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Valuing 'Wines in Process' at Wineries

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Kelli Hunt, Commercial Underwriter

A Brief History of the Wine Industry in Canada

According to Norwegian sagas, Viking explorer Leif Ericsson discovered grapes when he landed on the American continent around 1001 AD. He named the place Vinland. Although speculation continues as to whether Leif found blueberries or grapes at his landfall in Newfoundland, it is certain that wild grapes grew along the eastern seaboard of North America. Johann Schiller, who is acknowledged as the father of the Canadian wine industry, made good use of these grapes in the 19th century.

Schiller, a retired German corporal, was given a land grant just west of Toronto and in 1811 he planted a small vineyard from cuttings of wild vines he found growing along the banks of the Credit River. Schiller made wine from these domesticated grapes and sold it to his neighbours. Thirty-five years later the estate was bought by an aristocratic Frenchman, Justin de Courtenay, who had unsuccessfully tried to replicate the taste of red Burgundy in Quebec. He had better luck in Ontario and his Gamay won a prize at the 1867 Paris Exposition.[1]

Today there are over 700 licensed wineries in 9 Canadian provinces with the majority of the production coming from Southern Ontario and B.C.

In the alcohol beverage sector, wine ranks second in terms of economic value of production; after brewery products, table wines constitute the largest segment of the market, by a slight margin over distilled spirits.

According to Statistics Canada, production of vinifera grapes for processing, of which nearly all would be used in wineries, was 61 thousand metric tonnes in 2007.[2]

As the industry has grown the "typical" Canadian winery has become a very sophisticated and large business often with both domestic and international sales and as such the risk profile has changed dramatically.

Underwriting Canadian Wineries

Today's Canadian winery no longer consists of a small corrugated steel building with 5 acres of grapes. There are over 11,000 acres of grapes planted in the Niagara Region of Ontario alone and each winery usually includes production facilities as well as tasting areas and space to host large corporate and wedding events. These are multi-million dollar facilities that are often built of frame construction and to complicate things further they are usually located in semi or unprotected locations.

[1] Canadian Encyclopedia

[2] Statistics Canada

Not only have the values of the buildings and contents increased dramatically over the last 20 years but the wine in process (stock) has also increased as the wineries have grown in size and improved the quality of their product.

Stock is a critical issue for wineries since the production of wine can take months or even years to complete and the value of wines in process increases with each passing day.

At Signature Wine we recognize that just as a golf course is the most important asset to a golf club it is the wine that matters most to a winery. We have created the most comprehensive valuation and replacement options for wines in process but in order to properly protect our customers we need to fully understand the values and sales cycle at each winery.

Valuing Stock at a Canadian Winery

It is not uncommon for our underwriters to see wineries with stock limits over $25 million dollars as reported by the winery however when we drill down we usually discover that the values submitted are based on full retail selling prices and are not the proper representation of the true exposure to the winery.

When we receive a new submission we break the stock component down into two parts; 1) The value of stock by month and, 2) The various distribution channels where the wines will eventually be sold. Let's take a closer look at each component:

1) Monthly Value of Stock

Throughout the year as wines are finished and shipped or sold, the values of stock remaining at the winery will fluctuate. There can be swings of $1 million dollars or more from month to month and these changes must be identified in order to determine a proper value for insurance purposes. From a risk management perspective it is the average monthly value that should be utilized as opposed to the highest (or lowest) month. Below we have shown a monthly stock summary for our fictional winery, Justin Bieber Estates:

JUSTIN BEIBER ESTATE WINERY

Month	Litres (Bulk)	Retail Value	Litres (Bottled)	Retail Value	Total Retail Value
Jan	850,000	$34,000,000	210,000	$10,500,000	$44,500,000
Feb	820,000	$32,800,000	201,000	$10,050,000	$42,850,000
Mar	810,000	$32,400,000	175,000	$8,750,000	$41,150,000
April	780,000	$31,200,000	175,000	$8,750,000	$39,950,000
May	778,000	$31,120,000	175,000	$8,750,000	$39,870,000
June	670,000	$26,800,000	185,000	$9,250,000	$36,050,000
July	630,000	$25,200,000	220,000	$11,000,000	$36,200,000
Aug	540,000	$21,600,000	248,000	$12,400,000	$34,000,000
Sept	468,000	$18,720,000	202,000	$10,100,000	$28,820,000
Oct	440,000	$17,600,000	235,000	$11,750,000	$29,350,000

Month	Litres (Bulk)	Retail Value	Litres (Bottled)	Retail Value	Total Retail Value
Nov	965,000	$38,600,000	221,000	$11,050,000	$49,650,000
Dec	945,000	$37,800,000	201,000	$10,050,000	$47,850,000

As you can see the total value of stock ranged from $28.8 million in September all the way up to $49.6 million in November which is a spread of nearly $21 million dollars over the course of just 2 months.

In order to properly cover the stock at Mr. Beiber's winery we could either choose the highest value month and use that limit or we could average out the limits over 12 months and use the average amount. We prefer to average out the 12 months when underwriting because we believe this gives a better picture of the winery's assets at any given point and this way the winery is not being charged premium on a high dollar amount which might only be achieved for a few days out of the year.

In the example above the average monthly stock value is $39.2 million which is $10.4 million below the largest month (December) and nearly $11 million larger than the lowest month (September).

By using an average taken over the 12 months of the year we believe that the winery is properly protected with reasonable limits.

2) Distribution Channels

Canadian wineries typically have 4 distribution channels for wine sales:

1. Wholesale
2. Direct to Consumer
3. Direct to Restaurants
4. Export Market

It is important to breakdown the annual sales by each of these 4 main categories so that we can apply the right selling price to the wine.

For example, if Mr. Bieber sells a bottle of white wine to a customer visiting his winery he might get $15.00 however he will likely only get $5-$7 dollars for the same bottle of wine if it is sold through a large distributor such as the LCBO in Ontario or through the Liquor Distribution Branch (LDB) in British Columbia.

Most wineries sell the majority of their production through a large distributor and therefore the valuation calculation should be based on the wholesale price that the winery receives from the distributor and not the final retail selling price.

The remaining markets are usually much smaller by volume for wineries however they can be a meaningful part of the overall revenue because the margins are so much better.

Putting it All Together

By breaking down the annual production by month and then applying the right selling price we can arrive at a realistic limit that will properly protect the winery. In the example used in this report we see that a winery with retail stock values as high as $46 million would likely only require a limit of insurance in the $18 million dollar range in order to be fully and properly protected.

Conclusion

As you can see there is a lot of thought that must go into underwriting a winery. In addition to setting limits on the buildings and contents, setting a limit for wines in process or 'stock' is a critical factor that must be addressed carefully.

Going through this process with your winery customers will have a meaningful impact on the insureds bottom line while providing the peace of mind that comes with being protected.

By doing this exercise you will also demonstrate your knowledge of the wine industry and provide value added service to your customers.

For More Information

For more information about this bulletin or for questions regarding any of the commercial insurance programs available through Signature Risk Partners Inc., please contact:

Kelli Hunt
Commercial Underwriter
khunt@signaturerisk.com

Erin Symons
Director of Wine
esymons@signaturerisk.com

Signature Risk Partners Inc.
21 Price Street
Toronto, ON M4W 1Z1

email: info@signaturerisk.com
web: signaturerisk.com