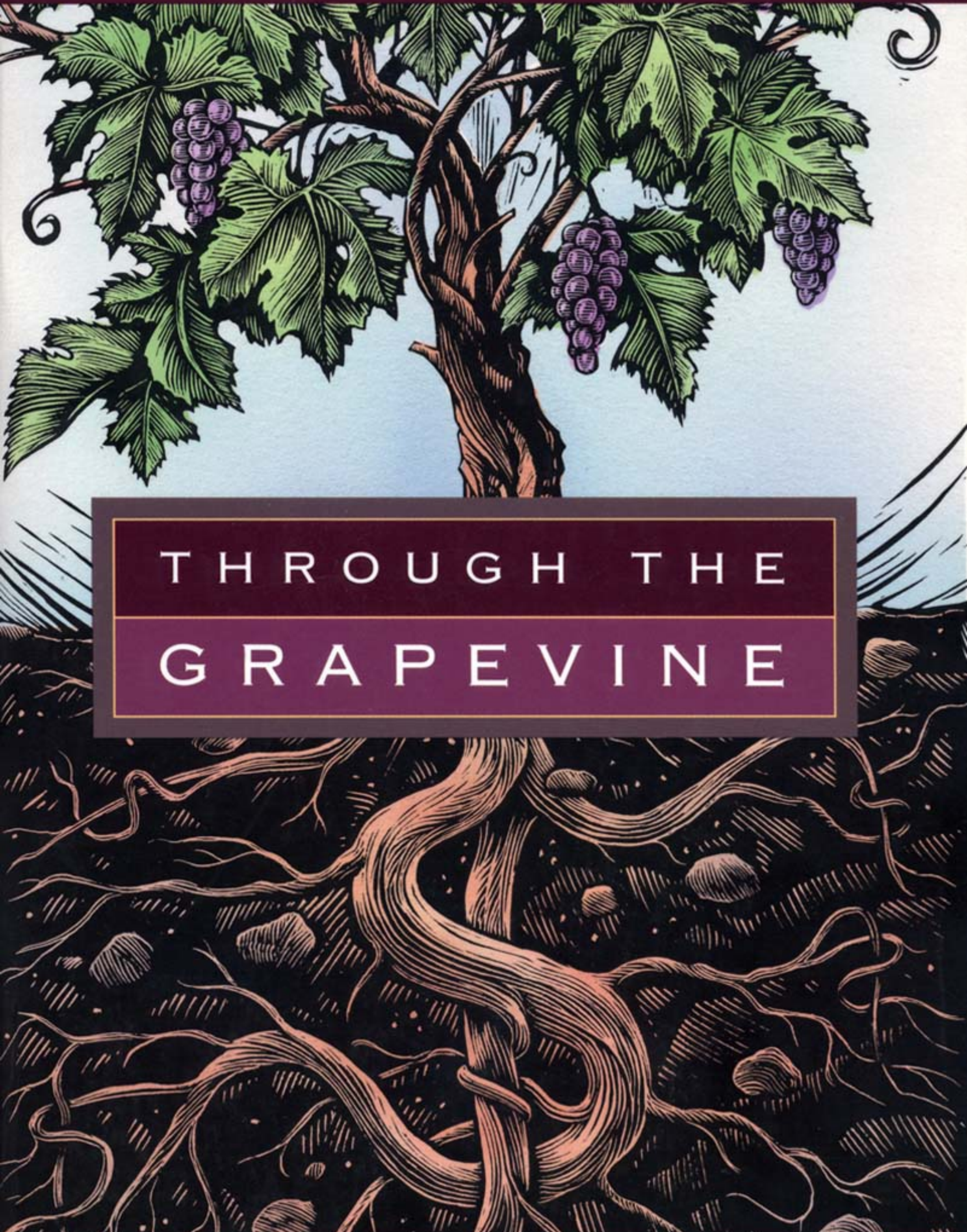
THE REAL STORY BEHIND AMERICA'S EIGHT BILLION DOLLAR WINE INDUSTRY

THROUGH THE GRAPEVINE



JAY STULLER & GLEN MARTIN

"A RAPID-FIRE, BEHIND THE SCENES TOUR." - SAN FRANCISCO CHRONICLE

CHAPTER ONE

What Makes and Breaks a Winery

P*roclaimed a genius sometime around 1973, Francis Mahoney fig*ured he had the wine business whipped. Just a couple of years after the native San Franciscan purchased ten acres in the Sonoma area, planted a vineyard, and began making limited quantities of exceptional Chardonnay and Pinot Noir, he found himself on expense-paid flights to New York. Put up in elegant suites, Mahoney had only to talk to wine merchants and wine lovers about his stunning new Carneros Creek vintages and bask in the praise.

Before the age of thirty, this former wine importer and retail salesman was a star. A level-headed man, who took this "genius" business with equanimity, Mahoney nonetheless sold every drop of wine he could produce. For nearly a decade, Francis Mahoney and Carneros Creek made all the right moves.

He then made one grievous mistake in judgment that nearly destroyed his winery. Business school grad students are rarely warned about such miscalculation. At its heart it wasn't even financially oriented, although the fallout cost him plenty. But Mahoney's singular bad move is instructive enough to serve as a wine industry metaphor.

Until Carneros Creek ran aground, Mahoney rode a rather heady business wave. From his work at Connoisseur Wine Imports, he'd come to understand wine. He could also see that as the Baby Boom generation came of age and affluence, it would develop a taste for finer wine, leaving behind the Pink Ripple and soda drinks that appealed to collegiate palates and budgets. A seemingly endless stream of young Americans had traveled through Europe in the late 1960s and early 1970s, seeking good times and finding a surfeit of cheap but high quality wines. Back in the United States, they found the wine market dominated by undistinguished jugs of Paul Masson, Gallo, and Italian Swiss Colony.

There were a few producers of decent wines, among them Louis Martini, Charles Krug, Freemark Abbey, and Robert Mondavi. But for every half-decent vintner, there were counters such as the flagging Beringer operation, a business on the ropes, selling what Mahoney felt was "an outrageously bad product." And yet Mahoney also noted the emergence of some superb but very small California wineries, including Ridge and Mayacamas.

He and his partner, Balfour Gibson, knew that a small operation, making wines that truly reflected the attributes of a given grape, could appeal to a thirsty market. The big operations either didn't have the grapes of requisite quality, ignored this potential market segment, or didn't have the slightest idea it even existed.

Mahoney didn't have to worry about large-scale economies. Unlike many others who built wineries at the time and shortly thereafter—the dabbling doctors, lawyers, and others seeking the romance of tax shelters and vineyards—he didn't have $500,000 or $1 million to plow into a startup. He didn't buy elaborate pumps, crushers, and a super-speed bottling system. He didn't produce large volumes of red wines, which must sit in expensive oak barrels for several years before it can be sold—

nonproductive inventory that overloaded a number of other novice vintners, who lacked the foresight to understand the capital-intensive nature of the wine business. But Mahoney did have a good product and, equally important, a guaranteed place in which to sell it: at Connoisseur Imports.

Mahoney started out in 1972 and 1973 by producing only 2,000 cases of wine, and he didn't bother with wholesalers. Every bottle moved either through Connoisseur, direct mail, or a few other specialty wine shops. Wholesalers were, however, coming out of the woodwork and looking for a piece of the action—like underemployed lawyers converging on the scene of an accident. But Carneros Creek didn't make enough wine to warrant farming out for sales help. It increased production by only 1,000 or so cases each year. With the help of his wife, Kathy, Mahoney filled out bills of lading, kept the books, and played the role of general contractor.

Demand for premium California wines soared, along with the prices retailers were willing to pay. In 1972 many Bordeaux wines were selling for around $3 a bottle. But then Ridge began asking $5 for its Zinfandels. Beaulieu Vineyards started getting $6.50 for Cabernets, and wholesalers offered $4 to $6 a bottle to an increasing number of producers, Carneros Creek included. With negligible or no marketing expenses to contend with, Mahoney watched good returns come in.

Still, the cash was never squandered at Carneros Creek. Mahoney carefully added new tanks. When he put a new chair in his office, it was a splurge. To both Francis and Kathy, these little additions were special. Within a decade Carneros Creek's business alone was worth between $2.5 and $3 million, not including assets. It held very little debt. By 1983 Carneros Creek produced 13,000 cases of wine annually and had been profitable in each year of business; earnings climbed from $45,000 to $50,000, and then $80,000.

Sporting a sunburn from hours in his vineyards, this strong, compact man with a receding hairline and a gap-toothed grin has the look of a farmer. Although city-born, Mahoney is clearly comfortable on the land, dressed in jeans and work boots and accustomed to hard, physical labor. But this articulate, university-educated farmer can also slide into a well-tailored tuxedo and blend with the movers and shakers of any business, at any elegant function. Because of his retail shop experience, Mahoney is also able to speak with and handle the most pretentious of wine snobs, responding to an obscure analogy used to describe a certain wine with an equally ambiguous, but technically correct, observation.

However, what Mahoney most enjoyed after he began winning winemaking recognition was the security he felt that allowed him to lunch with the Napa Valley Vintners, the "in people" of his life; patrician winemakers like Joe Heitz and Louis Martini, who had endured hard times Mahoney could not even imagine. He would listen intently to the men talk about how Cabernets fetched $1 a bottle—in a good year. Mostly, the men were taking a break from hard work, making small talk and shop talk—discussing weather, the merits of certain bird repellents, filters, and forklifts. Mahoney enjoyed the senior statesmen, but felt a bit troubled by a new breed that joined the gatherings: high-powered, almost venture capitalist types from Los Angeles and other foreign lands.

These winemakers, many of whom had first visited the Napa Valley as tourists, were now the ones who most loudly and strongly fretted about "the tourist problem," and the opening of still more wineries that catered to the burgeoning crush of visitors. Along with this influx, things were beginning to change rapidly.

The cost of land in the valley climbed rapidly as more and more new winemakers entered the business. Nationwide, inflation and interest rates rose during the late 1970s, pressures that began squeezing the more highly leveraged wineries. Carneros Creek had gotten in on the ground floor; because of its low debt, interest and inflation weren't significant factors. Moreover, Mahoney could sell $10,000 to $15,000 worth of wine on weekends at Carneros Creek, loading cases into cars and taking the checks—as direct as sales could be. In 1979 he sold out his stock in six to nine months.

Until then Mahoney's business, like much of the premium wine market, had been completely product-driven. That is, the wine literally sold itself. The producers made no special effort to get the product on the street, into different types of outlets and markets. But in 1980 Mahoney could see a developing need for marketing and strategic selling through a network of dependable wholesalers in other states. Competition was beginning to cut into his market. And now he'd have to cut wholesalers in on the profit, meaning he'd earn less per bottle than in California.

Winemaking has long been called "the Gentleman's Game." When one asks vintners about competitors, they are quick to disclaim that they are striving against another winery. No, while Chrysler executives may get thrills taking customers from Ford or Toyota, and mean to do so with every fiber in their bodies, winemakers behave—at least in public—as if their vintages all serendipitously appeal to totally different groups of customers. But wineries are in reality locked in fiscally mortal competition for a limited pool of wine drinkers.

It is a competition waged when product leaves the winery, outside of what Mahoney has called "the cocoon and camaraderie of the valley." It's a battle for the ear, heart, and mind of the wholesaler, who must have incentives to move one particular label among many, and who must in turn motivate retailers to continue the effort. It is also waged in the wine media, by winning attention from writers and critics.