THE MKF ADVISOR
WINE BUSINESS UPDATE
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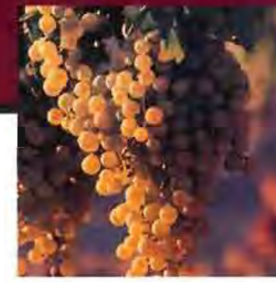

Wanted: Performance Metrics for Wineries

By Shandra Knego, CPA

Call them Key Performance Indicators (KPIs), Performance Metrics, Scorecards, or Benchmarks, the purpose is the same: to gauge business performance against a set of pre-defined measures. Properly done, a KPI review gives the business executive a high-level, real-time view of the health of a company encompassing financial, marketing, and sales performance.

MKF has developed wine industry specific KPIs that allow winery owners to effectively compare their business to their peers in many critical categories. The following is a summary of three wine business KPI's along with observations resulting from our financial reviews conducted in 2002:

- **GROSS PROFIT AS A % OF SALES**
  For most premium wineries this ratio should be 50% or higher. During 2002, this KPI fluctuated from a low of 34% to a high of 77%.

- **MARKETING COSTS AS A % OF SALES**
  This ratio has historically been 25% while current year performance suggests the norm may be slightly higher. In 2002, this KPI fluctuated from a low of 5% for a winery that essentially outsourced the marketing function through an agreement with a national sales and marketing agency to a high of 40% for a struggling winery in the midst of trying to regain lost market share.

- **ADMINISTRATIVE COSTS AS A % OF SALES**
  10% is a good rule of thumb for premium wineries. During 2002, this KPI fluctuated from a low of 6% to a high of 18%.

As indicated above, KPIs can vary greatly depending on the specific winery in question, and the cost structure and pricing strategy of that winery. Having relevant, comparable peer group data to calculate KPIs is essential in performing an effective benchmarking study.

Performance monitoring is just the first step. Managers need to define and implement KPI based incentives, provide employees with necessary resources to act, and continually communicate goals in order to effect change.

For additional information on obtaining an MKF Benchmark utilizing wine business specific KPIs, please contact Shandra Knego at (707) 963-9222.

—Shandra Knego, CPA
Ms. Knego provides business advisory and financial assurance services to wine businesses.

Inside

Back

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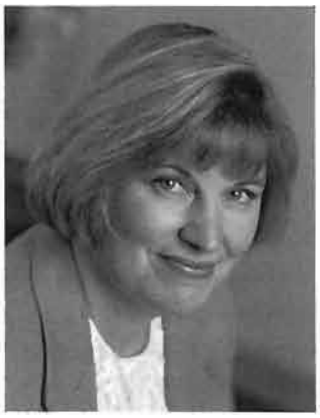

—**Wendy Petersen, CPA**
Ms. Petersen is a partner and Director of CPA Services with MKF. She provides tax planning, advisory and compliance services specific to the wine industry.

Partner Comment

Perhaps only once in 50 years will we see a new tax bill like the "Jobs and Growth Act of 2003" that President Bush signed into law in May, 2003.

If the new tax law delivers as many anticipate, businesses will be able to expand and grow more quickly with the help of bonus depreciation and the reduction of tax rates on dividends and capital gains, business managers will be able to generate a higher return on their investments as the cost of capital drops, and consumers will have more money to spend – all of which should improve the overall economic picture.

Now is the time to review your tax and business planning strategies, not only to take advantage of the new tax savings but also to position your business for the inevitable upswing.

The future will be here before you know it.

The Changing Role of the Winery CEO – Part 3

Winery teams are changing from the single owner operator to a team of professionals

By Deborah Steinthal

Current wine industry dynamics of increased competition and consolidation are revolutionizing how winery CEOs manage their businesses. This article is third in a series that describes best practices that these wine industry leaders are implementing in support of their growth strategies.

A growing number of winery executive teams are changing. In some cases, the traditional owner/operator is learning to be a different type of CEO and hiring a new, more professional executive team or, alternatively, hiring a professional CEO and crafting a new role for themselves as a member of a Board of Directors.

These new style industry CEOs are learning to be leaders, rather than managers. They are producing plans that are more customer-focused and requiring their entire executive team to be more effective in plan execution. Their role in building the culture and the team is more complex than ever before and often requires changes in approach and skill sets.

BALANCING PASSION WITH DISCIPLINE IS A FORMULA FOR SUCCESS

While entrepreneurs bring passion to their business, some have a tendency to chase after the newest, profit-making opportunity without much thought to long-term, bottom-line impacts. On the other hand, a professional and experienced executive team is able to bring more discipline to decisions to build long-term brand equity and not sacrifice brand strength for short-term economics. These executives have the necessary experience to focus winery programs on core business and to lead the organization through long-term commitment and vision.

THE CHANGING FACE OF EXECUTIVE TEAMS

Winery owners are realizing they need to do a better job differentiating their brands and so are seeking to build more knowledge in marketing and brand management. Wineries are hiring VPs of Marketing with brand management expertise, CEOs with strategic planning experience, and VPs of Sales with national sales track records. These new executive teams are streamlining purchasing and accounting practices, and using better planning tools coupled with more accurate and timely information to understand their market performance and pinpoint opportunities.

WHAT IS THE IMPACT OF THIS TREND?

The new breed of professionals can have demands that run counter to previously established winery culture. They expect more interactive planning cycles, more formality in evaluating winery progress against these plans, and sophisticated performance reporting through the IT systems. Staff turnover sometimes results as existing winery staff leave when new processes are introduced and new skills are required. The CEO needs to remain committed to this long-term picture because, however painful any short-term changes are, the results will far outweigh the investment over time.

—**Deborah Steinthal**
Deborah Steinthal is an executive advisor with MKF. She helps winery CEOs with strategic thinking, business planning and market strategy. Deborah leads MKF's CEO Forum – an executive program for an exclusive group of CEOs who seek stimulating discussion focused on critical leadership challenges.

Sweeping Tax Law Changes May Impact Wine Businesses

By Amy Smith, CPA

President Bush's proposed tax plan, called "Jobs and Growth Act of 2003," was signed into law on May 28, 2003. The new law provides important changes and, as a result, your business may benefit from terrific tax-saving opportunities. Many of these changes are effective in 2003. MKF's tax specialists have been watching this legislation since first proposed and have been analyzing and developing strategies in order to immediately assist clients to realize the maximum benefits.

INCREASED IRC SECTION 179 DEDUCTIONS

- The annual IRC Section 179 deduction increased from $25,000 to $100,000 for qualified property placed in service during the 2003, 2004, and 2005 tax years.
- The maximum asset acquisition phase-out threshold increased from $200,000 to $400,000.
- Off-the-shelf computer software will now be eligible as qualified property.

INCREASED BONUS FIRST-YEAR DEPRECIATION DEDUCTION

- The annual bonus depreciation deduction increased from 30% to 50% for qualified property placed in service after May 5, 2003 and before January 1, 2005.
- There is no dollar limit on the qualified asset acquisitions.
- The deduction is taken after the Section 179 deduction and before the regular depreciation calculations.
- The deduction is subject to the 263A capitalization rules (e.g. inventory capitalization).
- The deduction is not available for ADS property (e.g. vineyards electing to expense pre-productive costs).
- The deduction applies to federal tax and alternative minimum tax and is <u>not</u> a tax credit.

CORPORATE ESTIMATED TAX POSTPONEMENT

- The corporate estimated tax payment due on September 15, 2003 is temporarily postponed and due on October 1, 2003.

REDUCED TAX RATES ON DIVIDENDS & CAPITAL GAINS FOR INDIVIDUALS

- Tax rates on both domestic dividends and long-term capital gains are reduced to 5% for those in the lowest two brackets and to 15% for those in higher brackets.
- The tax rate reduction on dividend income applies to domestic dividends received in 2003 through 2007.
- The tax rate reduction on long-term capital gains income applies to sales, exchanges, and installment payments received after May 5, 2003 through December 31, 2007.

These are some of the highlights of the 2003 Tax Act and we expect further congressional interpretations and technical corrections. Many profitable businesses could benefit from the 2003 Tax Act. You may want to take advantage of the opportunities the new tax laws provide as you grapple with complex issues such as estate planning, succession planning, and appreciated real estate.

Please contact MKF to find out if your business could benefit from the tax savings offered by the 2003 Tax Act.

—Amy Smith, CPA

Ms. Smith specializes in income and estate taxation. She provides tax planning, advisory and compliance services specific to the wine industry.

Congratulations Amy!

A seasoned taxation expert with over 8 years of experience helping clients with income and estate taxation, Amy Smith was recently appointed a Partner with Motto Kryla & Fisher, LLP.

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MKF in the News:

Wine Market Report, July 2, 2003
State Wine Sales Display Volatility *By Rich Cartiere*

Because of the wide-ranging volatility of California wine sales in each state, wine marketers should analyze each state's varietal sales by major price segment before adopting marketing and promotional programs, according to the authors of the just-released Wine Trends State Report.

"It's extremely dangerous to look at a state as one, monolithic market nowadays," said Michelle Rowell, senior market consultant for St. Helena, Calif.-based Motto Kryla Fisher. "On a macro level, there were really no major trends last year; but at each state level, you begin to see some big changes."

Overall, wine sales increased in 27 states and the District of Columbia. Utah, which liberalized its wine sales laws last year, saw the single largest volume increase—up 36 percent. Perhaps because of a drop in tourism, Hawaii fell out of the Top 10 states for luxury wines, while Nevada, Colorado and Arizona, perhaps benefiting from increased "local tourism," entered that Top 10 list. California was the largest market—17.6% of all sales, down only one tenth of one percent from 2001.

The Wine Trends State Report 2003 lists case volume by state, the percent change in sales for those years, and each state's market share, containing 2001 and 2002 shipment data for seven varietals organized into eight price segments.

Rowell said wineries might not want to plan on increasing sales of Merlots priced above $30 per bottle in Arizona, which dropped from the 7th most important market for this varietal in 2001 to the 20 th in 2002, losing 76% of its volume. "Perhaps a better strategy would be to refocus the winery's Arizona salesperson and distributor on Cabernet in that same price segment, which appears to be hot in that state after an increase in volume of 144% from 2001 to 2002," suggested Rowell.

Nevada, Arizona, Colorado and Oregon became more important markets for Cabernet in 2002, taking the places of Massachusetts, Washington, Hawaii and Connecticut. For $30+ Pinot Noir, three of the same states that showed strides for Cabernet also entered the Top 10 for Pinot: Arizona, Colorado and Nevada. Louisiana and Pennsylvania and Hawaii all fell off.

Top 10 Volume States for California Wine above $30 per Bottle by Varietal

	Cabernet Sauvignon		Pinot Noir	
Rank	2001	2002	2001	2002
1	CA	CA	CA	CA
2	NJ	TX	NY	TX
3	NY	NV	HI	NY
4	TX	NJ	MA	MA
5	FL	FL	FL	FL
6	IL	AZ	NJ	DC
7	MA	NY	TX	NJ
8	WA	IL	DC	AZ
9	HI	CO	LA	CO
10	CT	OR	PA	NV

Percent Change in Sales by Case Volume

	All CA Wine - All Prices		All Wine – Luxury Segment $30+	
Rank	2001	2002	2001	2002
1	CA	CA	CA	CA
2	FL	FL	NJ	TX
3	NY	NY	NY	NV
4	TX	TX	TX	NJ
5	NJ	NJ	FL	FL
6	MA	IL	IL	AZ
7	IL	MA	MA	NY
8	PA	WA	WA	IL
9	WA	PA	HI	CO
10	GA	GA	AZ	OR

WINE TRENDS STATE REPORT AVAILABLE NOW!

The *Wine Trends State Report 2003* is a available for $1,500 per varietal.

For more information, please call Michelle Rowell at 707-963-9222 or email: mrowell@mkf.com

MKF professionals are the leading wine business advisors, providing CPA services, business consulting, industry research, and mergers and acquisitions services to the owners and managers of hundreds of premium wine businesses around the world for over twenty years.

For more information about MKF's services, please call Lisa Anthony, Director of Marketing: 707-967-5322 or e-mail lanthony@mkf.com

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MKF WINE BUSINESS Bulletin:

SUMMER 2003

A LETTER FROM THE CEO

DEAR READERS:

MKF has changed dramatically since our early days twenty years ago when we first offered CPA services to a small group of premium wineries. We now provide highly specialized and sophisticated financial and planning services to an industry that has transformed itself into a high-growth, professionally-managed and internationally-recognized consumer packaged goods business.

To continue to meet the growing needs of the premium wine industry, MKF will undergo its own transformation with a major reorganization to our business structure. Here is a preview of the changes that will be happening in the coming weeks and months.

THREE SEPARATE BUSINESSES

MKF has reorganized into three independently-managed organizations owned by MKF partners.

- **Motto Kryla & Fisher, LLP**, Wine Business CPAs directed by partners: Wendy Petersen, Amy Smith and Karen Coleman
- **MKF Group, LLP,** Wine Business Advisors directed by partners: Mike Fisher, Karen Kryla, Vic Motto and Gordon T. Axton, Jr.
- **MKF Capital Advisors, LLC** Wine Industry Mergers and Acquisitions (currently in process with registration and licensing), directed by partner Vic Motto

The purpose for the reorganization is two-fold: to strengthen and expand services in our three core business areas, and to address changes in the post-Enron regulatory environment regarding the independence of auditors and consultants.

Each of these businesses will be managed and staffed by current partners and associates, and will share staff, facilities, equipment and expertise so you will continue to work with many of the individuals you have come to know and trust. We are also conducting a recruitment campaign to bring in additional talent and leadership in several areas.

I invite you to contact me or any of our partners for further information or with any questions you may have. It is my goal and commitment, shared by everyone here at MKF, that you continue to experience the highly-professional service with a personal touch that you have come to expect and, at the same time, enjoy the benefits of greater focus, expertise and capabilities in all of the areas that we serve you.

John Heymann
CEO