And wine not: make your mark with an astute purchase

INVESTMENT CONCEPTS » Strange as it may seem, there are many parallels to be drawn between investment and wine

Wine as investment allegory

BRYCE SANDERS

Sometimes prospects with assets to invest may be unfamiliar with the equities markets. Perhaps they inherited a sum, or their windfall came from the sale of property. Communicating investment concepts and building trust can be difficult. This can be easier if you can relate the strategies to other familiar concepts. Many good prospects are also fine wine fans. Utilise their knowledge and appreciation of wine as a way to communicate investment concepts.

Eight investment lessons

1 Past performance is no guarantee of future results – red Bordeaux is an easier wine category to understand because of the 1855 Classification. (That year, the Bordeaux Chamber of Commerce issued a 5 level classification of 60 or more wines with remarkable little change to the list over 151 years.) Subsequent evaluations have been done by wine experts and other authorities however the 1855 classification is the most respected. Over the past 151 years, properties have been sold, acreage has changed and different winemakers have utilised new techniques.

The lesson: times have changed. Past performance is no guarantee of future results.

2 The manager can make the difference – prices vary enormously from vineyard to vineyard in Bordeaux and other wine areas. The wine comes from the same types of grapes grown in the same town in the same year and under the same weather conditions. Why will some wines sell for twice, three times, five or seven times the price? The skill of the winemaker often plays an important role. For example, one winemaker may have invested in advanced equipment and technology when their neighbour may be making wine the same way they did 50 years ago. In difficult years, the winemaker utilising new technologies may produce a tastier wine than the neighbour.

The lesson: this can help make the case why different unit trusts or money managers in the same style and size category have different results. Same stock universe, same market climate – the difference may be the people managing the money and choosing the stocks.

3 Diversification and asset allocation can improve returns – a varietal wine is made from one grape type. For example, in Burgundy, pinot noir is the primary red wine grape. (Gamay is used in Beaujolais. Although classified Burgundy, wine fans usually consider it as a different category.) If Pinot Noir did not do well that year, the winemaker's options are severely limited. This is similar to a sector fund in the equity markets. A wine like Chateauneuf du Pape in the Southern Rhone region of France can use up to 13 grape varieties in the blend.

If one grape type did not ripen well, the winemaker may increase the proportion of the other to make better wine. This is similar to a unit trust in a broader category such as large cap, value, global or asset allocation funds.

The lesson: asset allocation and diversification can increase the probability of getting better returns in a difficult market year.

4 Expert opinions – Robert Parker, Jancis Robinson, Michael Broadbent and Stephen Spurrier are familiar names to many wine fans. Critics like Mr Parker grade wines on a 100 point scale. 90 points or more often creates huge demand for a wine. He rates wines region by region and vintage, for famous wine regions and up-and-coming regions around the world. As a professional, he has the time and resources to conduct research that would be time-consuming for most consumers. Most wine fans regularly find a high-scoring wine from a little-known region and share it with friends.

The lesson: analysts and economists are the financial services industry equivalent of wine experts. You have access to their expertise and can bring ideas about up and coming companies to your client's attention. This is one example of how you bring value to the relationship.

5 Buy when good companies are out of favour – red Bordeaux used to have great, average and poor years. Technology has helped winemakers almost to eliminate poor years. They can produce tasty wine, although the quantity available may be less. Pricing has not caught up yet. For example, 2003 Haut Brion (red Bordeaux from the Graves region) is quoted around £150 for a bottle. 2002 Haut Brion was recently selling for about £60 per bottle. Same grapevines, same soil, same winemaker – but different year – and different weather conditions. The 2002 sold for less than 40 per cent of the 2003. For a wine drinker buying for personal enjoyment, the 2002 may not be as sublime as the 2003; it may not age as long. However, it is the same first growth chateau at a fraction of the price.

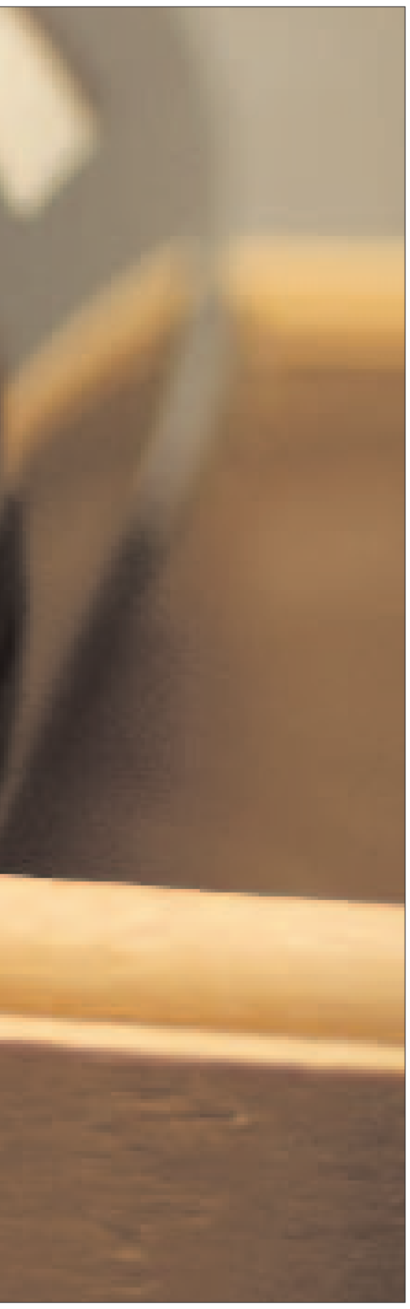
The lesson: good companies with good management come into and out of favour. If the business concept makes sense, the management is sound and the price is low, it may be time to buy.

It takes time

6 It takes time to get results – fine red wine is known for improving with age. Traditionally, red Bordeaux was bought and stored (laid down) for five to 10 years before it was considered ready to drink. Today, many wines are made in a more approachable style that provides enjoyable drinking today. However, fine red wines usually improve over five to 10 years.

The lesson: fine wine can be like zero coupon bonds, the type that are purchased at a deep discount and pay no interest to the holder during the life of the bond. At maturity, the bond pays off at face value, providing the bondholder with a compounded rate of return that does not change assuming the bond is held to maturity. This requires patience, like letting your red Bordeaux mature in the cellar until it is ready to drink.

A disadvantage of the stock market is the publication of share prices daily in the newspaper and on the internet. People have easy access to updated



Analysts and economists are the financial services industry equivalent of wine experts. You have access to their expertise and can bring ideas about up-and-coming companies to your client's attention

pricing and often expect to see quick results. Patience is a virtue.

7 Cult wines – first growth Bordeaux wines have been in demand for years, but a new wave of cult wines is being sought out by collectors and driving the prices up. You may have heard of California cult wines which can command prices in excess of £550 a bottle at auction (garage wines in France also command high prices). Collectors want these bottles for their collections – they are trophy wines. The wines are often awarded high scores by wine critics. Wine fans can own them but the price can be high. Everybody wants a good wine to drink but how much are they prepared to pay?

The lesson: The dot.com crash happened when high-tech stocks were bid up to stratospheric levels in the late 1990s. Some investors felt the old rules about buying on fundamentals did not apply. If a client wants to buy a hot stock, discuss the fundamentals. Ask them to articulate why they feel the stock will continue to rise in price.

8 Doing it yourself – sometimes prospects balk at fees. In these days of discount brokers, online trading and no-load funds, they feel they can do it themselves. When wine fans hear about high opening prices on 2005 red Bordeaux they may consider buying a few cases instead of investing their money with you.

The lesson: this is an ideal opportunity to show your relative value. Assume the prospect bought wine at auction, held it for a few years and sold it again at auction. What are the transaction costs? In the US, the Buyers Premium can be 17.5 per cent. Storage costs also apply. There is a cost to sell. Do not forget the spread between bid and offer. When you arrive at a total compare it to the cost of doing business with your firm.

The comparison is easier if you offer professional money management at a flat percentage based on assets under management or another form of wrap fee structure. Your equity and fixed income suggestions may also include income paid from dividends and interest. Their wine in storage does not. You need to cover transaction costs and spreads before you begin to make money.

Wine can provide access

Wine is a passion for many people. They may not be eager to discuss investing with a social acquaintance. However, they may consider wine a passion to share. Here are a few idea on how wine helps cultivate a personal relationship:

- Saving money – an interesting characteristic of most wealthy people is that they want to stay that way. If you can help save them money, they usually have an interest in talking to you. Wine is an inefficient market in many ways. Vintages of the same wine are priced differently, based on variables such as weather, critic's reviews and demand. Wine merchants have a limited amount of display and storage space. Lots of money can be tied up in inventory. When a new vintage comes in, they must put it somewhere. They may run sales on Bordeaux wines from less popular years. These can be real bargains. Find a good deal on a wine a friend collects and you have done them a favour. You may even go to buy it together.
- Getting together – wine fans love tasting different wines. New wine bars open up. Wine stores have tastings. Wine magazines organize consumer shows. Community organisations run wine and cheese events. These are all opportunities for an evening out and sharing a common interest. Often prospects want to get to know you as a person, determine if they like and trust you before they agree to become a client.
- Wine makes a statement – you are probably invited to friends' houses for parties all the time. What do you bring? Many people bring a bottle of wine. The bottle becomes part of an anonymous forest of other bottles on a gift table, or is opened as one of the party wines. Consider buying wine in a large format bottle such as a three-litre double magnum. Not jug wines or box wines, they are oversized versions of single bottles that make a statement because of their size and the effort required to open them.

Wines from Chile, Australia, Italy and California often come in large formats and the prices can be reasonable, within the range of what you would spend on a gift for a friend. Consider bringing a pen that writes on glass as part of the gift – other guests can autograph the bottle.

Bryce Sanders is president of Perceptive Business Solutions