

A Challenging Year for Washington Wine

Shipments of Packaged Wines (000s of Cases)

Out-of-State	8,658	8%
In-State Distributors	1,956	9%
Direct-to-Consumer	880	3%
In-State Retailers	169	16%
Total Shipments	11,663	8%

Shipments by Washington wineries declined by nearly 970,000 cases in 2020. This is based on Vintage Economics' preliminary analysis of Washington State Liquor and Cannabis Board data. Shipments primarily represent sales by wineries to distributors, retailers and consumers, though some transfers made prior to sale are included as well.

All sales channels were in the red in 2020. Distribution shipments, both to in-state and out-of-state customers, fell sharply. This suggests that surging chain store sales were not enough to offset the collapse in on-premise.

DtC held up better. An e-commerce spike nearly made up for tasting room losses, and almost half of Washington wineries reported gains in 2020. Nonetheless, the 3% drop (which may be revised up a bit) represents a sharp reversal from double-digit growth in 2019.

Following a severe first-half contraction, there was some recovery in the third quarter as wineries and consumers adapted to Covid-19. But a relapse occurred in the fourth as the virus surged again and restrictions were reenacted.

The aggregate figures on sales volume obscure important nuances. While the pandemic thrust

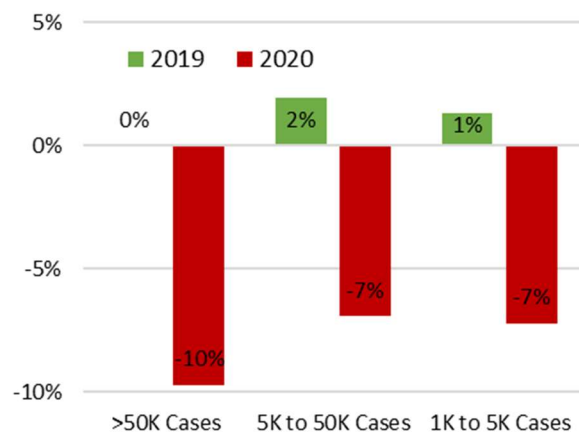
many wineries into distress, others thrived. Overall, four in ten reported volume gains in 2020 – compared to six in 2019 – a respectable performance given the circumstances.

Size didn't matter very much in 2020. Location mattered more. For example, a much greater share of Walla Walla wineries shifted from gains to losses in 2020 compared with those situated in Woodinville. This suggests that proximity to the large and affluent Seattle area consumer base was an asset relative to the more tourist dependent Walla Walla trade area.

Nonetheless, there were winners and losers across all sizes and geographies. Precept Wines, Washington's second largest producer, recorded a 12% increase in its case shipments and ten Walla Walla wineries saw gains of over 25%. Several emerging wineries, including Aquilini Wines, launched successful national brands despite the challenging environment.

Positioning going into the pandemic (strong retail brands, wine clubs and deep customer lists were assets) and the ability to pivot once it hit (with virtual tastings, phone sales, curbside pickup, etc.) appear to have been the definitive factors. Outdoor space was also an advantage in 2020 given restrictions on indoor activities.

Median Change in Shipments by Winery Size



2020 in Perspective

Washington appears to have underperformed the broader industry in 2020, though available data is limited and not strictly comparable. This suggests that some market share was lost. Nielsen data confirms this was the case in the retail stores it tracks.

It is important to recall that sales of Washington wine had been stagnant prior to the pandemic. The sudden change in trajectory that began in 2016 was mainly due to a reversal of fortunes at Ste. Michelle Wine Estates, Washington's dominant winery. It accounted for two of three cases of Washington wine sold in that year.

Washington's remaining wineries were able to pick up the slack in the ensuing years, but Covid-19 interrupted this dynamic. Shipments are down by more than a million cases from the 2016 peak and back to their level in 2014.

The sudden cessation of growth at Ste. Michelle led to a severe inventory glut and a structural imbalance between supply and demand for grapes, as growers had planted in advance of growth that never materialized.

Ste. Michelle began to initiate a "strategic reset" in 2019 and hired a new CEO in 2020. The company has taken steps to better align its supply with sales, including the disposal of excess bulk wine and grape contract buy-downs. It also introduced several successful new product lines in 2020 including canned and boxed wines. Nonetheless, SMWE's future trajectory remains uncertain.

While the outlook is still tenuous, the worst of the pandemic has likely passed and Washington wineries should benefit from an easing of restrictions and economic rebound. However, wine consumption is likely to remain relatively flat – though there will be a "re-shifting" of sales across channels.

Washington's smaller wineries should profit from a recovery in on-premise and tasting room sales in 2021, but distribution is likely to remain challenging. The state's large wineries will have to battle for share in a crowded marketplace. A solid performance from Ste. Michelle will be needed if the industry is to regain the ground it lost in 2020.

Total Shipments (000s of Cases)



Grape Market Update

The oversupplied grape market has triggered some slippage in prices for mainstream red varieties (particularly Cabernet Sauvignon) grown for mass-market bottlings by larger producers. White varieties are generally better positioned.

The “boutique” side of the market remains firmer, although the pandemic has forced some small wineries to reduce their grape purchases. A number of less planted varieties that make attractive wine club wines are in shorter supply.

There was some progress on the inventory front in 2020, mostly due to a small 2019 crush and the disposal of excess bulk. Though firm numbers are not yet available, the situation appears to have improved further in recent months due to an even lighter 2020 harvest and an acceleration in bulk wine sales.

The 2020 grape crush will come in at around 175,000 tons – a decline of one-third relative to the last “normal” harvest in 2018 – and the smallest since 2011. The lighter than expected harvest was due to a combination to poor fruit set, potential smoke exposure, and economic factors. On the plus side, quality is excellent.

Despite two consecutive small harvests and a reduction in inventory, the structural gap between supply and demand remains.

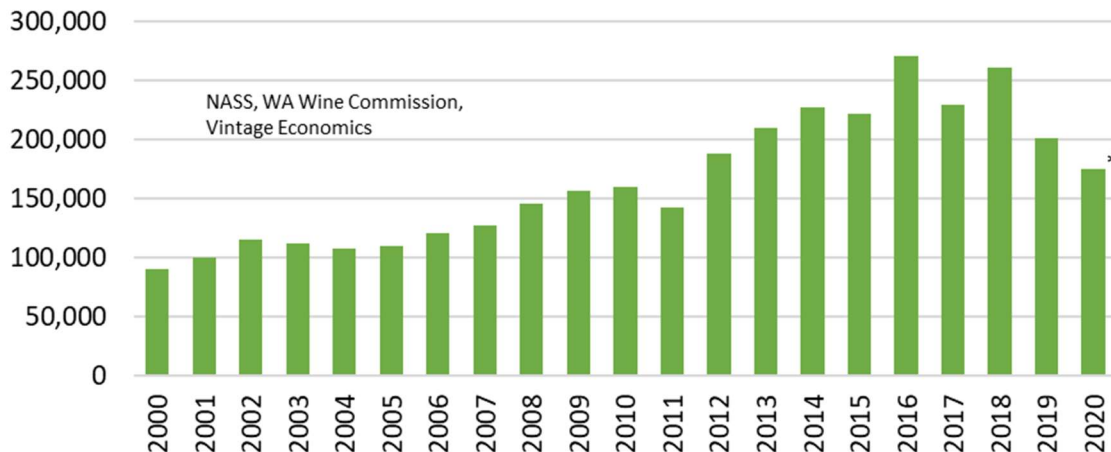
At pre-pandemic sales levels, wineries need approximately 220,000 tons of fruit per year to satisfy consumer demand. Current bearing acreage looks to be capable of producing just north of 250,000 tons per year on average.

This implies that either wine sales need to grow by about two million cases per year or reduce acreage substantially. These back of the envelope calculations are intended to be illustrative only, as there is considerable margin for error on both sides of the equation.

Given recent shipment trends and a competitive marketplace, it is unlikely that demand growth alone will be able to close the gap in a timely manner. And there are no obvious alternative uses for many sites at this point, so vineyard removals will likely be slow as well.

This suggests there will likely be at least a few more lean years ahead for growers focused on the “commodity” side of the market. Though as we saw in 2020 – anything can happen.

Washington Grape Crush (tons)



About Vintage Economics

Vintage Economics is market research and consulting firm focused on the wine industry. The firm is dedicated to providing insightful market research and analytics to help clients make better informed and more strategic decisions and position their businesses for success in a rapidly evolving and increasingly competitive market environment. Areas of expertise include market analysis and forecasting, strategic research, and data analytics.

Vintage Economics also supplies analytical reports and customized metrics and intelligence on the the Washington wine industry, including production and shipments by channel for individual wineries.

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