The global vs. domestic wine industry

Tom Shelton

Tom Shelton is president and CEO of Joseph Phelps Vineyards and has over 30 years of experience in the wine industry. He served on the board of directors of the Napa Valley Vintners Association from 1996-2000 and served as president of the trade organization in 1999. As one of the founders of Free the Grapes, Shelton has endorsed reform of the mandatory three-tier system of wine distribution in the United States. He holds a Bachelor of Science degree in politics from Wake Forest University and took graduate course work at the University of Maryland.

Tom Shelton began his address to the Global Executive Forum by saying “California wineries are notoriously poor exporters.” The reason, he said, is because “the domestic markets have been so vibrant and the growth in those markets so robust that exporting was always an afterthought.”

When he started working at Joseph Phelps Vineyards in 1992 he pitched the idea of overseas markets to Joe Phelps and the board of directors. They asked him, “Why do you want to do that?” After all, it takes time and money to pursue the global export trade.

“The globalization of our wine industry demands that we attack the export markets in a serious way. I’ve had a hard time convincing my board of directors of how important this is,” said Shelton. “I personally believe that we should be spending a lot more of our resources on export.”

He has been successful to some extent. “Our exports have grown from virtually nothing to about 15 percent of our business today.” He would like to see that number increase to 25-30 percent. “We’ve expanded our relationships to 26 different countries and we’ve been very aggressive in trying to develop more countries.”

The wine business in the United States is relationship-driven, a “belly-to-belly business,” said Shelton. “Relationships are even more important when I travel the export markets.”

Shelton said many of his longtime customers have become personal friends whom he visits every year, squeaking out enough dollars from the budget to allow him to travel. He also invests money in customers’ markets by bringing over their top sales people to visit Napa Valley. “It is very important for us to be able to continue those kinds of activities but it has been difficult for small companies to do it.

Joseph Phelps is considered a small winery, producing about 100,000 cases a year. “At that level you really have to have a distribution network. You can’t do it yourself through mailing lists and things like that,” said Shelton. “There are probably about 10 wineries in that category in the Napa Valley.”

Consolidation is occurring in the wine industry just as it is in the beer industry and Shelton said he is concerned about the “future viability of independent producers. We find ourselves having to form strategic partnerships just to maintain our position.”

About five years ago, Shelton entered into a strategic partnership with Kobrand Corp. out of New York. “This is a marketing group that creates packages of similarly positioned brands to sell to export customers. That has worked fairly well for us and it’s one reaction to the globalization of the industry.

“We’re definitely feeling the pressure from these consolidations and not only in the export markets but in the domestic markets as well.
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The industry

Phelps provided an overview of the scope and worth of the wine industry. California is the fourth largest wine producer in the world and the fourth largest world market in terms of consumption, said Shelton. “Although wine is produced in all 50 states, 95 percent of wine exports from America come out of California where the industry has created about 207,000 full time jobs.”

The industry’s annual economic impact on the state is $45.4 billion; it has grown nearly 40 percent from 1998 to 2002 according to a report from MKF Research for the Wine Institute and California Association of Winegrape Growers.

“One of the problems we see for the medium sized domestic producer is that ever country is trying to get into wine production in a very significant way and they all look to the US market for their sales,” said Shelton. Chile and South Africa are very aggressive and Europe has owned a significant portion of the US marketplace for a long, long time. However, European brands in the US are declining at a very rapid rate as consumers switch to Australian and Chilean wines.

Australia is becoming one of the largest wine producing nations on the planet. They export about 85 percent of their production. Foster of Australia was having a difficult time accessing American markets so they bought the Beringer brand which gave them a good distribution network in the US. Fosters paid a premium for the brand but in some cases the value of the network is more important than the value of the brand.”

The European Union currently represents the largest export opportunity for the US. The value of US exports is $794 million right now, which seems small but it has been growing at 20-25 percent annually.

“When the dollar was strong, we were really suffering. In 2001 and 2002, Joseph Phelps Exports declined precipitously due to the high value of the dollar and the Iraq war. When the US went into Iraq our sales in Europe went right to the floor and Phelps has not yet recovered in that market. Canada is our strongest export market right now followed by the UK and Germany.”

Wine producers have to comply with different regulatory rules country to country. “The US has been working on what we call ‘mutual acceptance agreements’ which basically means that if you agree to accept our rules, we’ll agree to accept yours. All the new world producers are signing on to these agreements, with the exception of Europe,” said Shelton. “Europe wants their rules to apply and we don’t necessarily want to play by their rules.”

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