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GRAPE PRICING

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In order to maintain equal footing with producers in today's competitive wine market, Napa Valley grape growers need to change the way in which grape contracts are negotiated. "Growers need to relate to the end product — the bottle of wine — instead of the size of the crop, which is generally how agricultural contracts have been negotiated for decades," says Andy Beckstoffer, largest independent grower in Northern California.

Grape growers need to take into account the cost of Investment and business risks as well as what the bottle of wine that contains their grapes is retailing for when they negotiate with vintners new pricing contracts that could extend into the next century.

That was the message area growers heard at a well-attended contracts seminar conducted Tuesday afternoon by the Napa Valley Grape Growers Association.

Urging growers to scrap outdated pricing formulas, Beckstoffer said the timeworn practice of using grape prices from the prior harvest to negotiate the crush at hand "is out of touch with reality."

A founding member of the Napa Valley Grape Growers Association and a member of its board of directors, Beckstoffer said there's little doubt grape prices will increase in '96, '97 and maybe even '98.

Some in the industry believe the most realistic scenario has prices for top chardonnay, merlot and cabernet sauvignon reaching $2,000 a ton by the next crush.

As an example, Beckstoffer showed those attending Tuesday's meeting the wide range of prices paid for Napa Valley cabernet sauvignon in 1994 alone. While the average amount was $1,465 per ton, one grower was paid $500, another $3,500.

In '94, five buyers controlled 26 percent of the local cabernet sauvignon crop and most bought grapes at below-average prices.

Recent surveys of industry members reveal profits are up for more than 80 percent of respondents, while nearly two-thirds of the vintners surveyed by Wine Business Monthly said they were eliminating discounts and raising bottle prices.

To support his claim of need for a change in grape pricing methods, Beckstoffer pointed to a decline in prices paid per ton for cabernet sauvignon, merlot and chardonnay the past three years while sales of those varietals have grown by 20 to 40 percent.

"If a winery comes to you and says you've got good grapes and they want 'em, how do you negotiate the price?," he posed. The man who sells grapes to more than 30 wineries, Beckstoffer suggests vineyard investment expenses, the annual cost of farming the land and the grower's desired return on investment need to be factored into a proposed formula for coming up with the desired price per ton of grapes — a figure that must be reached prior to entering into negotiations with winery representatives.

Beckstoffer put a price on bare land and added in present-day development and ongoing costs, suggesting a 9 percent return on Investment. Another panelist, certified public accountant Dave Brotemarkle, suggested return on investment at 15 percent to take into account the risks of farming.

Once the grower determines the revenue needed per acre to support a 9 percent return, then it’s time to negotiate grape prices, Beckstoffer said.

If a winery agrees to provide the grower with that per acre revenue, then it's the winery taking the annual risk of grape yield.

The grower could take on that risk, dividing his desired revenue per acre by yield per acre, whether annual expected yield is four tons or eight tons.

Beckstoffer proposed a few ways in which to negotiate a long-term contract that stabilizes grape prices, eliminating the necessity of yearly contract talks.

He feels the best method employs a bottle pricing formula. If the bottle of wine is to retail for $15, then the grape price could be 100 times that retail price, or $1,500 per ton. The formula could be negotiated at 80 or 90 times the retail price, tying the price of grapes to the winery's economic progress, he added. And the price per ton could fluctuate as bottle prices went up or down.

"For every $100 added to the price of grapes, you add $1.43 to the cost of a bottle of wine," Beckstoffer added. "On average, a ton of grapes produces 700 bottles of wine."

'To produce a premium case of wine in the Napa Valley costs $50 or less," he said.

A recent analysis by industry watchdog George Schofield has the cost of producing a case of wine at the Robert Mondavi Winery at 50 percent of its wholesale case price, at Chalone 60 percent.

If a bottle of wine retails for $10, the winery is getting $60 wholesale, he added. If a bottle is priced at $15, the winery gets $90 per case, at $20 per bottle, $120 per case.

"You just can't put Napa Valley grapes in a $10 bottle of wine," he concluded.

Brotemarkle's figures were slightly different. He maintains paying $1,000 a ton for grapes means that bottle of wine has to wholesale for $8 and sell for at least $13 retail; $1,800 per ton relates to $10 and $20 bottle prices, respectively.

The Napa Valley Grape Growers Association first advocated the use of bottle pricing in the mid-1970s. It was adopted in '76 by Robert Mondavi, Schramsberg and the former Spring Mountain wineries.

"You should seek to share industry profitability, not drive the winery out of business or out of the county," Beckstoffer cautioned.

"I think the time has come to base grape pricing decisions on sound business practices requiring return on investment, not the unstable and out-of-touch prior year market averages."

Napa attorney Steve Buehl said it's important winery and grower speak the same language in contract negotiations.

"If in doubt, spell it out" in the contract, he urged.