. Any benefits, however, are largely unproven and the authors warn of the lack of risk-management tools available for wine investment.

Liv-ex has traced the returns made on fine wine since 1982 and though there have been periods of very low or even negative returns such as 1997 and 1999 when profits failed to make the 5% 'cash hurdle rate' (the cost of money over time similar to getting interest from a Savings Society at 5%) overall the progress has been steady. Table 7 tracks this performance based on an index of 100 given to prices achieved by 200 wines deemed the most ‘investible’ when Liv-ex began in 1999. The plateau of the poor performing vintages of ’97 and ’99 and the inflated prices of the successful 2000 Bordeaux vintage can be seen as can the effects of the 2008/9 economic recession.

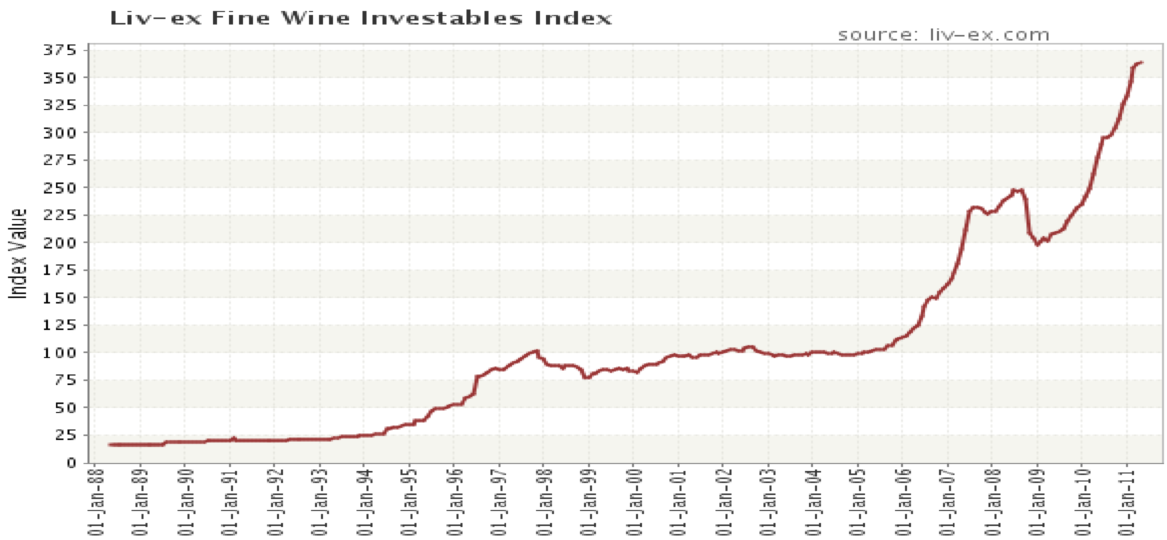

Table 7. Liv-ex tracking of 200 ‘investable’ wines on a 100 point index since 1988. © Liv-ex

Liv-ex concludes that only returns above 15% over time should be considered because of the increasing cost of money and the risks involved and that only 36% of traded wines saw that kind of return over those same years. The Wine Investment Fund estimate that, ‘each portfolio needs to generate approximately 1.2% compound growth per month to achieve target net of fees and expenses’ (see Ch 4, 4.1 2e). However, during a protracted recession of nil or 1% returns commonly achieved in Europe presently and provided the investor buys and trades wisely probably a 10% p.a. return would be attractive. The Liv-ex June 2011 report in Table 8 reflects such volatility, showing no growth at all for their top 50 or top 100 wine portfolios over the month (MOM). Although the figures are less healthy than the March 2011 report shown in Table 3 on page 10, top wines still outperformed stocks. Such figures, not even achieving the stated 1.2% monthly growth needed to cover costs, and only for the best performing wines, when most investors will have a mixed portfolio, must be a concern to potential investors, though performance over the year is still sound.

Low risk investment, despite being the safest, is often the most poorly rewarded. Wine as an asset may not be as obviously high risk as imagined. Fogarty (2006) believes in the

Indices	Level	MOM	YTD	1yr	5yr
Liv-ex Fine Wine 50	439	0.0%	9.4%	31.4%	240.6%
Liv-ex Fine Wine 100	359	0.0%	6.7%	21.2%	153.8%
FTSE 100	5,990	-1.3%	1.5%	15.5%	4.6%
S&P 500	1,345	-1.4%	6.9%	23.5%	5.9%
Gold	934	0.2%	2.6%	11.6%	173.1%

Table 8. Liv-ex June 2011 market report showing no monthly growth of top portfolios.

role of wine assets in diversifying risk, 'even if the return to wine is lower than standard financial assets and the risk higher, if including wine in an investment portfolio reduces portfolio risk, wine should be considered a worthwhile investment class' (Fogarty, 2006).

The relatively high interest rates on savings offered in South Africa, anywhere between 4% and 6% currently on quick access accounts and anything up to 9% on longer term accounts, bonds or Managed Funds (March 2011) means that investors don't have to take risks to achieve satisfactory returns. The blog page of Boschendal Estate's web site sums it up thus;

> 'SA also has other relative safer investments with decent ROI's like government bonds, interest on positive accounts and money market investments. These lower risk investments also make it more viable for investors to go for the safer investment options' (Boschendal blogmaster, 2009).

This might explain why investment in an alternative asset like wine is more active in Europe and the US where returns on savings are currently much lower, around 0.5% net on most Building Society savings accounts in the UK for example. If similar rates were offered in SA the pursuit of alternative, high risk (high return) investments might be much more in evidence.

With such low everyday saving rates and the worldwide severe recession starting in 2008 fine wine achieved a 5.6% return according to Bordeaux Index (Annual Report 2010), making wine investment an attractive option in Europe. The bounce back in 2010 was remarkable; by December, the Bordeaux Index had returned 32.4% on the year making it by some way the best performing asset class of 2010. Stephen Williams of The Antique Wine Company explains why,

> 'In tough and challenging economic times, money flows into wine because unlike paper assets, investors regard it as safe haven. Rather like gold, wine is a tangible commodity which has historically shown good solid returns through thick and thin. Because of this demand remains solid and cushions the lack of consumption.
> The result is that, even in the severest of downturns, wine doesn't crash in the way

that stocks and shares do. Fine wine prices may plateau and even dip occasionally, but not for very long before they come back up again' (Williams, 2010).

Williams' words seem justified with the announcement that Bordeaux 2010 is another superb vintage, with en primeur prices expected to rise by 15% - 30% (Lechmere, 2011). First Growth Bordeaux are likely to be €500 (R5000) per bottle on release (Spurrier, 2011) and despite market warnings of a weakened US and Asian economy and some buyer unrest with another price rise, sales are going to be rapid and 'tres sportif' ('very competitive', Von Neipperg, 2011).

Nonetheless, investment in wine is subject to market volatility. Being a 'wasting product' ie one with a finite lifetime, most wines rarely achieve long term investment of, say, ten years or more as most will have deteriorated beyond their drinking life. Investors trading themselves will need to beware of holding wines too long. A reasonable investment term, according to Stephen Williams, is 10 to 15 years, much can happen in that time.

6.1.6 Fraud

There has always been the temptation for fraud in the wine world as some wines are literally worth more than their weight in gold – the foremost traded commodity. A bottle of 1869 Château Lafite sold by Christie's in Hong Kong in November 2010 achieved $232,000 (R1.67m), with gold listed at $45,516 or R318,615 per kilo, the Lafite was worth 5 kilos of gold (March 2011). Unlike gold though, it is difficult to verify wine as genuine, making it vulnerable to fraud. The wealth being injected into the wine market from Asia has made counterfeiting a huge problem. Gregory De'eb, general manager of Hong Kong Crown Wine Cellars says, 'It's not a new problem -- in Europe it's been going on for more than 130 years'.

Buying en primeur presents its own problems. 'The biggest risk for consumers is the lack of regulation in the en primeur system which encourages unscrupulous companies to take advantage of customers' (Isark, 2001). The problem revolves around the fact that when you buy en primeur you buy the intention to own the wine in bottle, not the actual wine, so if a problem occurs after your payment but before you take possession then you could be left without the wine or your money and face a difficult task in convincing an insurance company to cover the loss as you didn't actually have possession of the wine. It might be possible to get your payment returned depending on the method of payment used, otherwise the only recourse is to the courts. Failed businesses may have no capital to return any or all money deposited with them and any wine, even in your name, would be sold to pay debtors who may be legally more deserving than holders of wine in bond, such as Customs, Tax and service providers.

Recent estimates have put the proportion of fake wines on the Asian market at 5% of the total; a staggering $70m (R5bn) a year of a $13.7bn (R100bn) total (Shadbolt, 2011). The most common deceptions in Asia are replacing the wine originally sold in the bottle with a cheaper wine and faking bottle labels.

> ‘Sometimes it's as subtle as putting, say, a Château Lafite '85 -- which is quite a lot cheaper -- into a Château Lafite '82 bottle. And at the other end, there was a very big bust by Hong Kong customs of a consignment of Mouton Cadet, which is not the most expensive wine on Earth, but someone had gone to the trouble of counterfeiting it’ (Tam, 2010).

In 2001, 30 bottles of 1982 Chateau Mouton-Rothschild sold in a Hong Kong auction for HK$5000 (R4680) each were found to contain wine that was retailing for HK$160 (R150), (Independent on Sunday, 2011).

With this in mind, fine wine empty bottles are highly desirable. There are web sites and companies blatantly advertising to buy pristine empty bottles, with Château Lafite the favourite. With a 1982 Château Mouton-Rothschild fetching $6,071 (R42,500) a bottle at auction in China it is unsurprising that to a criminal the empty bottle is selling for $1,500 (R10,800). Faking bottle labels is now big business and some businesses are going further;

> ‘I was sent a sample bottle of fake Lafite and it looked like the real thing. They'll often ask you to visit their facilities where they are making the whole product -- right down to the wooden boxes’ (Walker, 2010).

Counterfeiting is now spreading to other wines in Asia. Supermarkets all over China saw bottles of popular Australian brand Penfolds on the shelves with their highly recognisable branded label, only this time the typeface read ‘Benfolds’ (Lightstone, 2010).

Blatant attempts to defraud have included selling wine under false labels or with false descriptions, such as the 2009 ‘Red Bicyclette’ scandal where 12 people were sentenced in France for selling inferior grapes as Pinot Noir to E & J Gallo in the US and making €6.6m (R66m) in profit, or the discovery of 400,000 bottles of ‘Mont Tauch’ Fitou in China which had never been near France but had originated in South America (Macle and Fish, 2010).

For wine investment, provenance is everything, an area which has opened up many more opportunities to lose money to criminals.

In 2008 three people were found guilty of defrauding American investors of over $1.7m (R11m) by buying wines that had no investment value and by ‘selling’ wines to investors that they hadn't bought and had no intention of buying (Doward, 2008). The three directors of Vintage Wines of St Albans received prison sentences in the UK. One investor lost more than $500,000 (R3.5m).

In early 2010 it was noticed that top Bordeaux wines from the 2009 vintage were being traded (on paper) before the Châteaux had declared their release price. Investors in China were targeted by criminals offering wine parcels at bargain prices and often fraudulently taking payment for wines that nobody had the right to sell, or even owned, at that time (Woodard, 2010).

Since 2010, a new scam has emerged, Lionel Nierop of 'Bid for Wine' writes on Jancis Robinsons' website;

> '… namely hijacking the name of an established business. The fraudsters then use the name to sell wines for investment, presumably with the intention of pocketing investors' funds and leaving the legitimate business taking the heat' (JancisRobinson.com, 2010).

In 2011 investment company director Benedict Moruthoane of Templar Vintners Ltd and International Wine Commodities Ltd was jailed for seven and a half years in the UK for taking some £1m (R11m) from investors via the two businesses, neither of which bought any wines to back the investments (Budd, 2011).

Dominic Smith of Mayfair Cellars Ltd., also in the UK, stole wines stored by investors over a period of four years. It brought an otherwise successful business to collapse (Lechmere, 2006).

'Investdrinks.com' warns that,

> 'There have been instances where a 'merchant', faced with an urgent order, has 'borrowed' without the client's permission or knowledge from customer reserves to pay back later' (Investdrinks.com, 2011).

Wines seemingly safely housed in bonded warehouses may not be so secure, even without nature's intervention. Investdrinks.com recommend doing your own checks of 'due diligence' as bankruptcy is not uncommon.

> 'About two years ago there was a case where a small bonded warehouse alleged that a customer's stack of boxes came crashing down breaking all the bottles. Soon after the company went into liquidation and a new company started up. Despite legal action the unfortunate customer has been unable to get compensation' (Investdrinks.com, 2011).

Even with the best intentions, wine trading companies can falter. The largest fine wine trader in the world, Vinfolio in San Francisco, nearly collapsed into bankruptcy leaving wine owners in a very unsure position in 2010 before being rescued in a management buyout. Vinfolio was apparently successful and very popular as a retailer and storage facility for half a million bottles as well as an easy to use trading platform, so clients were shocked when cheques they received for wines sold were not honoured. Vinfolio seems to have recovered and has an active website, but events must have worried investors (Decanter, 2010. Robinson, 2010).

Wine investment attracts two kinds of risk, it seems, at least when using investment funds. Not only the risk of not achieving any real profit, but also the risk of large scale fraud. The nature of investment means that large sums are involved; losses can be similarly large. Consider the now defunct City Vintners Ltd in the UK who bought £8m (R88m) worth of wine on behalf of their 1,450 clients but charged far more than the wine was worth and netted £19m (R209m) profit from them (Investdrinks.com, 2008).

It is clear that any investment with a broker, importer or investment company should be thoroughly investigated before any money is exchanged. The new regulations of the Consumer Protection Act which came into force in SA on 1st April 2011 (CPA 2008) at least offer more protection to the investor, allowing them to demand full disclosure of the price of goods and services, and protection against false, misleading or deceptive representations. Key to investors is the opportunity to terminate a fixed-term contract by giving 20 business days' notice in writing and the shift from 'buyer beware' to 'seller beware' because of the power of redress now given to unhappy customers.

Though there are few real guarantees it makes sense to use established companies and to check them on the Companies register as well as examining their trading records. They should have excellent storage facilities and full insurances at every stage of the process and to visit storage premises, photograph and record as much as possible and keep secure all paperwork, especially receipts of monies paid. A wise investor would check optimum storage conditions such as humidity levels and heating / cooling systems, security and that their stock was identifiable by name or code numbers. They would expect individual stock certificates and auditor's reports of stock value.

The UK's Wine and Spirit Trade Association chief executive Jeremy Beadles says;

‘Bona fida merchants and brokers won’t have any problem proving their credentials, but consumers who ask the right questions will ensure they are not caught out by dubious dealers’ (October 2009).

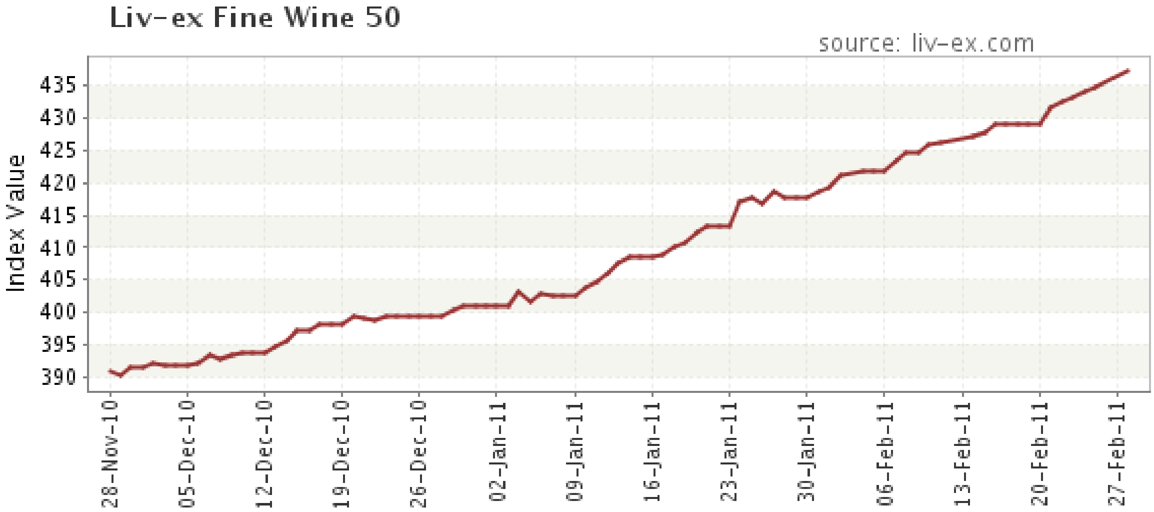

Table 9. Liv-ex top 50 investment wines monthly performance (Liv-ex 2011)

An example of a detailed, monthly performance chart that an investor should expect is shown in Table 9 above. The figures here track Liv-ex’s top 50 wines’ performance on a monthly index basis and give the investor a clear overview of his fund, whatever it may be.

For the individual investor buying, storing and selling his own wine there are essential rules to follow to at least reduce the risk of fraud. When buying from private sales or auctions the provenance and condition of the wine are key. The history of the wine and especially how much it has travelled affect its value; documents and receipts will help. The condition of the wine will tell a story, much can be gleaned from the condition of the label (after establishing it is genuine) and seal. Auction houses should do this prior to sale.

Sotheby’s provides a guide to each bottle’s condition and pays attention to losses in bottle – or ullage. An example is shown in Figure 2. Correct storage will be discussed below.

Sanlam SA give advice to their investors which ends, ‘a word of warning, though – the wine market is still mostly unregulated, and fraudsters have preyed on eager wine investors’ (Sanlam, 2010).

An attempt to introduce more regulation, albeit voluntary, to buyers and sellers of investment wines is the introduction of an ‘Investment Code of Practice’ in the UK (Budd, 2011a). With

Ullages (Level of Wine)

For Bordeaux, Port and other wines in bottles with defined shoulders the ullage/level is shown, if relevant, by its relevant position in the bottle. Our interpretations are as follows:

u. - ullage/ullages (levels)

n. - within neck; the normal level of young wines

bn. - bottom neck; completely acceptable for any age of wine

vts. - very top shoulder; completely acceptable for any age of wine

ts. - top shoulder; usual level for wines over 15 years old

hs. - high shoulder; typical reduction through the cork, usually no problem

ms. - mid shoulder; usually some deterioration of the cork and therefore some variation

Example: (u. 3hs) means 3 bottles ullaged to high shoulder.

For Burgundy, German and other wines in bottles with sloping necks the ullage is shown in centimetres, measured from the base of the cork. Example: (u. 2x5cm) means 2 bottles ullaged 5 centimetres.

1 Whilst we do all that is possible to indicate accurately the levels of older wines, such levels may change between cataloguing and sales. This may be caused by the ageing of the cork or by a change in the temperature of the storage conditions or the shipment of the wine.

2 There is a risk of cork failure in old wines which must be taken into account by the potential buyer.

3 Sotheby's will not entertain any price negotiation or credit after the delivery is made and returns will not be accepted.

4 Under no circumstances will substitutes be provided by Sotheby's; for example in the case of breakage, or error of description.

5 Labels may be stained where wines have been stored in damp conditions. It should be noted that such storage conditions are generally beneficial.

Figure 2. Sotheby's description of ageing losses, or bottle ullage, for bidders at auction. The amount of ullage gives a good indication of the health of the wine. Sotheby's 2011

backing from most of the leading merchants, the code offers guidelines for best practice and legitimate behaviour and could form the template for an SA trading practice.

6.2 Limited Trading wines

Fine wine investment doesn't go much beyond top Bordeaux, where supplies from some producers has actually shrunk (caused, often, by the search for improved quality bringing reduced yields) and some Burgundy, Champagne, Rhone and just one or two Italian and Spanish wines and a few Ports. Perhaps 75% of the traded fine wine market is produced by the top Bordeaux châteaux, as Serena Sutcliffe MW says,

> 'The Fine wine trade is absolutely concentrated on the very top French wines' (Correspondence 13/2/11).

New World wines are scarce in the international trading environment, with none included in Decanter Magazine's 'Fine Wine Price Watch' and only a few Californian and Australian wines quoted as investment potentials on most web sites. Langton's Auction House in Australia does considerable business in wine trading, but it tends to be largely domestic. New World wines carry greater risk; 'we would regard New World wines as a passion purchase, rather than financial investments' (Williams, 2010). Anthony Rose confirms,

> 'Outside France, Italy's Sassicaia and Spain's Vega Sicilia command international respect, although cult California and Australia don't quite cut it yet in the mainstream global investment market' (Rose, 2009).

Positive returns are also more a feature of 'high end' wines, mostly Bordeaux first growths and a handful of others. 'More expensive wines achieve larger returns and have lower volatility than less expensive wines' (Fogarty, 2006).

Sotheby's total sales in the US in 2007 showed how limited the market is, with Bordeaux first growths accounting for 37% of the total. When just two other wines are included (Cheval Blanc and Petrus) the total becomes 50%. Evidence of just how limited the fine wine market is can be seen by comparing the auction prices achieved by two traded wines on the Decanter Fine Wine Price Watch (Decanter, 2011). The gulf between Bordeaux First Growths and Medoc Cru Bourgeois, for example, is clear. Table 10 below shows Château Latour (1st Growth) and Château d'Angludet (Cru Bourgeois) both from 1996 and sale price achieved for one case. The Latour shows a growth over 5 years of 317%, the d'Angludet of just 10%, far less than the 'cash hurdle rate' (see 6.1.5).

	June 2006	April 2010	June 2011
Chateau Latour 1996	R27,830	R61,941	R88,792
Chateau d'Angludet 1996	R2,420	R2,662	R2,684

Table 10. Auction price achieved by two traded wines over 5 years (Decanter, 2011).

The fine wine market revolves around fewer than two or three hundred wines, perhaps 1% of all wine, traded around the world and sought after by those who want to drink and enjoy it, those who want to collect and rarely drink it and those who have no intention of ever drinking it but see it as purely an investment to be traded later.

Section 2

Chapter 7

7.1 South African wine culture

It is now 352 years since the first wine was produced in South Africa, yet the industry is considered 'New World', and it seems that any wine drinking culture is very much younger than that. Roland Peens, of 'Winecellar', believes that SA's wine culture is only twenty years old (Peens, 2011 Appendix F) and industry expert Dave Hughes thinks that South Africa,

> "Doesn't really have a wine culture" (Appendix D).

For a very long time South Africa had one internationally recognised wine, 'Vin de Constance', and a lot of sweet or semi-sweet usually white wine ('wyndruif' or Semillon) of variable quality. Wine was often drunk for its effect rather than any inherent enjoyment and indigenous farm workers grew used to the rough and sweet produce of the farms they worked. Favourable exchange rates, strong links to its biggest export market – the UK – and massive replanting of high yielding varietals after phylloxera invasions in the 1860's saw production increase and income fall due to over-supply. Some 80 million vines had been replanted and it was known that farmers would simply poor unwanted wine away.

By the early 20th century the situation was so serious that a Government funded controlling organisation, the KWV, attempted in 1918 to set quotas in the key areas of varietals, production yields and prices. The KWV determined what could be grown where, how much could be produced, how much would go for distillation and what price could be set. This lasted until 1992. Setting predetermined price levels obtainable for your produce is hardly an incentive to search for quality, the first target becomes to achieve or exceed production levels. The increase in wine sent for distillation helped create South Africa's love of Whisky, Brandy, other spirits and fortified wines which even today have a 24% share of the alcohol consumption market leaving still wine with just 12%; beer accounts for some 46% (SAWIS, 2011).

The 1950's and 1960's saw an attempt by Government to link drinking habits amongst the population to race and decided to bar all black people from working in the liquor trade. Two things happened, firstly, the State controlled who had access to alcohol and secondly, alcohol purchase, manufacture and consumption amongst the majority black population was driven 'underground.' Even today, the local 'shebeen' does a healthy trade and the 2008 Alcoholic Beverage Review stated;

> ‘One of the liquor industry’s biggest challenges is that a significant proportion of the liquor trade remains unlicensed’.

Accordingly, most black people see beer, Brandy or other spirits as their first choice and many have, ‘never tasted wine’ (Loubser, 2004).

Those that were able to purchase wine did so for immediate consumption. This was partly because wine was generally of a poor quality and would not keep. Cellar hygiene was a new science, corks were often faulty and storage conditions inadequate. Those that could, drank imported European wines, which were more readily available then than today and an incredibly strong Rand, achieving R2 to the British Pound at one point made this affordable.

The isolationism of Apartheid and a dramatic fall in the Rand, to R20 / £1 soon made drinking foreign wines expensive and the market became largely domestic and for white people. The Soweto Wine Festival original member Lyn Woodward and co-founders Marilyn Cooper CWM and Mnikelo Mangciphu felt that in 2004 it was time to “start introducing South Africa’s quality wines to the remaining 80% of our population,” clearly identifying the racial divide in consumption. Wine, they wrote, is not only “…for white South African’s to enjoy. It should be a way of life for all” (http://www.sowetowinefestival.co.za, 2011).

The end of Apartheid is almost the beginning of South Africa’s wine culture, though this is hardly borne out by falling consumption figures. Dave Hughes’ pessimistic view of a wine culture is supported by the 2011 SAWIS figures which saw South Africa in 62nd place in the World consumption per capita table, with domestic wine consumption of 7 Litres per person per annum (6.2L for natural wine only). This is despite being the 8th largest producer in the World (SAWIS, 2011). In 1986 consumption was nearly 10 Litres per person, but consumption has never been large and the falls have not been as significant as, say, France, whose consumption has fallen by more than half from a high of 120L to 39L per person (SAWIS, 2011). Investment will always be difficult when there are, ‘fewer people drinking less wine’ (Forrester, 2011 Appendix B).

Only in the last 20 or so years has the stirrings of a wine culture emerged. There has been a significant red wine boom, vines are virus free, wines are better made and able to age and homes at the top end of the market are even being built with cellars. A serious reputation is being established for SA style port wines, Muscadels, botrytised wines and for MCC sparkling wines. Consumer education has improved and many understand wine maturation and appreciate that some wines improve with keeping. However, the everyday consumer wants young wines. Even in 1994 Michael Fridjhon wrote about the ‘fashionable, forward, soft fruit tannin wines’ that were taking the place of classic, restrained old style wines. Roland Peens of ‘Winecellar’ laments how difficult it is to sell old wines (Appendix F).

people distrust wines of age and doubt the chance of them still giving any pleasure. An investment culture needs to hold aged fine wines in reverence to add to their desirability.

The challenge in developing a sufficient wine culture to support a healthy investment industry is in getting young people to adopt a wine based lifestyle despite mixed messages linking wine with health issues and the lure of spirit based RTD's. Ken Forrester believes it is also about educating the public and developing discerning palates, something absent at present (Forrester, 2011 Appendix B). Another challenge is to further encourage the black and coloured population into an acceptance of dry wine styles and regular wine consumption especially in areas where beer and spirits reign; it is perhaps easier to establish a wine culture in the Western Cape where visiting vineyards is a popular activity, but as Norma Ratcliffe says, "the market is in Johannesburg" (Ratcliffe, 2011 Appendix G). The potential benefits to the wine industry and the Government of a wine consuming black population are enormous. Some 79% of the population are black and more than 8% - some 2.7 million people - comprise the salaried, educated and middle class 'Black Diamonds' who could become a likely investment segment (UCT Unilever Institute of Strategic Marketing, updated 2008). Johann Krige at Kanonkop has sold lots of fine wine to prominent black South Africans and thinks this will continue and increase (Krige, 2011 Appendix E).

Government has a role to play in developing a wine culture but it has the dichotomy of promoting responsible behaviour and moderation whilst receiving some R38.7bn in duties and VAT from wine products in 2010 (SAWIS, 2011). More than 2.2% of the country's GDP comes from the wine industry which employs some 275,600 people (SAWIS, 2011). The Government has enjoyed a greater income from wine each year since 2005 than the producers of the wine themselves. Yet in comparison to other countries the duties it imposes seem fair. In SA, R1.62 is charged in Duty on a bottle of wine (R2.32 p/L) and then 14% VAT (SARS, June 2011); on a R20 bottle of wine this amounts to R4.65 or 23% of the total. In the UK £1.69 is charged in Duty and then 20% VAT (UK HM Rev & Customs, March 2011). The average price paid for a bottle of wine in the UK (Feb 2011) is £4.26 of which the total tax is £2.88 and the Government's share 47% of the total price, twice that of SA's. The percentage declines with increased bottle price; on a R100 bottle in SA the government's share would be 16%. More duties are collected along the chain, such as storage, brokerage and delivery, but that is true of all countries. Duties and VAT do not seem to be a barrier to developing a wine culture or investing in wine in South Africa, though government support of the industry, where average turnover reached R40m per wine farm last year, but average profits were nearer R200,000 (den Dulk, 2011 Appendix A), would stimulate an industry recovery.

Undoubtedly, wine investment requires an active and broad based wine culture.

Chapter 8

8.1 South African wine investment

There are investors in South Africa who are investing in fine wines, either through brokers or investment companies, by buying and trading foreign wines in the world market. Very few are buying and trading only domestic wines. The question is how is to grow investment and trading in South African wines at home and amongst an international clientele. A review of the reasons why there is little fine wine investment in SA wines is required.

8.2 Barriers to investment in SA wines

8.2.1 Wine value

Building a base of wine collectors and connoisseurs will take time. The indications are that an indigenous wine culture is only emerging. It will require winning many more over to regular wine drinking, especially amongst the young (18 to 25 age group) and 'Black Diamonds,' and changing attitudes to buying, keeping and paying more for wine. It will need to build an understanding of mature wines and crucially that fine wines have value, both in drinking enjoyment but also as potential investment. It will also need a belief that South Africa has its own fine wines and in the real value of those wines. South African fine wines are priced at around 1/10th of their international counterparts (Forrester, 2011 Appendix B) and this creates an impression to international investors that they are of lower quality and also an expectation of entitlement from domestic buyers holding prices down. Investors won't be seduced by margins of 20% on a wine costing R40 (ie R8 profit) but might from a wine at R500 (ie R100 profit); top wines need to be expensive to attract investment, a bitter pill for domestic consumers.

8.2.2 SA's short history of fine wines

The production of fine wines in South Africa has been a relatively recent phenomenon. A universal recognition of those wines as such is probably even less recent, if at all;

> 'We do not see South African wines as an investment – indeed, the auction world does not feature South African wines at all' (Sutcliffe, 2011).

It will take 50 or 60 years to develop a history of fine wine production (Peens, 2011 Appendix F) but a start is evident. Excellence is regularly recognised in a number of domestic competitions and publications and increasingly rewarded on the international scene.

8.2.3 Domestic recognition of SA fine wines

The SA wine trade is very price conscious. The KWV control of prices until the 1990's has left an historic view where the quality of the wine does not determine its price (Howard, 2011 Appendix C). Differentation of wine quality is essential to an investment market and trade and consumers need signposts.

Platter's South African Wine Guide is now in its 31st year and is the first port of call for many looking for 'Superlative Cape Classics' rated 5 stars by the team of tasters. Platter's annually announces its Winery and Wines of the Year and in 2011 gave more than 50 wines their highest award. Despite an international audience, Platter's underlines that the awards represent quality, ' in an SA context' (Platter's, 2011).

Since 1990 the National Bottled Wine Show in South Africa has issued Veritas Awards and together with its coveted Veritas emblem, has become synonymous with top quality wines and there is no doubt that retailers draw consumers' attention to successful Veritas wines. The organizers believe that their Gold and Double Gold awards are of value to the whole industry, creating a prestigious image and state boldly; 'the results are trusted implicitly when international as well as local wine buyers use them to assist in their buying decisions' (Veritas, 2011).

Slightly younger is the Trophy Wine Show, sponsored by Old Mutual, which since 2002 has awarded Trophies and medals in numerous categories. The inclusion of three international judges (with six local judges) gives the awards a degree of international recognition and helps establish South African wines amongst the best in the world. Co-owner Michael Fridjhon notes how the show is tracking progress;

> 'The clear signs of an overall quality improvement at the top of the wine market - which we have seen for some time' (Fridjhon, 2011a).

Judge Debra Meiring MW felt of the 2011 show that, 'quality in South Africa is at its highest ever', and the UK"s Neal Martin wanted SA fine wines to 'get around the world' and that you 'have to start re-thinking South African wine' (Bolander, 2011).

The Michelangelo International Wine Awards (Est.1996) also try to infuse a foreign perspective and included, in 2010, 15 judges from 15 countries spending six days judging the 1,310 wines entered. Only domestic wines are judged, however, so without a direct international 'blind' tasting comparison one could debate the 'International' label. The small entry (Platter's rated over 6,000 wines in 2011) is another area of criticism.

The Terroir Wine Awards asks its seven local judges (five of whom are winemakers) to assess typicity and expression of origin in its awards, which must ultimately help fine wines establish their place and authenticity in the pantheon of world wines.

Another ‘International’ wine competition, the Santam Classic Wine Trophy (Est 1998) only assesses domestic wines, but is judged solely by French judges, though placed here under ‘domestic recognition’ as SA wines are only judged in SA, against each other and not against foreign wines. This competition is a direct attempt to get South African wines under the noses of important industry figures from a nation historically quite insular in its wine tastes (and to get an impartial judgement). It is held in association with France’s leading wine publication, La Revue du Vin de France (RVF) and a limited number of only 17 medals can be won to ensure legitimacy and credibility for winners. The organizers state the aims of the competition are to;

> ‘Recognize, reward and promote wines of elegance, balance and finesse. Wines should also show ability to age well. The Classic Wine Trophy is given to the most iconic entry’ (Classic Wine Trophy, 2011).

‘Elegance, balance and finesse’ is a classic French concept, almost flying in the face of New World blockbuster wines and will help establish SA wines as wines offering more than just big fruit and alcohol. It is a concept closely associated with investment wines. Success also brings international exposure say the organizers and, ‘following our 2010 RVF article, two South African wine estates were approached and asked to be represented in France: Vergelegen and Ataraxia’ (Classic Wine Trophy, 2011).

Other competitions and awards, such as the SA Young Wine Show, Diners Club Winemaker of the Year, the ABSA Top 10 Pinotage Awards and the plethora sponsored by Wine Magazine SA all help to raise awareness and support the pursuit of excellence.

There are critics of domestic competitions, however. Local judges can also be insular in their tastes. The 2007 response by some winemakers that the earthy, burnt rubber notes of domestic red wines identified by Jane MacQuitty (2007) took a long time and faced much resistance before concessions were made in winemaking. Local judges are often stakeholders in the industry, frequently winemakers (even sometimes judging their own wine) and maybe not as independent or well-travelled as one would like. As Remington Norman MW says, SA wine tasting panels are;

> ‘..One of the biggest challenges facing SA wine’ (Norman, 2011).

Neil Pendock quotes Norman in his plea for truly international palates to judge SA wines (Pendock, 2011). Tim James CWM goes even further;

'It would be depressing indeed to imagine that the Trophy Wine Show judges have awarded gold medals to red wines representing the best the Cape has to offer' (James, 2009).

Platter's Wine Guide best wines have not been without their critics abroad also;

'A recent London tasting of wines rated 4½ and 5 stars by the Platter's Wine Guide was described by Times pundit… Jane MacQuitty as a car wreck. "Of the 63 wines I tasted, only 13 came through as winners… South Africa's tell-tale dirty, rubbery red wine pong was there in abundance" ' (Pendock, 2008).

Comments like these, despite being made years ago, take a long time to fade in the memory of international investors.

Domestic palates, after years of isolation, few top foreign wines on domestic shelves and such a short period of fine wine production, may be at odds with international tastes – and investment considerations. Neil Pendock is perplexed by blatant variations;

'That there is a disconnect between international and local palates was demonstrated in January at the Chenin Challenge when another MW, Cathy van Zyl, correlated at an impressive -0.77 with panel chair Michael Fridjhon. Sure two judges can disagree on the odd wine, but when there is such disagreement over all the top wines, confusion reigns worse than in the Tripoli town council (Pendock, 2011).

Perhaps some reservation should be held over locally judged domestic wines, especially when compared with top foreign wines by a home jury. Perhaps though, it is just too difficult to believe for some when comments are published such as those emanating from Jörg Pfützner's 'Big Five' tasting held recently in Cape Town. Pfützner pitted five SA wines against five top French wines over five vintages of each and the attendees agreed that the 1995 Kanonkop Paul Sauer 'totally outperformed the Mouton-Rothschild 1995', which was 'so much more youthful and more intricate than the latter' (Eedes, 2011). In the same magazine review, Eedes concludes that the Paul Sauer is 'more than capable of matching up to a French great.' Remington Norman's comments above seem applicable here too when one considers that there were fewer than 20 local people in attendance and that the cost of attending all elements of the tasting was R5,000 each (Wine Magazine and the author of the above comments were invited free as, one suspects, were the winemakers of judged wines who were also in attendance), hardly an unbiased or random sample.

Similar concerns can be raised about the 'SA Top 100 Wines' challenge, announced in May 2011. Critics might challenge the concept of the 'top' 100 wines in SA (as the general public would interpret the results) knowing that in total only 390 wines were judged. Indeed of the

6,000+ wines in SA, some categories were statistically insignificant, for example of only 32 Chenin Blancs entered, 14 are now the 'top' in SA and of only 28 Cabernet Sauvignons amongst the many hundreds available, some 8 are also the 'top' in SA. Investors will need better guidance than that.

8.2.4 International recognition of SA fine wines

Entry into the world market in the 1990's saw many of the then 70+ co-operatives in SA release poor quality, cheap wine abroad. This was an opportunity to 'dump wine' (Howard, 2011 Appendix C) and international markets may still be affected by the low standard then coming out of SA. The SA wine trade had no cohesive view of how to sell wine abroad and little understanding of how to position fine wines (Howard, 2011 Appendix C). Only now are SA wines commanding more shelf space in key foreign markets. Yet in Sweden, where the Government monopoly prevents mass imports of cheap wine so that wine is judged only on quality / price ratio, SA has been the biggest imported wine producer for the last three years. With a blank canvass SA wines have obvious appeal.

For investment purposes, especially by foreign investors, it is important for SA wines to establish themselves internationally, though some, such as Eben Sadie, have a slightly different take on this (see below). This is happening and each year more SA wines are appearing in fine wine lists amongst international publications and competitions.

One of the most important is the International Wine and Spirit Competition. For more than forty years the IWSC has involved a panel of international judges and some 30 or more associate judges drawn from more than 15 countries to taste blind and award in varietal and national categories. South Africa has established itself as a regular medal winner and in 2009 received 10 Gold Best in Class medals as well as 107 Silver Best in Class medals. In 2010 only three Gold Best in Class medals were won, but SA did collect two International Trophies. Possibly the most important achievement so far has been Kanonkop's three time success in winning the competition's most prestigious trophy; the Pichon Lalande Red Wine Trophy, a feat unmatched by other New World countries and especially impressive as it is in the same class as First Growth Bordeaux and Grand Cru Burgundy. It was a similar story in the UK based Decanter Magazine World Wine Awards, where SA again won two International Trophies in 2010. Also in Europe, two South African wines were awarded Gold medals in the prestigious Concours Mondial Bruxelles in 2010. The 2011 results of the International Wine Challenge (IWC) held in London saw SA win 13 Gold Medals (this was 3% of the 'Golds' awarded) and 66 Silver Medals. There is an important issue here, though, some top producers do not enter their wines in competitions and others don't make enough to export to all the critics, publications or shows in key countries.

It is not just about winning competitions. Inclusion in ' best of ' lists and recommendations by publications such as Wine Spectator and Wine Enthusiast in the US, and UK magazines Decanter and Wine, as well as frequent mentions on websites such as Robert Parker's and Jancis Robinsons' will familiarise foreign buyers with many of the best SA wines. Emil den Dulk, owner of De Toren, recognised this when Fusion V was named the only SA wine to be rated in the top 100 wines 2010 in US magazine Wine Enthusiast, he believes it 'raises the profile of all South African wines' (den Dulk, 2011).

Regular appearances on restaurant lists will also help; Mike Ratcliffe speaks proudly of Warwick wines appearing on the lists of 'four of the top ten restaurants in the world'. Many foreign buyers are already familiar with names such as Sadie, Meerlust, Warwick, Kanonkop, Glen Carlou, Thelema, Rustenberg, Rust en Vrede, Vergelegen and Tokara. Consider the travel website article on Viamichelin.co.uk which enthuses;

> 'I discovered this exceptional wine-maker thanks to the venerable Parisian wine shop Les Caves Legrand on Rue de la Banque. I asked Kristeven M'Boungou, their knowledgeable and charming New World wine specialist, which South African wines I should try first. 'Eben Sadie's vintages!' was her unequivocal answer' (Tresmontant, 2010).

Eben Sadie's wines are an interesting case in point. Firstly, Eben had never heard or read the quote above and though flattered, he is at odds with any attempt to appease critics or enter competitions. Despite his red blend Columella receiving 95 points from Parker in 2005, 2007 and 2008 he is completely unmoved by this. He has even withdrawn his wines from sale in the US. "I make wines to drink.. I don't run after awards and I don't take my wines around the world for approval" (Sadie, 2011 Appendix H). Sadie is suspicious of wine ratings and making wine to achieve ratings;

> "Selling on the tail of achievement is risky."

Sadie points out that wines achieving 95 points one year with a satisfactory vintage the following have little option but to be given 95 or 96 points the following. The saturation of wines now regularly receiving 90 points or more makes the assessment flawed. His point is made by the US website of '90pluswines.com' which currently lists (though many are past vintages of course) more than 7,450 SA wines rated at 90 or more points; generous by any account.

> “…anyway, 95 isn’t enough now, now you need 98 or 99 to really get noticed”
> (Sadie, 2011 Appendix H)

Sadie echoes many winemakers in South Africa and elsewhere who don’t “play the award game” (Sadie, 2011 Appendix H) and who don’t want their wines as collector’s items or investment opportunities, now or in the future.

South African wines have never become regular features in the pages of ‘The Wine Advocate’, Robert Parker’s influential US buyer’s journal. Part of the problem was his – and his key tasters - lack of familiarity with SA wines given their small role on the world stage. SA Master of Wine Greg Sherwood wrote on the Wine Anorak website in 2002 that,

> ‘.. to my knowledge, no large and comprehensive tasting of all the top (SA) wines has been carried out recently in the way Mr Parker has just done with boutique Australian offerings’ (Sherwood, 2002).

This may change now that ‘The Wine Advocate’ has a new taster with responsibility for South Africa. Neal Martin, a British wine writer, is more familiar with SA wines and perhaps, more kindly inclined toward them as his comments in 8.2.3 show. Good news for some, but again Eben Sadie has his doubts, fearing that winemakers might start to make wines to gain high scores, something SA wines have largely avoided so far.

Still, more than 100 SA wines have been given ratings of the all-important 90+ points over the years by Parker and several, including Ken Forrester’s FMC Chenin Blanc, Sadie’s Columella and Warwick’s Trilogy have achieved 95 points. Normally, 95 points would ensure instant worldwide attention, esteem and immediate un-availability. In the case of most French, Italian and Spanish blue chip wines, such a rating would make them very scarce indeed, whatever was not withheld at the Château / Estate would be taken by agents or importers who would adjust their prices with rising demand. Very few bottles would make the shelves of retailers and it would be necessary to join a waiting list to purchase by the case through a large dealer such as Berry Bros. & Rudd in the UK. You might or might not be lucky and requesting, say, ten cases might see you receive three. With South African wines this is not often the case. Part of the problem is that most SA wines are easily available, there is rarely the clamour on release which sees them disappear overseas or to corporations. Some SA wines are in huge demand, of course, but most suffer because;

> “Supply is bigger than demand, there is no scarcity value, it is too easy to get the wines” (Peens, 2011 appendix F).

Scarcity increases desire; a Château Latour on a supermarket shelf anywhere in Europe would be a rare event and would not be there for many hours, a Meerlust Rubicon can be found in numerous bottle shops – and supermarkets - in the Western Cape, their website is still offering the 2006 for sale at the winery. It is not because of restricted production; Château Latour produces around 18,000 cases of Grand Vin and Château Margaux 12,500 cases annually, Kanonkop produce around 4,500 cases of their benchmark Paul Sauer red.

8.2.5 Inadequate storage facilities

Wine drinkers in South Africa have traditionally never stored their wines. As in Europe, the vast majority of wines are consumed on the day they are bought. The climate has much to do with this, keeping wine is difficult for most, only in the last few years have cellars been a reasonable addition to homes under construction and only at the top end of the market.

Figure 3. Three easily available home wine fridges; from l to r; Fuxin JG110, the Whirlpool ARC 205 and the Artevino FV150G from the Wine Essentials range.

Successful investment requires wines held for several years in excellent condition, there are few means of achieving this.

a) Home storage

Long term storage of wine requires a constant, low temperature, ventilation, absence of light and vibration and sufficient humidity. The climate in most of South Africa means that areas for storage need to be cooled, naturally or mechanically. Most homes would be too hot and even shaded parts, such as cupboards or garages, would not keep an even temperature below 18°C. The nature of investment means that most wines will be held for at least one year, usually more and serious investment will require considerable space making a specially designated area for storage essential.

Wine fridges are commercially available holding up to 270 bottles under suitable conditions; constant temperature (usually adjustable) shaded and with little movement, but lack of humidity is a problem for long term storage and they are expensive and will take up considerable space for the serious investor. In Figure 3 above three typical examples are shown; the Fuxin JG110 holds 110 bottles and costs R10,500 ($1,500), the Whirlpool ARC2050 holds 88 bottles and costs R9,286 ($1,326) and the Artevino FV150G holds 150 bottles and costs R19,999 ($2,857). Eurocave UK's popular range includes several cabinets that hold up to 230 bottles and this size would make more sense for long term investment, though this model costs R39,499 ($5,643) in South Africa. Better value might be the Artevino FV270S, holding 270 bottles for R18,999 ($2,714 at 'Wine Essentials'). Prices need to be factored in to potential profit returns. Future buyers would expect the wines in their original boxes, though, so these need to be stored and some might expect the original sealed boxes, which might prove difficult. As mentioned above, many homes are being built with cellars but only at the top end of the market. It is possible to have a cellar, often built in a spiral shape, dug beneath the floor of a garage, kitchen or spare room. A selection of styles and the technique used is shown in Figure 4.

Figure 4. A selection from the Spiral Cellars UK catalogue of underground cellars. ©SC

This is common in Europe where one of the leading suppliers, Spiral Cellars, has installed more than 3,000 in France and the UK since 1981. According to Spiral Cellar's Lucy Hargreaves, the most popular installation is a 2.25 metre cellar holding 1,360 bottles for £25,500 inc VAT (R280,500). It takes 5 to 9 days to fit. Spiral Cellar's designs include a 1.35 metre mini version (650 bottles) for £15,400 (R169,422) up to a 3 metre deep cellar holding 1,870 bottles and costing from £30,718 (R336,798). They receive many enquiries daily from all over Europe and are hoping to appoint an agent in South Africa soon (Hargreaves, 2011). Brian Bennett offers a 14 part free 'design your own cellar course' via his website homewinecellardesigns.com but it is not specifically for the South African market.

A minimum yearly recommended investment of £4500 (R50,000, Premier Vintners UK, 2011) would enable purchases of some eight cases of fine SA wine, or about 100 bottles. The investor would need six or so years before profitable trading, meaning a cellar able to hold around 600 bottles. This means a choice of, say, three large wine fridges costing cR50,000 in SA or an underground cellar at cR170,000. Both require some electricity usage. Compared with storing wine at a merchants (see below) these are both expensive in the short term, as eight cases might cost R6,720 a year to store and after six years 48 cases some R40,000 a year (discounts for bulk would apply, though) enabling storage at a merchants for only 2/3 years for the cost of the wine fridges. Fridges and cellars become very attractive financial propositions for storage of more than 500 bottles for more than two years and allow instant access and personal trading (with a licence) – and drinking – but don't permit the 'in bond' or 'on paper' trading that a broker provides.

The quality and specifications required to meet the demands of the investment market make home storage difficult unless one is prepared to spend many thousands of Rands and this coupled with the necessity for a seller's licence and having to trade from home, means that this is not a sensible option, though attractive from a tracking and security point of view. Even though wine fridges and underground cellars do an excellent job, wine stored at a merchant's facility seems more acceptable to the trade;

> 'The main problem with investing in wines is storage….buyers may be wary about lone sellers' storage guarantees' (Wasserman, 2010).

b) Off site storage

Wine-searcher.com lists dozens of professional storage services worldwide, including Singapore, Canada and New Zealand, but they list no sole purpose wine storage facilities in South Africa (Wine-searcher.com, 2011). There are many self storage facilities throughout the country, but few cater for the specialist requirements of wine. Garage type spaces are available from companies like SA Self Storage and Storage People for around R700 per month, but these are not temperature controlled and would be unsuitable long term.

c) Wine merchant storage

Most investors and collectors would consider leaving the wine with the merchant they bought it from, or renting space at a wine merchants. The facilities would be suitable for longer term storage but travel to the store or delivery of the wine, as well as rent should be factored into profit estimates. The average R70 per case per month space rental fee, for a reasonable investment holding of twenty cases over a period of one year would deduct R16,800 from any potential profit return. Also, the business might not welcome frequent visits to check on the wines and if you were trading yourself the logistics and inconvenience caused by removing and replacing cases could cause friction.

One of the first to offer on-site storage was the Bergkelder in Stellenbosch. They will store wines bought from their own Distell brands in perfect underground conditions for a fee of R42 per case per year. Owners may visit their wines and tastings are offered of the vintages that they bought free of charge. Delivery anywhere on removal is also free. Excellent value indeed, but the limiting factor is that only Distell wines, the owners of Bergkelder, are permissible and despite the spate of recent awards for brands like Fleur de Cap and the world class Nederberg dessert wines most do not figure on the international stage yet. For domestic investors, though, this service provides a cheap way of building a portfolio of wines which could become investible, especially the estate wines of Stellenzicht, Plaisir de Merle and Uitkyk, but the risk factor is there. This is no doubt a longer term proposition than buying first growth Bordeaux and investors would have to believe that not only can the wines survive in good health until demand makes them desirable, but also that they will be sought after in years to come and worth much more than was paid for them.

Whichever method is chosen, there remains in the eyes of the investor at home and abroad, 'concerns over quality of storage' (Fridjhon, 2011) of wines held in South Africa.

8.2.6 No trading platform

Profit from investment depends upon being able to sell wine at the right time. This requires access to potential buyers, as Jancis Robinson MW says, 'obviously you need a way to trade' (email, Jan 2011). In Europe there is a route to buyers via consumer magazines, dozens of wine brokers, several auction houses, various websites and ultimately most wine merchants who, given sufficient assurances about provenance and storage, would buy from a walk-in customer. In South Africa it is not so simple.

There have been efforts to establish a secondary trading platform in SA, most, according to Michael Fridjhon, 'have failed'. Attempts to create investment funds have faltered 'due to a lack of investor support' (Wasserman, 2010). Presently there is, 'no real transactional environment' (Fridjhon, 2011) and attitudes towards such efforts have not been kind;

> 'In local industry circles…there has been doubt, if not outright disbelief, that this country could support an en primeur market' (Morris, 2008).

There are several reasons for this. Firstly, the number of potential investors is small, perhaps as few as a couple of thousand according to Roland Peens. A comparison of sales of retailer WineCellar in SA and Farr Vintners in the UK confirms this. In 2010 WineCellar sold 450 cases of wine, Farr Vintners sold 67,500; some 150 times the amount. Ken Forrester estimates that the total economically active wine-drinking market in South Africa amounts to some 600,000 people, in the UK or Germany it could be 20 million.

The need for investment from abroad is apparent. There may be many more in SA who would invest were they aware of the potential, but ‘right now, it’s a tiny market’ (Phillips, 2011). Rob Morris agrees;

> ‘The pool of local spec buyers is virtually non-existent. Crucial to any success will be international demand’ (Morris, 2008).

The market may be small, but it is healthy. Beyers Truter could sell several of his wines many times over and has to limit sales and disappoints many hopeful buyers. He says,

> ‘There is a secondary trade market and I can prove it…I just haven’t made any money out of it’ (Truter, 2011a Appendix I).

Indeed, Truter laments missed opportunities of investment in the 1980’s. Wine legend Jan ‘Boland’ Coetzee wanted Truter to invest with him in some 1986 Kanonkop Paul Sauer at R87 a case. Truter didn’t want to go in on the R26,000 deal for 300 cases. Within four months, rave reviews had pushed prices up to R400 a case meaning Truter missed a potential profit of R47,000 in four months in 1987.

Secondly, the competition for investors’ money is considerable. Even with six basis points recently chopped off the savings rates fixed return deposits can offer the investor around 7% to 9% (investors will remember just two years ago when 11% was available on some saving bonds) and this without the risk of the volatility of luxury commodities. With guaranteed returns, no effort and no risk the attraction of wine investment funds realising only a few percent more, if at all, wanes.

Thirdly, with no buyers driving demand there are few, if any, secondary trade organisations. Some auction houses have held wine sales, especially of deceased person’s stock, but demand is patchy, sales have not been conclusive and there appears little passion to offer more (see Chapter 9 for a review of the role of the CWG and Nederburg auctions). This may be part of the distrust of older vintages, traditionally poor storage and the preference for young wines mentioned earlier. Auction house Boland Auctions usually integrates wine in its general sales;

> ‘We often have a few cases of wine in our general auctions, but these prices tend to be around R35 per bottle and sellers generally want much higher prices’ (Brown, 2011).

Well known auction house Stephan Welz & Co. in a recent communication showed no interest in holding wine auctions (McRae, 2011) and Christie’s SA does not intend to offer wine auctions here. Without a platform to sell, buyers might hesitate to invest in wines and without sufficient buyers and sellers secondary trade houses will hesitate to offer sales platforms.

Norma Ratcliffe at Warwick Estate does not need access to a secondary market to sell her wines and had no need to offer wine futures. Whilst in charge, Ratcliffe could sell everything from the winery and found that anyone hoping to invest in her wines was quite prepared to buy direct. Older vintages were more popular among buyers who wanted a wine to drink immediately and many would pay a premium to get them. Few had adequate storage to buy and hold younger vintages, so wine for investment wasn't considered. Either way, "people are going direct to producers, they are not bothering with auctions" (Ratcliffe, 2011 Appendix G).

The Bergkelder Vinotèque in Stellenbosch was perhaps the first to take advantage of the South African producer / consumer / investor link in 1984. They offered members pre-release wines whilst in barrel and storage on purchase. Pre-release offers didn't last long, though and are no longer available. The problems were largely administrative as under the Distell ownership their twelve brands and dozens of labels made offering en primeur impractical (Van Deventer, 2011).

Kanonkop Estate offered en primeur for the 1986 vintage, sold in barrel in 1987. The offer was well received and most was immediately sold. The wine was stored at Kanonkop but problems arose when some purchasers, who had paid at least a year previously, failed to collect their allocation. Owner Johann Krige was frustrated with the logistical problems that ensued. Some buyers were untraceable, some had moved away or abroad, others had died. In the end, Krige was left with 4,000 cases of wine which was taking up room at the winery, taking up time and money in administration and could not be sold as ownership was unclear. Krige still has enough wine should the owners appear, but managed to sell the rest. It was a harsh lesson which has convinced Krige that Brokers are essential, "we are winemakers, that is what we should be doing" (Krige, 2011 Appendix E). Recent success with their limited release Black Label Pinotage, sold in two tranches, has led Kanonkop to re-establish an en primeur offer, but this time through négociants.

> 'The first allocation to our two négociants will be 600 bottles, with the next tranche of 400 bottles released a few months later once the market has determined the value of the wines' (Krige, 2010).

Kanonkop's responsibility will end when delivery is made to the négociants, as in Bordeaux, and Krige forsees that this will further establish a secondary market for the wine;

> 'With two négociants controlling the supply and demand they will be able to buy back stock from willing sellers to sell on to parties willing to pay a higher price.'

Krige is selling previous vintages of Pinotage through three négociants now and by 2012 will have a full en primeur system in place for the 2011 vintage. By 2012 Krige believes his wines will have sufficient credibility to sell in barrel and expects to add the Paul Sauer red blend to the offer. Krige believes other fine wine producers will soon follow and within five years there will be the basis of an en primeur system in South Africa. With en primeur offering the best opportunity to realise profit any expansion of such schemes must bode well for increased wine investment.

> 'This secondary market, which the South African wine industry needs more of so as to establish itself as a producer of really premium wines, will open up a totally new set of dynamics in the wine industry, as well as creating an appreciation for and collectability of fine local wines' (Krige, 2011a).

The release of the Black Label Pinotage is a deliberate attempt to stimulate a secondary trading market, 'in which demand outstrips supply to the extent where a number of collectors and wine-lovers partake in a healthy willing-buyer, willing-seller scenario as is the case in the French industry' (Krige, 2011).

There may be a very limited trading platform for wine at present but the signs are good for the future and most investment is based on predicting future trends and gambling on future supply and demand.

8.2.7 Lack of Icon wines

'Icon' wine, some definitions ;

'object come to be regarded as having a special status' (Wikipedia)

' limited, pre sold, hands on, unique style and quality' (L.VdWesthuizen)

'A cult wine must have its own particular taste… and it must have ageing potential' (Dubourdieu)

Only 1% of the world's wines are tradable, it seems, the very best of just four or five countries; their icon wines. With such a short history of fine wines SA has not established its top wines on the world stage;

> 'I am afraid that South Africa just does not have any iconic wines' (Sutcliffe, email, 2011).

Nevertheless, icon wines are emerging in SA even though fine wines only constitute 6% or 7% of the wine market in SA (Ratcliffe, 2011 Appendix G). Bordeaux took four hundred years to establish its classification hierarchy and even then changes were made later. If it is true that SA's fine wines are only some 20 years in the making then it is hardly surprising that firstly there are, 'very few possible icons' and secondly that there is a 'lack of agreement on what would be the icons' (Fridjohn, 2011).

A 2011 survey of industry professionals saw only 30% of respondents prepared to name iconic SA wines. Figure 5 below shows that some wines drew agreement but that even the most frequently named (Kanonkop PS) received only 16% of the votes. Some respondents seemed to back Fridjhon's view of a lack of world vision and what makes an 'icon' investment wine, naming their own, unreleased wine in barrel as an icon wine when previous vintages merited only two or three Platter's star ratings.

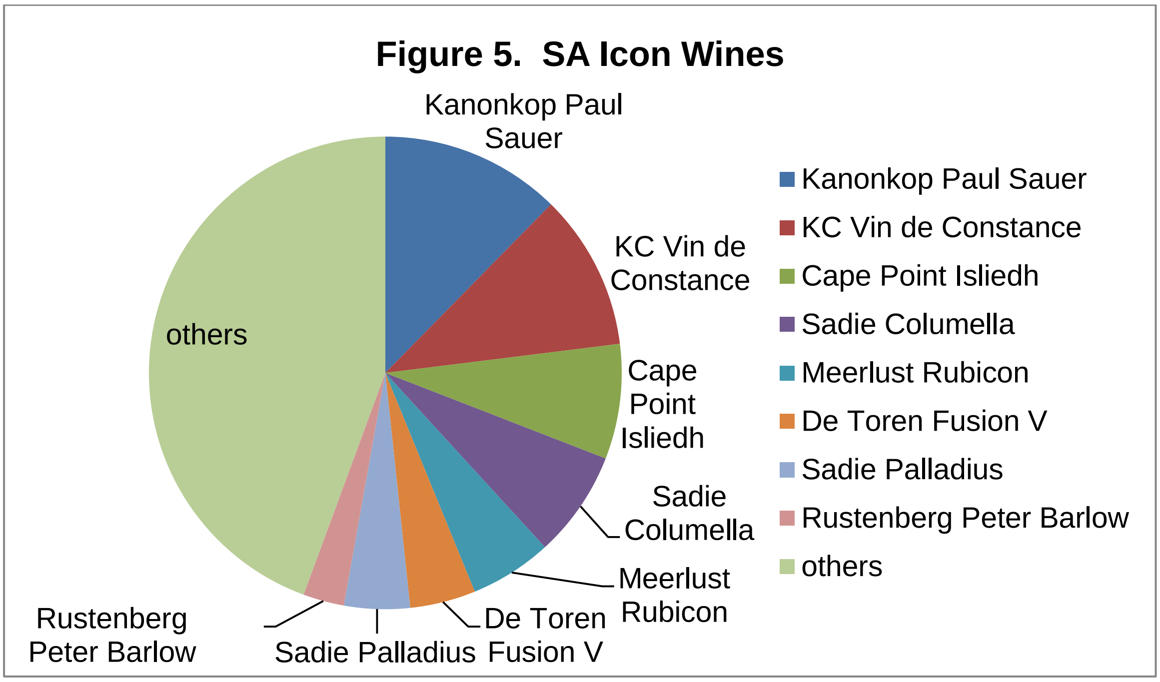

Figure 5. SA icon wines survey, 2011

Johann Krige believes that South Africa now has enough top wines to stake a place amongst the best in the world and Beyers Truter believes there are dozens of SA icon wines but that most people – especially those in the trade – are 'too scared to name them' (Truter, 2011a Appendix I). This is reflected in the survey response.

In the early days of the Pinotage Association, Truter tried to get 'Grand Cru', '2nd Cru', '3rd Cru' designations for wines so as to identify for the public the excellence of SA's best icon wines. His ideas failed to receive support.

Commenting on the afore mentioned 'Big Five' tasting (page 46), wine writer Christian Eedes agrees with Krige and Truter;

> ‘South Africa may not have as much depth as France when it comes to high-quality producers, but those that we do have don’t have to stand back’ (Eedes, 2011).

It might be inevitable that in an emerging fine wine market many wines are vying for top honours and no wines automatically assume ‘Grand Cru’ honours. Different vintages bring different results and it may be entirely healthy that Zonnebloem Limited Edition Sauvignon Blanc 2007 gets a Double Gold at Veritas but just 4 stars from Wine Magazine or that Spier’s Private Collection Pinotage 2004 wins the Trophy at the IWSC but only rates 4 stars in Platter’s. Healthy, maybe, be not conducive to establishing icon wines.

Icon wines may not establish themselves, they rely on marketing, ratings and price. This is why SA has no world icon wines; little marketing abroad, not enough overseas ratings and too low a price (den Dulk, May 2011 Appendix A). Any marketing in key countries such as the UK has been for the commercial end of the market and has damaged chances of establishing icon wines (den Dulk, Ibid). However, an analysis of just the last four years of selected SA wines shows that quality is becoming recognised and consistent. Even five years ago the best SA wines were ‘exceptionally classy’ (Van Zyl, 2006).

8.2.8 Lack of consistency

Table 11 below shows selected successful wines in the Platter’s Wine Guide between 2004 and 2008 with other international ratings as a comparison. It reflects a pattern true for many SA wines of investment potential and seems to challenge Eben Sadie’s main belief as to why local wines do not feature on the world stage; lack of consistency.

Sadie feels strongly that Bordeaux, Burgundy and other top wine regions dominate investment because of their track record. It is because they have consistently produced quality wines (despite occasional weak vintages) and driven demand around the world, not for twenty or thirty years, but for hundreds. Their wines have become brands suggesting luxury and achievement. When one buys Lafite one is making a statement, buying a lifestyle and that is a major driver in the Asian market, where the quality of wine served to guests is a marker to how much esteem they are held in. Many purchases in Asia are made to reflect prestige rather than any enjoyment of the actual wine. Sadie believes that “it takes twenty years to make a great wine and it will take at least three generations to erase negative opinions held of SA’s poor wines of the 70’s and 80’s.” He concludes;

> “It will take another 20 years to achieve consistency and even then the world won’t take us seriously” (Sadie, 2011 Appendix H).

Wine	Vintage	Platter's Rating SA (stars / 5)	Wine Spectator US (points/100)	Wine Enthusiast US (points/100)	Decanter UK	IWSC UK
Boekenhoutskloof	2004	5	90	92		
Cabernet Sauvignon	2005	4.5	92	90		
	2006	5	92	91		
	2007	5				
	2008	5				
Kanonkop Paul Sauer	2004	4.5	90	92	Trophy	Gold
	2005	4.5		94	Trophy	
	2006	5		92		
	2007	4.5		92		Gold
	2008	4.5			Silver	Gold
Ken Forrester FMC Chenin	2004	4.5	91		Trophy	
	2005	5	92			
	2006	5	93			Silver
	2007	4.5	93		SA Top 10	Trophy
	2008	5	92		5 stars	Silver

Table 11. Selected SA investment wines showing consistency over time in international ratings

This is an area that Johann Krige of Kanonkop feels puts off potential overseas wine investors. He feels that SA wines lack credibility, buyers are unsure as to their reliability, quality and ageing potential. It will take many years and lots of blind tastings of older vintages to show that they have investment potential. Krige holds vertical tastings of his Paul Sauer red for his distributors around the world in their home countries to prove its quality and often finds that his wine is most preferred when pitted against Bordeaux first growths. Bruce Jack concurs, ' I've drunk (SA) Cabernet blends from the 1960's that are still alive and magical' (Jack, 2006) and Beyers Truter recently enjoyed a 'delightful' Tassenberg red from 1969. The world seems slow to accept this, however, there appears little change in the five years since Vergelegen's UK agent wrote, 'give it time…it took many years before Grange took its place in fine wine trading circles' (Strachan, 2006).

8.2.9 Lack of awareness

A lack of awareness refers not only to the international investor recognition of SA wines but also to a domestic lack of realisation of investment potential in domestic wines. Rob Morris found an even more serious lack of understanding of investment in en primeur amongst SA producers in a 2007 survey. Morris found that many wineries said they offered en primeur wines but did not understand what this meant and were really only offering secured allocations at the release price (Morris, 2008). Johann Krige of Kanonkop supports this;

> 'South Africa doesn't understand en primeur' (Krige, 2011 Appendix E).

International investment in SA wines on any real scale is still a long way off. This may be partly because of a lack of awareness of SA fine wine quality. The reference website Wikipedia sums up why this is so,

> 'For much of the 20th century, the wine industry of South Africa received very little attention on the world stage' (Wikipedia, 2011).

Now, attention is being drawn to SA fine wines but with competition from California and Australia as well as the classic regions it could take many years for them to be considered amongst investible wines. Many wine consuming nations do not have access to SA wines and in major markets their visibility is poor. Mike Fisher writes to potential investors in the US;

> 'South Africa is the least known of the major wine-producing regions amongst US consumers. Go into any grocery store and of the 300 wines on the shelves, you will be lucky to find more than one or two of South African origin' (Fisher, 2011).

Familiarity with SA branded wine is the basis for people to trade up and if the consumer is unaware of SA wines, there is no basis for investment as there are no customers for the secondary trade. The founder of the first wine investment company in the US, Michael Wigley clearly identifies the problem,

> "A wine can be great but if no one's ever had it, it's not a good investment' (Wigley, 2007).

There is also a lack of awareness by SA investors of the potential returns from wine investment and of a lack of understanding of how asset investment in wine can be easily achieved by novice investors. People might not invest money in anything which is new and unknown to them and for some it may be that they are completely unaware that wine investment is so successful abroad and that such returns can be made. This may be because the returns on wine have often been understated (Fogarty, 2006). In a report on Australian wine investment, James Fogarty proposes that wine returns are better than most literature shows because investors mostly avoid poor vintages and thus are not subject to analyses of wine prices which include all vintages. Also, Fogarty points out that in many countries wine returns are not taxed whereas other assets are, so 'as the comparisons of asset returns typically made in the literature are comparisons of pre-tax returns, these comparisons understate the value of wine investment' (Fogarty, 2006).

Potential investors may not be aware that they may be less at risk of poor judgement than buyers of stocks and shares as they already know of the quality of the product, it has already been judged and determined for its value and quality and unlike the holders of shares in businesses which may or may not succeed wine investors can largely predict the future of their assets.

Similarly, investors may not realise that wine can fall under the 'personal collectibles' SARS category and any profits made from resale will be exempt from Capital Gains Tax. Unless the investor regularly trades his wine as a business activity the income he receives from any gains made in sales are not taxed. With other investments dividends received are taxed and not only does this affect the potential returns of other types of investments but it can also affect the individual's overall income tax liability.

8.2.10 Lack of confidence

It could be argued that South Africa is neither New World or without a history of fine wine production. With constant production of wine for over three hundred and fifty years and a wine generally regarded amongst the best in the world since then (Vin de Constance) it might be expected that SA wines already hold a certain prominence and credibility around the world. Yet there remains a lack of confidence in SA fine wines. Internationally, the wines have to prove their longevity and must continue to prove their quality. Only time can provide the answers and tastings of 20+ year old vintages conducted by the likes of Johann Krige provide the evidence. The old world remains sceptical of new world wines' staying power, German wine merchant Jan-Erik Paulson is an example,

> 'Wines from the New World and fashionable new style wines do not in my opinion have the potential for a long term increase in value. The reason for this is the ability to produce an ever increasing amount of bottles and the lack of proof of their ageing potential' (Paulson, 2006).

Paulson is incorrect in his assumption that winemakers can produce an ever increasing amount of bottles. The Wine of Origin scheme and a growing understanding of terroir has made icon wine production very site specific. Most top wines come from limited areas, even single vineyards, restricted by the extent of suitable terroir with its particular soil, aspect and microclimate. Part of the investibility of, for example, Domaine de la Romanée-Conti is that it cannot come from anywhere else and certainly cannot be duplicated anywhere else. It is important to establish to the world that SA icon wines are exactly the same, unique to an area or Estate and that production is limited and cannot be increased on demand.

It has taken hundreds of years to establish confidence in most investment wines, but once established, reputations are hard to damage. Weaker, perhaps rain affected vintages in Bordeaux such as 2003 or 2008 frequently produce wines which are easily challenged by many SA wines, yet they still sell at auction and for a price their quality fails to justify. SA wines will only be judged on their quality, most reputations are yet to be built. As Jamie Goode says, these are exciting times as icon wines and areas of potential are being discovered every day;

> 'South Africa's best wines are yet to be made, which is encouraging, I suppose. There is much potential' (Goode, 2009).

Confidence, though, will take time to build and as CEO of Cybercellar Fiona Phillips says, 'certainly the rest of the world isn't ready for investment in SA wines' (Phillips, 2011).

Chapter 9

9.1 The Cape Winemakers Guild Auction

Since 1982 the Cape Winemakers Guild has promoted excellence in winemaking. Members are invited to join after nomination and years of proving their worth. Its annual auction fulfils many criteria. Originally to showcase its members' best wines, a major aim of the event was to raise money for charity. Some believe things may have changed. For some wine estates it is absolutely necessary for their financial health (Truter, 2011a Appendix I) and necessary as a shop window to sell their wines. For others, it provides an opportunity to buy and resell after considerable mark-up (Wine Magazine, 2007). For Truter, it is a lot of work and one could question how genuine it is in its original intent (Truter, Ibid). Certainly, few of its wines are available at retail later and those that are have incurred the secondary trade profit margin increase. Some question the quality or longevity of auction wines, most of which are released very young. The 2010 auction saw more than 13,780 bottles sold at an average of R280 per bottle, not unreasonable as long term investments for wines with commercial desirability. Possibly the average consumer would balk at R280 a bottle and that may be why only 35% voted the CWG a 'relevant' organisation in 2007 (Wine Magazine, 2007a) but as a means of acquiring limited quantity wines as an investment it is a vital part of any secondary trade. Figures in Table 12 show that private buyers are now the majority of the audience and that they are spending an average of more than R15,000 each (though

	Total	Trade	Private	% Private		Trade	Private	% Private
Year	Buyers		Collectors	Collectors	Total Turnover	Purchase Amount	Purchase amount	Turnover
2010	139	63	76	55%	R 3 867 200	R 2 715 200	R 1 152 000	30%
2009	159	88	71	45%	R 5 337 400	R 4 180 400	R 1 157 000	22%
2008	100	66	34	34%	R 4 935 100	R 4 150 100	R 785 000	16%
2007	113	63	50	44%	R 5 063 200	R 4 363 100	R 700 100	14%
2006	127	65	62	49%	R 3 620 000	R 2 989 000	R 631 000	17%

Table 12. A breakdown of buyers at the CWG auctions in the last 5 years. © CWG, 2011

possibly on behalf of several friends or a club etc.). Despite a limited number of wines available, their lack of track record (as wines are usually 'one offs' – other than the reputation of the producer) and the bigger buying power of trade buyers, who are spending nearly three times more each than private buyers (Table 12), there is at least an opportunity for individual investment direct from the producer.

Though most of the CWG wines are made specifically for the auction, some are separated cuvées from selected barrels. Ataraxia and LeRiche have created 'auction' wines separately from their normal production and whilst it is unfair to make direct comparisons (auction wines are best selection, single vineyard [Le Riche], vinified separately) with their retail varietal, it is possible to examine the prices for these wines at auction. Table 13 shows the average price achieved at the CWG auction in three years for the auction version of these two wines against the approximate cellar door price of non CWG wine at the time. In all

Ataraxia Chardonnay	2007 (06 vintage)	2008 (07vintage)	2009 (08 vintage)
CWG price	R326	R303	R525
Non CWG wine price	R140	R155	R174
Le Riche Res. Cab Sauv	2008 (05 vintage)	2009 (07 vintage)	2010 (06 vintage)
CWG price	R491	R582	R461
Non CWG wine price	R180/350*	R280	R220

Table 13. Comparison of prices achieved for special cuvée CWG wine and non CWG wine. * the 2005 Le Riche was released in two tranches, one after Platter's had made the wine its 'wine of the year'.

cases the CWG wines achieved higher prices though consideration must be given to the charitable nature of bidding and the uniqueness of the cuvée. As well as spotlighting the top end of the market, CWG auctions push up prices, establish differentiated quality levels and enhance the prestige of investment wines.

9.2 The Nederburg Auction

Now in its 36th year, the Nederburg annual auction is a trade event which offers producers not only an insight into their brand's demand but also what the trade will pay for their older wines. With auction red wines being at least five years old (two years for whites) it allows comparison of wine ageing and the value of older wines, based on sale price. Kaapzicht, for example, realised that the release price of their Steytler 'Vision' red was too low based on the auction's demand and price achieved for their five year old (Howard, 2011 Appendix C).

Wine volumes are too low to impact market prices generally, but it gives international buyers an idea of the range of prices across quality levels in SA wines and because wines are the same as the original release – just older – it allows a degree of price comparison for investment purposes.

The importance of The Nederburg auction for investment purposes lies in its tracking of wine prices, especially where the same wine has appeared at the auction over two or three years.

An analysis of auction sales from 2006 to 2010 provides important information for investors. NB. prices have been converted to single bottle values for ease of comparison and only the highest price paid is considered as that is an indication of what the market is prepared to pay. Also, consideration must be given to the charitable nature of the bids.

a) Natural dry **white wines** comprise just 18% of the total. Their average age is 3.37 years, yet values have increased significantly within that time. Table 14 shows how selected white wines have increased in value, making them investment considerations.

b) **Vintages** matter to buyers, and therefore to investors; not all the older wines automatically receive the higher bids, eg Kanonkop Paul Sauer 1999 (alcoholic, early drinking vintage) sold for R300 at 9 years old, but the 1998 (excellent red wine vintage) sold for R633 at 8 years old.

c) Older wines attract generous bids, their age increases their value generally suggesting that **confidence** in the health of the wine is high, eg Chateau Libertas 1959 sold for R3833 per half bottle in 2009 and the Zonnebloem Pinotage 1974 sold for R433 in 2010. However, one should consider the 'novelty' value of such wines.

White wine	Approx		
	Price on release	sold in 2010	Increase
DeGrendel Koetshuis Sauvignon Blanc 2007	R75	R153	104%
Vrede en Lust Viognier 2008	R110	R183	66%
Durbanville Hills Rhinofields			
Sauvignon Blanc 2007	R70	R116	65%
L'Avenir Chenin Blanc 2006	R50	R86	70%
Spier Private Collection Sauvignon Blanc 2007	R70	R163	132%
Uva Mira Chardonnay 2008	R200	R266	33%

Table 14. Selected white wines at Nederburg auction 2010 with increased values

d) There are opportunities for the investor to acquire investment quality wines at '**bargain**' prices, eg Uva Mira Chardonnay 2007 lowest successful bid was R166 (before VAT) in 2009 when its cellar door price at the time was R175.

e) Not only 'blue chip' wines acquire value, many **commercial, higher volume** wines achieve excellent value growth, eg Chateau Libertas, whose price today is around R35 achieved R108 for the 1994 in 2010 and R1000 for the 1968 in 2008. Also, Zonnebloem Cabernet Sauvignon whose price today is around R70 achieved R1633 for the 1970 in 2010 and R2333 for the 1964 in 2008.

f) Top investment wines show **consistency** in their returns. Table 15 shows how three suitable investment wines consistently achieve healthy returns at five or six years old. Such consistency is essential for investment purposes even if growth is erratic.

Wine at 5 yrs. Old	achieved in '06	'07	'08	'09
Jordan Cobblers Hill	R316	R350	R225	R233
Hamilton Russell Pinot Noir	R300	R250	R366	R266
De Toren Fusion V (6 yrs. Old)	R416	R416	R400	R416

Table 15. Consistency in top investment wines over time at Nederburg auction

Tracking price changes at the auction, of wines that have appeared more than once, does not appear to reflect any trends, though 2008 and 2009 show perhaps the effects of the recession. Table 16 below shows wine price achieved at auction for selected wines over two or three years that they have appeared.

g) Top investment wines **increase in value** over time. Though Table 16 makes a generalised conclusion difficult, it is evident, as Table 17 shows, that 'blue chip' wines attract prices which reflect considerable growth between their release price at cellar door and appearance at the auction. There is no reason why a secondary trading market could not achieve prices similar to the Nederburg auction, in which case the investor could expect returns similar to Table 17 over a five year period; an average of which amounts to **30% pa.**

Wine	2006	2007	2008	2009	2010
Nederburg Edelkeur NLH 2002		R116	R77	R87	
Nederburg Edelkeur NLH 2004		R141		R79	R125
Asara Bell Tower Red 1998	R166	R95	R131	R250	
Chateau Libertas 1994 (1.5L)	R166			R175	R216 (adjusted)
Le Riche Reserve Cabernet Sauvignon 2000		R250	R266		
Zonnebloem Cabernet Sauvignon 1967		R2666	R1083	R800	
Kaapzicht Steytler Vision 2003			R233	R233	

Table 16. Selected same wine Nederburg auction prices over time

The Nederburg auction is less accessible to the individual buyer. Only people with liquor licenses are allowed to purchase wine at the auction, though the public can pay to attend a pre auction tasting of some of the wines on sale. Should they then wish to purchase they either have to ask an attending retailer to bid on their behalf, or go through the Bergkelder Vinoteque who will bid for them. This service is only open to Vinoteque members, however, who already have wine stored at the Bergkelder, though the service is free. Only a few individuals bid by proxy in 2010 and it is aimed more at the Vinoteque's larger buyers and

Wine	Vintage	Release Price	Auction price*	Growth	Annual growth
De Toren Fusion V	2000	R110	R416	278%	55%
	2001	R135	R416	208%	41%
	2002	R170	R400	135%	27%
	2003	R205	R416	103%	20%
Jordan Cobblers Hill	2001	R150	R316	110%	22%
	2002	R165	R350	112%	22%
	2003	R168	R225	34%	7%
	2004	R168	R233	39%	8%
Kanonkop Paul Sauer	1994**	R58	R433	645%	43%
	1995***	R69	R316	358%	30%
	1998****	R100	R633	533%	79%
	1999*****	R130	R300	130%	14%

Table 17. Comparison of release and Nederburg auction prices, showing growth over time. * at 5yrs age, ie the 2000 vintage appeared at auction in 2006, the 2001 in 2007. Kanonkop Paul Sauer was sold at **15years/***12 years/****8 years/*****9 years of age and annual growth has been adjusted accordingly.

trade customers. Many 'Nederburg auction' wines will appear on retail shelves after the auction, after attracting retail mark-ups and VAT paid at auction. Auction wines come direct from the wineries, so provenance is guaranteed.

An investor looking to sell wines onto the market would not be able to use the Nederburg auction, making the development of secondary trade outlets, such as auctions, vital to establishing a trading market.

The Nederburg auction shows that there is a demand for aged SA wines and that SA wines grow in value over time.

Section 3

Chapter 10

10.1 The way forward

There are signs that the traditional en primeur system in France is wilting as producers tire of seeing négociants make huge profits at their expense. Changes in US law has seen some Bordeaux Châteaux ship directly to purchasers in the US and négociant firm Millesima is among the first to cut out others in the chain. Top Bordeaux producers have their own agencies in place in major markets and this could make it easier for SA residents to purchase wines at attractive investment prices. This could in fact stimulate an interest in SA wine investment as consumers become more familiar and more confident in buying, holding and trading. Selling top Bordeaux in SA to other South Africans might show how simple it could be and how relatively low in risk. *Getting South Africans to invest in European wine successfully is perhaps the best way of stimulating investment in SA wines.*

Investment wines are an exclusive category and SA wines must fight for their inclusion. Waiting for the world to discover SA excellence puts us alongside Australia, California and now Chile and New Zealand. SA winemakers need to be ambassadors for SA regions and styles and need to be cognisant of the best from around the world. As Roland Peens says, they need to 'look outward' and understand great wines, but then create greatness of their own and the more uniquely terroir based the better. Beyers Truter has identified, 'SA's best winemakers were much more in sync with their terroir than international commentators gave them credit for' (Truter, 2011).

A shift in wine style, away from the fruity, soft tannin early drinkers seemingly so favoured by a large part of the wine drinking public may not be necessary, at least for the top wines. Most investment quality SA wines already possess the ability to age, with a structure and balance that suggests long life. What is required, perhaps, is to educate potential investors that certain wines improve over years and as with top Burgundy and Rhone may be less enjoyable in their youth.

At the other extreme, there may be no advantage in creating 'blockbuster' wines big on alcohol and fruit aimed at appeasing influential foreign judges with little to distinguish them from other New World countries. It seems wrong just to 'manufacture' a wine in a style which will score well in competitions and achieve the magical 90+ score.

> 'One of the ugliest facets of the modern wine world is the rise of the point chasers- people who buy wine solely on the basis of Parker's ratings' (Goode, 2009).

SA wines would appear to have all the requirements to become highly investible. They are achieving recognition abroad and because of years of isolation and a general dismissal of SA as capable of producing world class wines many winemakers have been 'compelled to operate with more care, dedication and conviction than their international counterparts' (Van Rensburg, 2011).

SA has proven itself almost uniquely capable of excellence in five diverse wine styles. No other country, except perhaps Australia, can match SA's capability of producing world class wines in each of the following categories;

Port style wines
Muscat based dessert wines
Botrytised wines
MCC sparkling wines
Bordeaux blends

And this does not include Chenin Blanc whose Loire examples have proven its ageing ability and where SA could establish a unique style. Nor does it include Cape Blends or Pinotage, which might be a harder international sell (as might Muscat based wines). Each style has candidates for international investment. Perhaps a way forward for SA to compete in the international wine trading market is to promote the niche positioning of these styles rather than contest the heavily populated Chardonnay / Cabernet / Merlot / Shiraz straight varietal style.

10.2 Creating a market

Familiarity with iconic domestic wines, together with imported icon wines and a belief in their inherent quality, longevity and desirability will inevitably mean that such wines will appear for sale, months or years later, as owners seek to raise funds on their back. Individual sales, avoiding licensing laws, through websites or magazines, via clubs, brokers or retailers is already happening on a small scale. This will increase and secondary trading will expand. Perhaps, despite the competition they provide to the small investor, hotel and restaurants could be encouraged to buy through auction more often and to trade regularly to refresh their wine lists, thus enlarging the market. This may be difficult to achieve as most are tied to distribution contracts and many will have no desire to expand or improve a wine list with auction bought wines where margins are tight (Forrester, 2011 Appendix B) or where there is little demand for expensive wines. It is believed 'The One & Only' Hotel in Cape Town still has 2/3rds of its international fine wines bought upon opening on its shelves two years later. In difficult times, refreshing wine lists with exciting traded wines could be seen as an effective marketing strategy.

Central to creating a market is distribution, especially abroad. There need to be links, through agents, foreign industry commentators or joint investments (as Bordeaux's growing presence in South America). South Africa has little access to foreign distribution channels (Forrester, 2011 Appendix B) and this must be addressed to get SA wines amongst the fine wine market. De Toren's will be marketing (through Bordeaux agents) an en primeur, very limited production wine, solely in Europe and the US next year, after it has been assessed by Robert Parker. Owner Emile den Dulk's belief in the quality of this wine and its subsequent rating will help to create a demand for other top SA wines and will;

> 'take SA wine to another level' (den Dulk, 2011 Appendix A).

Wherever demand exists, businesses will appear to meet it, whether providing storage facilities, transport, advertising or auction. Markets do not just appear, they evolve to answer a need. It will take time to establish an efficient secondary wine trade in SA, but the seeds are there.

The Asian wine market which now drives worldwide demand was built on the acquisition of wine brands as status symbols and lifestyle indicators. The potential profit of being central to the market was identified and a committed drive, fuelled by government, brought this to reality; it bore little resemblance to an understanding of wine. Indeed many felt it was in contradiction to decades of belief that the Asian palate was fundamentally different to western palates and that fine wine was unpleasant to many Asian consumers. Perhaps a lack of fine wine history, lack of understanding of the product or lack of wine culture should be no barrier to establishing a trading market in South Africa. Perhaps what really matters to potential wine investors is the numbers, and they certainly add up.

If the investor isn't seeing that potential, some winemakers are. Beyers Truter's missed investment experience has him seriously considering buying some of his own stock, holding it back and releasing in tranches. Truter has seen the vast capital income successful wines could generate by initiating his own secondary market; he believes his 'Diesel' Pinotage could easily sell at R750 a bottle a year or two after initial release and could net the winery some R750,000 more than they will otherwise get. But Truter is reluctant to do this, he cares about his customers and isn't about to take advantage of them;

> 'I can't, or won't, hold (stock) back as it upsets customers…it is basically screwing them' (Truter, 2011a Appendix I).

10.3 Creating a portfolio

Presently, the South African investor is buying foreign wines, probably Bordeaux. First Growths provide the headlines but there is a growing polarisation of the wine investment market. At the top end there seem plenty of people willing to pay R50,000 or more per case and others looking for more stock for less outlay, say under R20,000 per case. There is not much in between and this provides an opportunity for SA wines. There are currently no SA wines on release (maybe some older vintages) that sell for more than R1,300 a bottle (excluding the recently released 2006 'The Bilton' at R3,000 which only amounted to some 30 cases and is unlikely to be repeated) and most for much less. The most expensive – available - wine is probably the 'Rust en Vrede 1694' at R1,200; about the same price as a 1996 Bordeaux Third Growth Château Palmer. Once demand is established trading could easily push up the price of top wines so that SA wines fill the void in the middle sector of the market, offering excellent quality at prices well below established blue chip wines. Pitching SA wines at the lowest end of the price range is not where 'brand SA' want to be. Many believe that this area will provide some of the greatest gains in the future (Albany Portfolio Management, 2010). To understand the value of SA wines, consider the prices of current release icon wines, excluding top Burgundy, Rhone and First Growth Bordeaux, with some top SA wines, in Table 18 (prices converted in April 2011).

In most cases buying from the Estate will likely be cheaper (refer to the winery price for Vega Sicilia in Chapter 4, 4.1, 1b), for example Ken Forrester's FMC Chenin Blanc is R260 at the winery but R350 retail locally (May 2011). SA wines may seem expensive by SA standards, perhaps, but compared with international icon wines currently being traded quite a bargain; especially if one accepts a similar degree of quality. Andre van Rensberg remembers how sensational it appeared when his 'V' red wine broke through the R550 retail barrier, describing it as,

> '…a moonwalk…a small step for Vergelegen a giant leap for South African wine' (Van Rensberg, 2006).

South African fine wines can fill the void of high quality at low prices and could make creating a portfolio of exceptional wines very price advantageous.

Vergelegen Red#	R390	Vega Sicilia (Spain)	R1,950 *
Kanonkop Paul Sauer	R280	Sassicaia (Italy)	R1,100 **
Meerlust Rubicon#	R280	Harlan Cabernet (US)	R4,640 ***
De Toren Fusion V	R290	Screaming Eagle (US)	R8,285 [1]
Warwick Trilogy#	R290	Tignanello (Italy)	R500**
Sadie Columella#	R660	Penfolds Grange (Aus)	R1,800[2]
Waterford The Jem#	R760	Tua Rita Redigaffi (Italy)	R1,300**
Kanonkop Black Lbl Pinotage #	R1,100	Schafer Hillside Select (US)	R1,610[3]

#Prices quoted from Cybercellar's list

* *Four Walls Wine Co. UK* [1] *Private Classified Co, US*

** *Arvi, Switzerland* [2] *Lea & Sandeman, UK*

*** *Suburban Wines US* [3] *Winezap.com, US*

Table 18. A comparison of current release prices of selected icon wines, April 2011.

For this reason, savvy investors might look at top end SA wines as providing a budget way into the market. Buying a case of each SA wine in Table 18 (8 cases in all) would cost around R48,400 – much less if bought direct from the Estates. This is less than the cost of one case of 2009 Château Mouton-Rothschild bought in SA. SA wines could offer an exciting alternative to investors who currently buy the second wines of top estates or Third or Fourth Growth Bordeaux. An interesting portfolio might include a case of Sadie Columella rather than a case of 2008 Château Pontet Canet 5th Growth Bordeaux, currently selling at exactly the same price (Albany PM, 2011). Or more than three cases of Nederburg's Edelkeur NLH 2004 for the same price as one case of Château Siduiraut 2001 Sauternes, or maybe nearly four cases of Boplaas' Cape Vintage Reserve 2007 port for one case of Dow's 1994. An example currently on SA shelves is the Moet & Chandon NV Champagne, retailing at more than five times the price of Krone Borealis and twice the price of Graham Beck's Blanc de Blanc. A balanced portfolio of domestic wines will contain a selection of 'blue chip' wines (those with a proven track record and pedigree, a degree of scarcity, ageing potential, established desirability, even waiting lists), a selection of speculative 'low risk' wines (established, respected producers, competition success, ageing potential, rising stars) and some 'high risk' wines (often vintage dependent, maybe larger production, niche customers

Blue Chip	Kanonkop Paul Sauer	Meerlust Rubicon
	Vergelegen Red	De Toren Fusion V
	Warwick Trilogy	Waterford the Jem
	Sadie Columella	Sadie Palladius (white)
	Forrester FMC Chenin (white)	Kanonkop Blk Lbl Pinotage
	Haskell Pillars Shiraz	Kanonkop Cab Sauv
Low Risk	LeRiche Res Cab Sauv	Boekenhoutskloof Cab Sauv
	Boekenhoutskloof Shiraz	Vilafonte Series C Shiraz
	Newton Johnson Domaine PNoir	Cape Point Isliedh (white)
	Nederburg Edelkeur (white)	Bouchard Finlayson Galpin Pk PNoir
	K C Vin de Constance (white)	Anwilka Red*
Higher Risk	DeTrafford Shiraz	Spier Frans K Smit
	Kaapzicht Steytler Pinotage	Haskell Aeon Shiraz
	Tokara Director's Red	Vergelegen (white)
	Jordan Cobblers Hill	Rustenberg John X Merriman
	JP Bredell Vintage port	Hartenberg The Stork Shiraz
	Thelema The Mint Cab Sauv	Graham Beck Cuvee Clive MCC
	Ernie Els Red	Ataraxia Chardonnay (white)

Table 19. A subjective list of investible SA wines of varying risk.

or high price on release). Undoubtedly, these will be top quality wines and most will be red wines as there are few whites with the ageing capability to meet long term investment requirements. Based on the key features mentioned, a possible and highly debatable selection is shown in Table 19.

A very subjective list, to which could be added the wines of Morgenster, Uva Mira, Val de Vie, Hamilton Russell, De Krans, Sequillo and many others. Anwilka Red* is included because it is already being traded in Bordeaux via French company Fidelis Wines and thus may already have a familiarity factor to overseas investors. The white wines included tend to have established themselves as capable of many years ageing, important when most portfolios won't show any returns for at least five years. For this reason it is difficult to consider Sauvignon Blanc as a potential investment wine, though some styles, such as those of the late Didier Dagueneau are challenging that premise. Room might be kept for 'wild card' wines which suddenly become fashionable or which achieve success in competition, such as Eagle's Nest or Rijk's Private Cellar and which present an exciting – if risky - gamble. Nevertheless, such a portfolio would contain few mistakes and, as is the beauty of wine investment, any 'mistakes' can always be drunk and it is hard to imagine any of the above giving anything less than real pleasure.

There would appear to be several ways to create a portfolio of wines for the SA wine investor. First choice would be to buy from the vineyard, especially en primeur. Provenance is guaranteed, the price is the absolute best and storage could be at home or at a merchants. Second choice would be the CWG or Nederburg auctions. Both allow individuals, though it would be necessary to have a least one case stored at the Bergkelder in order to qualify for proxy bidding at the latter (at a fee of R42 p/c,p/y). Both are an opportunity to acquire small lot investment quality wines, though competition is fierce from trade buyers. Third choice would be to buy through a reputable merchant such as Winecellar, Reciprocal or Cybercellar. Their access to investible wines, knowledge and advice, possible storage facilities and delivery makes acquiring stock easy. Last choice would be to buy from retailors, who often discount wines to make space or believing them too old. Despite paying retail margins there may still be profit possibilities in the mid to long term. At present, it might prove impossible to invest in SA wines via an investment company, as they are yet to include SA wines in their portfolios.

Summary and conclusions

The wine investment market is based on a small number of wines, perhaps 5% of the total, originating mostly from a few European countries. Bordeaux dominates the secondary trade scene and First Growth Bordeaux is the most frequently traded. Investible wines have long proven histories, over decades or centuries and have acquired considerable prestige and often cult status. They are positioned at the pinnacle of the luxury goods market.

Despite criticisms, problems with vintage based demand variation and over-pricing, the en primeur system in Bordeaux continues. Many Châteaux are circumnavigating the traditional three tiered négociant system but its demise is not yet in sight. Investors in Bordeaux have to buy through merchants or at auction because of the négociant system so the secondary trade deals with nearly all the buying and selling of wine and the success of such sales has made wine a significant part of the overall investment market. The impact of the Asian market has shifted the centre of the secondary trade to the Far East and now three ‘hubs’ exist; London, New York and Hong Kong.

Significant price rises have occurred for fine wines and investors and investment funds have realised large returns, so much so that wine has become a desirable asset class, offering portfolio diversification and a degree of risk aversion. Numerous investment houses and funds have sprung up offering double digit growth for investors and many have achieved returns over the last decade of 15% per annum or more, even with the recession of 2008/11.

The wealth generated by the wine market has brought some unwanted by-products. Fraud and deception is now widespread and the market is ‘shaking out’ more dubious funds and businesses; it is an area of the financial market that is still quite unregulated, and the investor needs to be well informed and cautious.

As with other types of investment the investor can invest in a fund administered elsewhere or can buy stocks himself through a merchant or at auction. Little knowledge of the market is required with the first, much more with the second and third. Many considerations should inform any buying or selling decision. These include knowledge of the ‘right’ wines to buy, vintage variations, the costs of buying en primeur or holding wine ‘in bond’, access to correct storage and the legality and costs of trading via merchants, at auction or privately.

South Africa has a small wine trading market, with few investors and a handful of trading merchants. Attempts to offer trading futures or a secondary market have been patchy and mostly unsuccessful. This is because of a lack of wine culture in SA and a relatively short history of fine wines. The isolationism of the 70's and 80's saw key markets without access to SA wines and often SA wines were out of touch with changing European and American tastes. Re-entry to the world stage has seen real progress in production and quality and considerable international competitive success. The key word is potential and for those willing to take the chance there exists a real possibility of profit in the future. The Nederburg and Cape Winemakers Guild auction results show how SA fine wines increase in value. Many SA wines are proving themselves capable of longevity and are of investible quality and there seems general agreement that establishing an effective wine trading market in SA is only a matter of time.

The benefits of a wine investment trade in South Africa could be significant. It could attract foreign investment. The Government would receive revenue via Duties and VAT. Employment opportunities might arise in new businesses and expanded existing businesses such as investment companies, storage facilities, exporters, brokerages and auction houses with margins available all along the chain. Wine producers would see an increased demand for investment wines, pushing up quality levels and producer income and promoting 'brand SA' worldwide. The investor would be able to purchase and trade icon wines made available through a secondary trade and potentially generate wealth.

There are very few 'downsides' to investment in SA wine. But, for this to happen, four things are necessary.

Firstly, there needs to be a greater recognition of SA's *icon wines*, especially abroad, and an acceptance of their inherent quality and longevity.

Secondly, there needs to be an *en primeur* offering of such wines to maximise profit potential for investors and make future returns more likely.

Thirdly, there needs to be a *platform* for the buying and selling of such wines on a secondary market via auctions or private sales (and a review of legal issues surrounding this).

Lastly, there needs to be more people successfully investing in (European) wine as an asset and that could lead to people *brave enough* to pioneer the investment in SA fine wines; to be the first to invest money into holding and trading SA wine with a return maybe years away.

A risk, yes, but less than many other asset classes and offering, perhaps, returns in double digits or at least something nice to drink.

> 'Wine should always be savoured, but those who choose to both save and savour wine may be making a wise decision after all' (Fogarty, 2006).

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Appendices

Appendix A Interview with **Emile den Dulk**

Why is there currently little or no investment in SA wines?

There is no wine culture. SA's wine history is one of control. The KWV did an effective job of controlling wine and wine drinking in SA. It meant there were no big wineries (except co-ops, whose wine was variable) and no real export until 2004. Even now, three co-ops have some 80% of the market. We have a beer culture.

But no trading facilities for SA wines?

En primeur here could work, only for a handful of wines. We will be doing en primeur next year on an estate wine, not under the De Toren name. This will be an icon wine, launched internationally (there's a lack of market here for this sort of wine). It will raise our profile abroad and it will take SA wines to another level, raising the profile of all SA wines. I don't resent Parker's influence and I've invited his SA contributor (see 8.2.4) **to taste my wines in barrel. We need to positively promote our wines on the world stage and Parker is a way to do this.**

What do you feel is an icon wine ?

An icon wine is determined by marketing, ratings and price. To me, an icon wine is 'made', not manufactured. It means low yields, manicured vines, hand destemming, absolute commitment. SA has no world icon wines; it's because of little marketing abroad, not enough overseas ratings and too low a price. Any marketing in key countries such as the UK has been for the commercial end of the market and has damaged chances of establishing icon wines.

And what hope is there for future wine investment?

Difficult. SA wines have no access to distribution channels. SA wines are not big enough abroad. It will need much better distribution. More capital as well. It takes a huge amount of capital investment to take a wine from 92 points to 95 points. You might need a separate cellar just to do MLF treatments, for example. Most wineries don't have that capital. Figures show that last year wineries had an average turnover of R40m, but the average winery only made R200,000 profit.

Appendix B Interview with **Ken Forrester**

Why is there currently little or no investment in SA wines?

Firstly, there is not enough market size. In SA there are probably only 3m white and 200,000 black South Africans who are economically active, perhaps 20% of that population would be active wine drinkers who might consider investing. That's about 600,000 people - it's tiny compared to European markets or the US or Asia.

Also, there is not an educated wine drinking market here. People don't have discerning palates.

And there is declining wine consumption. So, there are fewer drinkers drinking less wine.

And no trading facilities for SA wines?

SA wines are currently trading at about 1/10th of their international real value, judged on quality compared to foreign wines. Because prices are cheap there is not enough margin in SA wines. To receive 20% return on a wine you need expensive wines to make it worthwhile. 20% on a R30 bottle is R6 – not attractive enough. 20% return on a R500 wine is R100, that's more attractive.

This creates another problem, one of entitlement. Because wines are cheap, people expect them to be, and stay, cheap. People feel entitled to cheap wine, especially living amongst vineyards. There is a resistance to increasing prices – even though wines are better, vines are replaced, costs have increased. Look at the reaction to the R1000 wines out there, but a Margaux would cost you six times that.

There is also a view of people overseas that SA wines are cheap ie poor quality. This is an historical problem, going back decades.

As an experienced restaurateur, can I ask why the on-trade doesn't use auctions or the secondary trade ?

The restaurant trade is probably divided up so that 50% of the trade is in Gauteng, 20% in Cape Town, 15% the Garden Route, 15% KZN. So some areas have most of the trade.

Consider Cape Town. The competition is fierce. There are about 4,000 restaurants for about 120,000 regular clientele. That means some 30 regulars for each restaurant, so imagine what that means each week or month? Why invest in expensive wines which might or might not sell – especially in hard times ? And why buy foreign wines when people will look for the cheaper local alternative ? I've been told the One & Only in

CT has still got 2/3rds of the foreign wines it bought on opening still on its shelves after more than two years and they are fantastic wines.

Also, most on-trades are tied into distributors' contracts. That means they buy from a list – however restricted it might be. Most owners wouldn't buy at auction, especially if it undercut agent's prices.

Auctions here at present wouldn't answer this, the Nederberg (auction) is an example. It wouldn't meet on-trade needs, some 70% of the wines there are Nederberg's (Distell's) own.

Appendix C Interview with **Bennie Howard CWM**

Why is there currently little or no investment in SA wines?

SA's wine history is still in minds. The trade is very price conscious. The quality of a wine does not determine its price. This is a leftover from the days of the KWV. Price controls lasted until the 90's. Then, 70 co-ops produced on the basis of a minimum price, quality was not a concern. When international markets opened up to SA many saw it as a chance to dump poor quality wine overseas to get rid of excess. Foreign markets probably still see SA as a mass producer of average or poor wine. But in Sweden, where the state monopoly of alcohol prevented the dumping of wine into the country SA has had real success because they selected on the basis of quality / price. On this basis SA has been the number one imported country for the last three years.

Also, there is no cohesive view of how to sell SA wine overseas and not enough quality wines to show. There is also a lack of understanding of how to position our top wines against those of, say, Australia.

As a consultant to the Nederberg Auction, can I ask how this impacts on investment wine ?

Well, its volumes are too small to impact market prices, but it gives other benefits. It gives the producer an idea of what the trade will pay for their older wines and how sought after they are. It also creates a confidence in the brand and that the trade believes and has confidence in older wines.

Appendix D Interview with **Dave Hughes Hon. CWM**

Why is there currently little or no investment in SA wines?

It is largely because of our history. Before the Second World War, we drank European wines. By the 1960's, the strengthening of the Rand, from R2 to the GB Pound to R20 meant that those wines became expensive and there was a bit of a red wine boom of SA wines. But those wines, before, say, 1973 were poorly made and didn't keep. This was partly because of poor corks and anyway, wine was bought and drunk straightaway. Also, the law prevented anyone selling wine without a licence and this restricted purchase and consumption. SA doesn't really have a wine culture.

Since the 80's though, things have changed?

Wine drinking only began in the 60's, and only in the last 20 years has wine been good enough to keep. People are more aware of storing wine better at home and some wineries began to store for the customer, such as the Bergkelder.

But no trading facilities for wine?

There are no wine auctions, perhaps because of the years of poor wines, they are allowed to sell deceased estate wines and to bona fide collectors. It shows how bad laws were in preventing investment in domestic wine, the lifting of Prohibition was only in 1961.

And what hope is there for future wine investment?

People will have to spend more on wine. More on imported foreign wines. Top wines have to develop a performance level thus creating icon wines but at the moment there is still no wine culture here.

Appendix E Interview with **Johann Krige**

Why is there currently little or no investment in SA wines?

One of the problems is credibility of SA wines as investment wines. Even Bordeaux has problems at the moment, the Chinese bailed out the Bordeaux system and saved en primeur from collapse.

Also, South Africans don't understand en primeur.

And no trading facilities for wine?

We were one of the first to offer en primeur. In 1987 we offered futures but we stopped in ’92. The problem was logistics. Some of the wine owners couldn’t be traced, some had moved away, some might have died, but we couldn’t contact them on the details we had. We were left with 4,000 cases taking up room in the cellars and wasting time and money in admin. We should have used négociants. Even today most of those people haven’t been in touch.

What happened to the wine?

We still have some of it. The problem was we couldn’t sell it because it wasn’t ours, technically. We’ve got around that and sold most of it, but if the owners came back now we could still sort them out.

And what hope is there for future wine investment?

We’re selling futures again. But this time through négociants. Once we deliver the wine to the négociants that’s the last we’ll have to do with it. We are winemakers, that is what we should be doing. We have three brokers selling the wine, the Black Label Pinotage. We are selling the ’06, ’07,’08,’10 and 2011 then we will sell from barrel. By then the wine will have proven itself and have quality credibility, so by 2012 we will sell in one tranche. Eventually we will sell the Paul Sauer as en primeur too.

Within five years there will be several wineries selling en primeur. There are enough top SA wines now to justify it.

And a big enough market ?

It is a small market, but top wines still sell out. Several wineries could sell on a secondary market now. We could sell some wines several times over. We sell lots of fine wine to black South Africans – potentially the biggest market - and prominent black South Africans and think this will continue and increase.

Appendix F Interview with **Roland Peens**

Why is there currently little or no investment in SA wines?

There are several reasons for this. SA has no history of fine wines, it needs 50 or 60 years to build this up. SA has no generally accepted icon wines, accepted here or internationally. Apartheid made it difficult for international and domestic society to have access to SA wine and helped create attitudes towards SA wine which still linger. Wines were of poor quality and short lifespan, people had little confidence in

the product and there was a lack of awareness of wine quality and vintage variation. Only since the 90's have attitudes been changing and the public become aware of wine. SA winemakers need to look outward, to look at the best around the world.

But no trading facilities for wine?

There is no trading platform for wine. People want young wine, ready to drink tonight. Old wines are hard to sell and aren't kept. There is no 'in bond' storage here. You are not allowed to keep wine in bond more than one year which puts pressure on businesses. Also there is a double VAT jeopardy whereby the buyer (me) **pays VAT then brokers on and has to add VAT in order to get the VAT I paid on the wine back, as the purchaser is probably not VAT registered so I can't reclaim it back from them. This means VAT is paid twice and this makes the wine more expensive. You can add R10-R30 per bottle costs on any wine brought in to SA before VAT.**

And what hope is there for future wine investment?

There are probably only 2000 potential investors in SA. The market is small. We sold 450 cases of wine last year (2010)**. Farr Vintners in the UK sold 150 times that much. Also, allocations are a problem, established players have most of the market. Our allocation of Château Ausone was three bottles, only four bottles of DRC were sent for the whole SA market. Not many people invest in foreign wines either. Investment needs to see returns of 10-15% to be worthwhile. That won't happen with SA wines. Supply is bigger than demand, there is no scarcity value, it shouldn't be so easy to buy SA icon wines, it is too easy.**

Appendix G Telephone interview with **Norma Ratcliffe**

Why is there currently little or no investment in SA wines?

It may be partly because there has been disappointment. Not just with vintage variation or poor quality wines in the past, but because we don't store wines properly. People don't have wine storage at home so don't buy wines to keep. We get people asking us for older vintages, which we sometimes have, so they can drink the wine immediately.

Some 6-7% of the market is fine wines – not very much, and Johannesburg is where the market is.

But no trading facilities for wine?

There is no way forward for SA wines at auction. Investors, and buyers, are going direct to producers, they don't bother with auctions.

And what hope is there for future wine investment?

Maybe en primeur would be good for investment purposes. We don't need it at Warwick, we can sell all we want from the cellar door or to regular buyers. We don't need to look at futures

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Appendix H Telephone interview with **Eben Sadie**

Why is there currently little or no investment in SA wines?

Lack of consistency. Bordeaux, the centre of the trade, has shown consistency over time, a very long time. Kanonkop Paul Sauer is the only SA wine that can show any consistency over time. It takes some 20 years to show consistency, and even then the world won't take us seriously. It takes 20 years to make a great wine and three generations to erase bad opinions of SA wine. Even now the US doesn't see SA as making any high end wine.

Your wine is thought to be a future investment wine. Is this pleasing ?

I don't want people to buy my wine to sell. I want them to drink it.

Your wines win lots of awards, including Columella getting 95 'Parker' points three times ?

I make wine to drink, we don't run after awards. We don't play the award game. Thank God SA winemakers don't run after awards like California ! We've withdrawn our wines from sale in the US – we are not looking for prizes. Selling on the tail of achievement is risky. We don't take our wines around the world looking for shows, we do five tastings in the countries of our agents and that's it. Anyway, 95 points now is not enough to really get noticed, now you need 98 or 99 points.

Appendix I Interview with **Beyers Truter**

Does SA have any icon wines ?

There are lots…I had a Tassenberg red recently, under cork, from 1969, and it was delightful, unbelievable. People are too scared to name SA icons, like the Kanonkop

Paul Sauer. It takes time to become an icon, maybe 20 years of quality. An icon wine to me is 'time over price over quality'. There are many more icons than people think, like Neil Ellis, Steytler Vision, Boekenhoutskloof, Galpin Peak, my own 'Diesel', LeRiche…

I wanted to introduce a Grand Cru, 1er Cru, 2nd Cru system for the Pinotage Association to establish quality levels and get people to fight for wine improvement, but it didn't happen.

Why is there currently little or no investment in SA wines?

I think we're missing out. I missed out in 1986. Jan Coetzee wanted me to go halves with him in buying 300 cases of Kanonkop's Paul Sauer en primeur at R87 a case. It meant parting with R13,000. I didn't and then it got rave reviews and within four months was selling at R400 a case. I could have made R47,000 profit – and that was in 1987!

I thought about doing it with my own stock, it could sell for much higher prices, but I can't, or won't hold stock back to sell later for a higher price, it would upset my customers – it's basically screwing them. 'Diesel' Pinotage could easily sell at R750 a bottle a year or two after initial release.

And what hope is there for future wine investment?

There is a secondary trade market, I can prove it, I just haven't made any money out of it. A futures market is coming, but only for some wineries.

Do you mean like the Cape Winemakers Guild auctions?

Yes. Some wanted it to create a secondary trade. But you could argue things have changed and ask how genuine it is in its original intent. I do it for charity, but it is a lot of hard work. For some wine farms it is absolutely necessary to sell their wines and raise their profile. For them it is a shop window.
