Winter Report - 2022

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Up, Up and Away

In a perfect world, the headline would be referencing 2022 grape prices! But in reality, we're talking about costs associated with grape production and vineyard development. Input costs have escalated at an unsustainable clip over the last year. Inflation has been widely reported in mid-January to have reached its highest level in 40 years, and the vineyard business is not immune from its impacts.

It seems likely to us that current inflationary pressures are going to have a significantly disruptive effect on our lives, our businesses and our economy that will last well beyond 2022, despite all the talk of "easing inflation" this year. To assume prices/costs will magically roll back to 2020 levels, as if 2021 didn't happen, is kind of like thinking that there's still a chance that we will pull out of this pandemic and resume activity as if it was 2019. It's simply not going to happen.

Central to winegrape growing are costs that I argue are not going to just go back to "normal." It's true that some inputs are subject to market forces from many directions and can certainly ease in the future, like fuel and fertilizer, for example. But what about labor, utilities and water? Does anyone seriously think those will get cheaper? If they do, they should be reminded that they are in California. What about the fact that the cost to develop a vineyard is capitalized? (We are essentially locking in relatively high development cost over the life of the planting contract.)

The only thing that's cheap today, ironically, is money. But you better hurry up and get your hands on some, because forecasts are for interest rates to rise as early as the end of the first quarter. The relatively low cost of money doesn't nearly make up for the escalated cost of everything we are buying with it. In a recent *USA Today* article, inflation was reported to be up a staggering 7 percent in 2021, with "core" prices (fuel and food excluded) being up 5.5 percent.

New cars went up almost 12 percent in cost last year. Do you think tractors are any different? Steel landed at about 12 percent up year-on-year, but during the year, steel was hovering at levels as high as 70 percent over the previous year. Steel is up 25 percent from two years ago, explaining the more-than-a-dollar increase per stake in pricing we have seen for T-stakes.

It's impossible to assign a generic number to the cost of water (or associated cost increases) in California, simply because of the geographic and hydrologic diversity. But I sure wouldn't want to be the guy claiming water will get any cheaper or more available in California any time soon. I think we can all agree that isn't going to happen.

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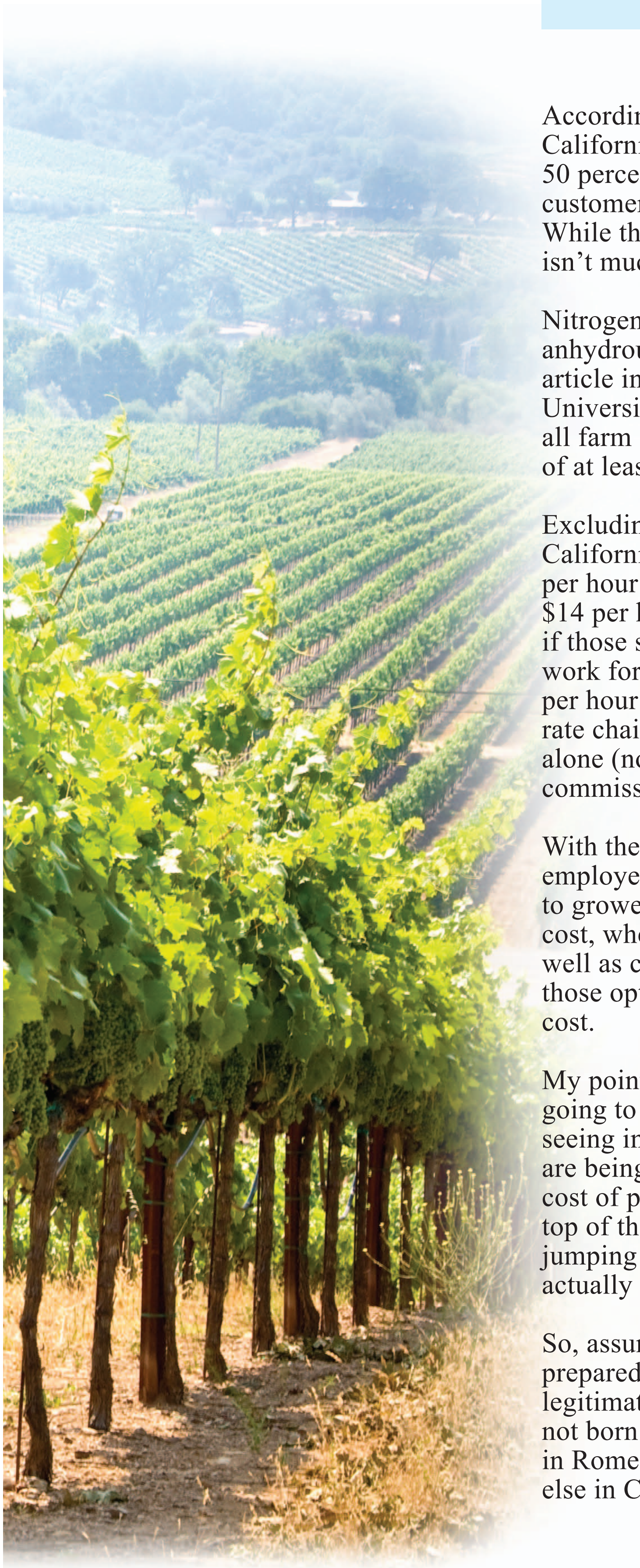

Rising Production Costs

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According to chooseenergy.com, of the 48 contiguous states, California is in the top five for electric rates, coming in at over 50 percent of the national average for the average residential customer and having experienced a 6 percent increase last year. While these are residential numbers, I'm willing to bet agriculture isn't much different.

Nitrogen fertilizers more than doubled in price last year, with anhydrous, urea and potash all up well over 100 percent. A recent article in the on-line magazine *Successful Farming* cited Purdue University researcher Michael Langemeier stating that prices on all farm inputs were at record highs, climbing a historic average of at least 12 percent.

Excluding Washington, D.C.'s $15.20 hourly minimum wage, California has the highest minimum wage in the country at $15 per hour for employers of over 25 people. The minimum wage is $14 per hour for small employers of 25 and fewer employees (as if those small employers can magically find people to actually work for a dollar less an hour). With that having gone up a $1 per hour on January 1, and assuming that trickles up the pay-rate chain, we just experienced a 7 percent increase in labor alone (not to mention labor cost add-ons like payroll taxes and commissions).

With the implementation of overtime pay at 40 hours for large ag employers (>25 employees) this year, another cost can be added to growers' ever-increasing cost list. Growers will try to avoid this cost, where able, by reducing work days and/or shift lengths, as well as continuing to transition to mechanization. However, where those options are not practical, the end result is simply higher cost.

My point in all this cost narrative is that winegrapes are simply going to cost more to produce. Any material increases we are seeing in grape prices as a result of the last two short state crops are being at least partially, if not totally, negated by the increasing cost of production. Winegrape growing has never been near the top of the list of highest margin ventures to begin with, but these jumping input costs are really pinching any margin that might actually exist.

So, assuming a "balanced" 2022 market, buyers should be prepared for growers to make some pretty convincing and legitimate arguments for higher grape prices. These arguments are not born of greed, but rather necessity. As the adage goes, "When in Rome, do as the Romans do" – metaphorically, if everything else in California is going up in price, then why not grapes?

2022 Market Update

Central Valley Update

by Karl Lehman

The past few years have been a roller coaster of epic proportions for Central Valley winegrapes. The Central Valley primarily produces winegrapes that go into the "value" segment of the wine market. In this segment of the business, primary market forces can be summarized by using the acronym "PIE" (Production, Imports, Economics).

On the production side, there are two components that need to be accounted for – total yield by variety and yield per acre. With a majority of wine grapes being planted in the Central Valley in the mid to late 90s, we've seen yields decline over time. Those vineyards are past their productive peak and are also challenged regarding the need to convert to mechanization. Mechanization is a must-do in Central Valley vineyards, due to labor costs and availability, in order to remain economically viable long term.

California's new vineyard removal burn restriction (www.valleyair.org/agburnalternatives) will likely cause some pullout fast-tracking. So we may be moving toward needing more production. Planting contracts have been available for mainly white varietals as well as Rubired and a very narrow list of red wine varietals, as wineries anticipate removal of older vineyards. On new developments, we are seeing tighter spacing to maximize production along with trellis systems that lend themselves to mechanization. New plantings are a must for the long-term sustainability of this segment of the business, but the economics must justify such an investment.

We are experiencing unprecedented inflation that is impacting all aspects of the wine business, but the most important aspect is the production side. To my knowledge, only Jesus was able to make wine out of water. The rest of us actually need grapes. Cultural costs are at an all-time high, and changing daily. Collaboration is needed between buyers and growers so that there's a true understanding of costs involved. An area where we are starting to see some strong collaboration is the movement toward sustainable certifications, with bonuses offered for doing so.

Lastly, imports play a significant role in the ebb and flow of the Central Valley wine business. I'm not sure if we are ebbing or flowing right now with imports, but one thing is for sure – the reliability and affordability of imports (particularly those in bulk) has certainly been suspect in recent months. We see buyers beginning to question their reliance on foreign supply and looking more toward multi-year relationship building with Central Valley growers. So, remember "PIE" when thinking about the Central Valley grape market and the factors that affect our sustainability as a segment of the wine business.

North Valley Update

by Kyle Collins

One of the great things about working in the California wine world, is that no single year is just like its predecessors. There are new challenges to overcome, new opportunities to seize, and new faces to meet each year. I'm blessed, and extremely proud, to be one of those fresh faces on the team at Allied Grape Growers, and I couldn't have picked a better time to hit the ground running!

The 2021 season felt, for several months, to have finally broken a down cycle in the Northern Interior. Riding a COVID spike in retail wine sales, buyers were out and active early in the year and continued propping up a healthy spot market through the harvest season. This activity was a welcome sign of hope for growers who continue navigating a perfect storm of rapidly increasing input costs, a constricting labor pool, consistently inconsistent COVID requirements, and challenging regulatory hurdles around labor and material.

Fast forward to the winter of '21 and early '22 and things feel much the same, but

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North Valley Update
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with a bit of a cautious eye toward the horizon. Most buyers are having advanced talks on early contracting, with some already actively moving to lock up multi-year supply in January, while a small number are taking a more conservative approach. Pricing has so far held steady and, in many varieties, has continued to improve since the close of the '21 season.

Lodi Zinfandel, in particular, stands out as a variety that has seen multi-year contract minimum pricing increase, by as much as 50 percent from just two years ago!

With all that said, everyone is looking with a degree of uncertainty at tenuous retail wine sales, and there is always the question of what mother nature might have in store for us in early 2022. Growers would be wise to maintain a balanced understanding of security versus risk, as they engage in their contract negotiations.

Vineyard removals continue to be a common sight in the North Valley, and we expect the time line to accelerate for growers that were "on the fence" on redevelopment with the announced "burn ban" just around the corner. Some opportunities for planting contracts, especially around Lodi, have also begun to surface, but current material costs associated with vineyard development means growers have been deliberate in fully vetting their situations before signing on.

To put a bow on all of this, the current market is one of opportunity for both growers and buyers, but, as always, proceed with an appropriate degree of caution. It is critical now, more than ever, as new buyers enter the North Valley grape market to see the whole picture.

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Sustainable grape pricing is critical to the industry's continued viability, but stronger grape markets also provide growers the opportunity to place value in relationships, security and fit. We at AGG are excited to see what this season has in store, and are looking forward to a successful 2022!

North Coast Update

by Chad Clark

Over the past 12 years with AGG, I have never seen such an early, active grape market throughout the North Coast. As expected, given the short 2020 and 2021 winegrape yields, combined with the existing and current bulk wine supply, we have continued to expand opportunities for both our growers and winery partners.

The North Coast grape market is hot! The majority of the activity has been with the four main varieties: Sauvignon Blanc, Cabernet Sauvignon, Chardonnay and Pinot Noir (and in this order). Sauvignon Blanc has been highly desired in all tonnage amounts, regions and for multi-year terms. Pricing and returns have been very sustainable, given yield-productive properties or blocks.

Cabernet Sauvignon (Cab) has seen most of its current activity within Napa and Sonoma Counties, with several discussions regarding Cab in Lake, Mendocino and Solano Counties (for cost averaging). Pricing continues to strengthen, but still seems to be an unknown regarding where it will land or flatten out, specifically in Napa Valley. Potential terms for Cab have been multi-year, especially with the many one-year "trial" agreements having been done in recent years.

Chardonnay has been very active in all areas of Napa Valley and Sonoma County (Russian River Valley, Sonoma Coast and Carneros). Pricing has been strong in most all areas, with highlights being Russian River and the "west county" of Sonoma.

Pinot Noir activity is mostly seen in Russian River Valley and Sonoma Coast appellations, along with Napa Carneros. Pricing has been solid and very specific to the intended program on multi-year agreements.

Additionally, the demand for organically farmed alternative red and white varieties continues to grow with wineries of all sizes. Pricing

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discussions and agreements have been mostly based on intended retail or direct-to-consumer bottle prices.

The common continued question of crop size, given the 2021 growing season, is a typical talking point with all growers and wineries. Stunted growth blocks are yet to be determined on how they will fair for the upcoming season. I estimate these blocks and blocks with high water stress to have lighter than average yields for 2022.

Farming and management costs are increasing, again; several of our growers have mentioned significant cost increases for 2022 and looking forward. We have seen grower budgets with cost increases of 100 percent or more, considering the previous 10 years. We cannot stress enough the importance of taking into account increased costs, when negotiating contract terms.

In closing, I remain very optimistic, excited and prepared for the 2022 season, and having the ability to reset, put the past behind us and move forward with a clear mind and healthy outlook. Cheers.

Central Coast Update

by Michael Haddox

Obviously, we are still in a strange new world, and it would be silly to think that things will ever go back to the old normal. But I do believe we are seeing the right conditions for a fantastic rebound from the past few years.

Through this past harvest and over these past few months, we have seen an uptick in foot traffic at local Central Coast wineries and tasting rooms. Signs are back out, and tourists are back at the hot spots ready to support local businesses. All great signs of good times ahead.

In regard to the market on the Central Coast, things aren't moving as quickly as in the other regions of California, but don't let the quietness fool you. There has been quite a bit of activity in the form of vineyard sales and acquisitions. Several large winery players have acquired existing vineyards for their estate programs in all areas of the Central Coast, with vineyards selling at substantially higher prices than we have seen for some time. A few recent transactions closed in record time at full asking price.

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This trend makes sense, as the market for grapes and bulk wines continues to see high demand and stronger prices across most AVAs and varietals. As expected, Cabernet Sauvignon leads that group with Sauvignon Blanc still underplanted and in short supply in our region.

Quality from the 2021 vintage appears to be great and from the conversations we are having with our growers and buyers on the Central Coast, we expect that trend to continue into the 2022 season. Buyers should be proactive with sourcing needs again this year to ensure hitting the quantity and quality targets needed. And for growers, now is the perfect time to sign up new and existing blocks into the AGG family. We have strong demand currently for Merlot, Syrah and Zinfandel.

The weather has been interesting to say the least. With good rain totals and colder than normal temperatures, we are trending in the right direction for the upcoming season. Fingers crossed for a little more rain, as we still have a few months to hold our breath.

The biggest take-home for the Central Coast this year is the opportunity for planting contracts. We haven't seen this opportunity in a while, but some are talking about the need to develop vineyards for specific needs in the immediate future.

Reach out if you have interest in evaluating a planting contract or if you have some ground you wish to plant or redevelop. Now is a great time to talk.

AGG

Allied Grape Growers

Collins and Bond Join AGG's Staff

Kyle Collins has been named AGG's manager of North Valley operations, effective November 15, 2021. He joined the managerial grape sales team, which also includes the North Coast, Central Coast and Central Valley operations. In his new role, Collins oversees Northern San Joaquin Valley grower relations and is responsible for negotiating economically sustainable grape purchase agreements for the association's North Valley members.

"Kyle is the perfect addition to Allied Grape Growers' top-notch team of professionals," President Jeff Bitter said. "He comes with strong experience, a great resume and a commitment to the North Valley as his home. Most importantly, Kyle embodies the same values as our company and our growers. We are excited to welcome him to our dedicated AGG family."

Collins comes to the association with a decade of experience in the wine industry. For the past three years, he was a vineyard manager with Gallo Vineyards, where he managed daily operations on five northern interior ranches, fostered collaboration between Gallo and outside stakeholders, managed ranch operating budgets and directed harvest operations. From 2012 to 2018, he was a grower relations representative for E. & J. Gallo Winery, where he oversaw the contracting of Lodi/Delta winegrapes, coordinated grape pricing and long-term strategic grape supply development, monitored vineyard practices, worked with growers to ensure exceptional fruit quality and assisted with harvest operations. Collins started his career as a grower relations representative for Constellation Brands.

"I am thrilled for the opportunity to join the family at Allied Grape Growers," Collins said. "I look forward to continuing the long-running tradition of service and commitment that has defined AGG's presence in the North Valley."

Pam Bond has been named to North Coast operations support, effective December 1, 2021, and is working closely with AGG's North Coast regional manager and grower relations representative. Her role is to provide administrative support around contract negotiations as well as field support for grower relations. Bond worked with AGG through the 2021 harvest as a seasonal employee before accepting this full-time position.

"We are very excited to expand our North Coast staff with someone with such rich experiences and reputation," President Jeff Bitter said. "Pam brings a delightful spirit and work ethic to AGG, and she will serve our growers and grape buyers well. Her experience in all aspects of administration and operations, from vineyards to winery, will be an asset for our rapidly growing North Coast business."

Bond comes to AGG with extensive experience and connections in the industry, specifically with coordinating successful vineyard management strategies and initiatives with growers designed

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Scholarship Opportunities
for College and High School Students

Allied Grape Growers/Ag One Foundation Robert "Bob" McInturf Endowment

For: Fresno State Jordan College of Agricultural Sciences and Technology students, with preference to those majoring in agricultural business, plant science, or viticulture and enology.

About: The Jordan College selects the deserving scholarship recipients each spring for the next academic year. AGG established this endowed scholarship fund with the Ag One Foundation to honor longtime AGG President Robert "Bob" McInturf, who passed away in 2013. After a career in the military, Bob and his wife settled in Fresno, where they resided for most of their lives. He worked for the family farming operation, which included hundreds of acres of winegrapes and raisins. Bob was a founding member of AGG in 1951, and served as our first president for 36 years.

Scholarship Funds: The number of scholarships available each year is dependent upon how much income the permanent fund earns. In 2022, three scholarships are available at $500 each.

Application Deadline: February 28, 2022

Website: http://www.fresnostate.edu/jcast/agonefoundation/endowment/alliedgrape.html

California Association of Winegrape Growers Foundation

For: Students whose parent or legal guardian is employed by a California winegrape grower. (See full application details on the website.

About: The CAWG Foundation board selects several recipients from high schools throughout the state each year. Scholarship selection is based on scholastic ability, financial need, community involvement, leadership and a 500-word essay. Since the scholarship program's inception in 1998, the foundation has awarded $494,500 in scholarships. Funds are raised through the generous donations of members of CAWG and the California wine community.

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Scholarship Funds: Four-year scholarships are $8,000 each for students attending a University of California or California State University campus. Two-year scholarships are $2,000 each for students attending a California community college. The Robert Miller Scholarship for Viticulture and Enology is awarded to a Central Coast student who is enrolled or will enroll at Allan Hancock College or Cal Poly San Luis Obispo.

Application Deadline: March 4, 2022

Website: https://cawgfoundation.org/scholarship-eligibility-requirements/

New Staff Members
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to increase quality and revenue. She previously worked for Swanson Vineyards and Winery in Oakville as director of vineyard and estate operations from 2010 to 2020, and as assistant vineyard manager from 2002 to 2010. During her time with Swanson, she served in management positions; handled grower relations; was responsible for all aspects of grape purchases, sales and communication; and worked on pest and disease identification and control.

Bond was a member of the California Department of Food and Agriculture's PD/GWSS Board from 2012 to 2020, including a one-year term as board chair. She holds an associate's degree in viticulture from Napa Valley College.

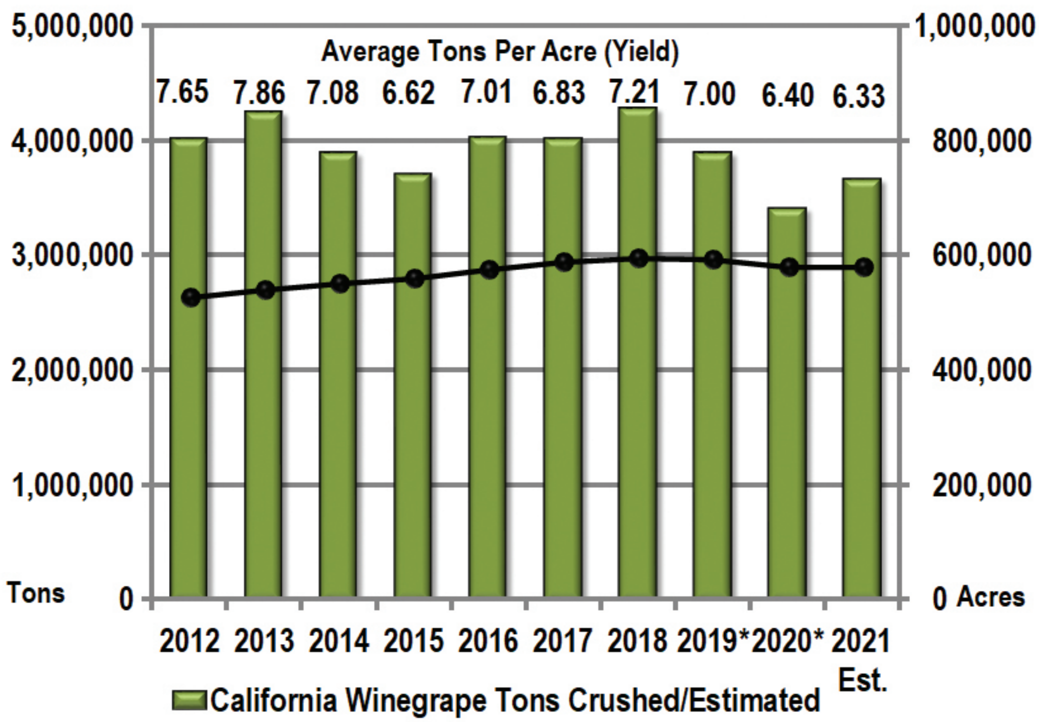
"I am delighted to become a member of Allied Grape Grower's excellent team," Bond said. "I look forward to contributing to their service to, and collaboration with, North Coast growers and wineries, working together and weaving the ongoing story of beautiful wines."

General Industry Outlook:

In so many aspects of our lives as Americans, there is much uncertainty about the future. The pandemic has taught us a lot of things, not the least of which is flexibility! Just like we have learned to adapt and be flexible with our expectations/reactions surrounding the pandemic, we are also continuously learning to do the same regarding the grape and wine markets.

No matter the time, no matter the year, there have always been lots of different things happening in the grape and wine markets simultaneously. There's a simple reason for this……winegrapes and wine are not commodities. The markets for winegrapes and wine are specialized, unique and very distinct, so there is never a one-size-fits-all interpretation of the market. There are often times where one variety is long in supply while another is short..….or maybe one region is in oversupply, while another region is starving for more product.

10-Year Estimate Annual Winegrape Yield



*For crop years 2019 & 2020, yield was estimated due to material amounts of unharvested grapes

However, what the pandemic has done to the grape and wine markets has been to take away the confidence of the producer to make risk decisions. Most folks are used to different-behaving markets, but along with that they are also used to being able to confidently identify trends and make planning and marketing decisions. The pandemic has taken away our ability to rightly/accurately identify many of those trends. We've heard it said many times over the last two years: "Don't make large decisions or take big risks based on trends associated with the pandemic, because it can change tomorrow."

It's not unusual for us here at AGG to be asked what the future holds. After all, that's what we do; we make decisions and share information based on what we know about supply and demand, in the midst of industry trends. It is, however, much harder these days to identify trends that are here to stay versus trends that are a result of a market shift caused by the pandemic.

Add in wildfire smoke, and things can get real unpredictable! Obviously, the general uncertainty today causes people to ask even more - What does the future hold?

Short Crops Are the Key

It may be surprising, but the most important aspect of the relative "health" of the winegrape market today doesn't have to do with the pandemic and channel-shifting, per se. (Those in the interior regions may assume this). It also doesn't have to do with the 2020 wildfires. (Those in the coastal regions may assume this). It actually has to do with lighter statewide yields the last two years.

We're not saying that channel shifting and smoke rejections didn't influence the market, because they most certainly did, but above all else, two short crops in a row has been the driving force behind the now healthier/more-balanced grape and wine markets. Short crops gave us breathing room by providing the time wine producers needed to balance supply. It allowed those that were long on inventory the time (and option) to sell.

Graphically illustrated, in the chart at the left, are our estimates of annual winegrape yield over the last 10 crop years. For that ten-year period, statewide yield averaged seven (7) tons per acre across all winegrape acres in the state. But notice the last two years were estimated to be significantly less, at nearly 10 percent off. More than the pandemic, more than smoke exposure/rejections, this had a balancing effect on the market.

In 2020, a "market bump" was provided by the shear number of tons rejected due to smoke, because that decrease in crushed grapes happened in a segment of the market that was the most oversupplied and was most in need of "supply relief." While it was not at all good for growers, it was good for market balance.

How "Strong" Is Our State of Balance?

So, back to the question of where we go from here. The answer will be frustrating, but, "It depends!" To be more specific – it depends on crop size. Last year at this time, we were still throwing up plenty of warnings regarding potential oversupply in the future. One short crop at that point (2020) wasn't enough to assure grape market balance for the future. A year later, we have backed off that warning, considering that we have had two short crops in a row.

In 2019, after we had experienced an oversupplied market with grapes left unpurchased, we provided the industry with perspective that we were in a cycle of producing 200,000 tons too much annually. This was further quantified by a call for the removal of at least 30,000 acres. (Quick math here: 30,000 acres x 7-ton-per-acre average yield = 210,000 tons.) We also estimated that 200,000 tons were left unharvested that year. Essentially, the industry excess for 2019 was left on the vine.

By the time 2019 rolled around, we had been overproducing for some time. It wasn't a one-year issue. Wine shipment growth slowed significantly around 2015/2016, but we produced four-million-ton crops all the way through 2019. Since we were adding about 200,000 tons a year more than we needed to our inventory, 2019 represented the breaking point.

The last two short crop years (with some help from smoke in 2020) has relieved that three-to-four year buildup of excess wine. We are no longer concerning ourselves with jumping right back into an oversupply situation. But make no mistake – any series of 4-million-ton crushes in a row will challenge that balance once again, assuming we see no growth in wine shipments. One good crop isn't going to do it, but if we have a series of them, beware.

Our industry is most comfortable from a supply/demand aspect, with crushes of about 3.8 million tons. Any more on a repetitive basis, and we have too much. Any less repetitively, and we have too little. Of course, this assumes wine shipments don't change materially one way or another. All evidence today points to that reality; we aren't growing overall wine shipments. Latest data from various wine industry analysts point to another flat shipment year in 2021.

We have been writing about lack of wine shipment growth for some time in our newsletters, so we will spare you the repetition. Despite this, the exciting news is there are some wineries/producers doing very well and increasing their position and market share. Those wineries/producers quickly look to scoop up supply from others who are struggling to grow shipments. As a result, there is an ample amount of grapes and wine being traded currently, at virtually all price points in the market place. Our regional manager updates earlier in the newsletter will give you an idea of the relative hot spots.

Prognosticating the Interior Markets

One large misconception about the health of the "lower-end" of the market is that grocery stores are selling lots of value-priced wine during the pandemic. That is not at all reality. While the off-premise segment of the business has benefited from the pandemic, lower-priced wine offerings have not, as "premiumization" continues. Wines below $11 per bottle continue to struggle with maintaining market share. Some of the most recent numbers for certain price categories below $11 show double digit declines in 2021.

Considering the volume that this segment of the market represents, that is a scary proposition. At this point one might be asking, "How can the interior grape market be as healthy as it is in the midst of declining shipments below $11 per bottle?" There are five primary explanations to that question, none of which is the sole reason, but collectively they explain how/why the interior regions grape market is in balance.

The first reason is that the interior regions of the state have been decreasing in acreage to "keep up" with decreasing demand over the years. While shipments have been declining, so has production, due to pullouts and a general lack of

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planting. The chart below illustrates the pulling/planting dynamics of recent years. Pullouts have averaged 12,000 acres per year, while plantings have only averaged around 8,000 acres per year.

Secondly, going into the pandemic, the interior regions were actually suffering from the coastal over-supply of grapes and wine, which thwarted the opportunity for market balance. Even if we assume the "below $11 market" was in supply/demand balance on its own, the segment immediately above that was not. Coastal over-supply started to rear its head as early as 2017, which put supply pressure on the interior segments of the market, as good quality coastal supply was many times priced equivalent to "California" supply.

Next, the interior market feels healthy today because of the obvious lack of grapes available for sale. There are relatively very few spot market winegrapes for sale in the interior regions today, because most buyers have been actively buying on multi-year agreements for the last two years. This has effectively taken grapes off the market and contributed to a sense of shortness. We don't anticipate that scenario to change until 2023, at the earliest, as some of those first three-year deals signed in 2020 are expiring after 2022.

Another factor is that there is incredible competition amongst all players that are squeezing into the pandemic-strengthened, off-premise segment of the market to try to capture sales. This competition squeezes those producers' margins. An effective way to preserve margin is to acquire lower-cost products. And as has been the case for all times, the interior grape growing regions of the state offer the most "affordably-priced" grapes. Simply put, interior region grapes are being utilized (at some percentage) to control cost in higher-priced wines.

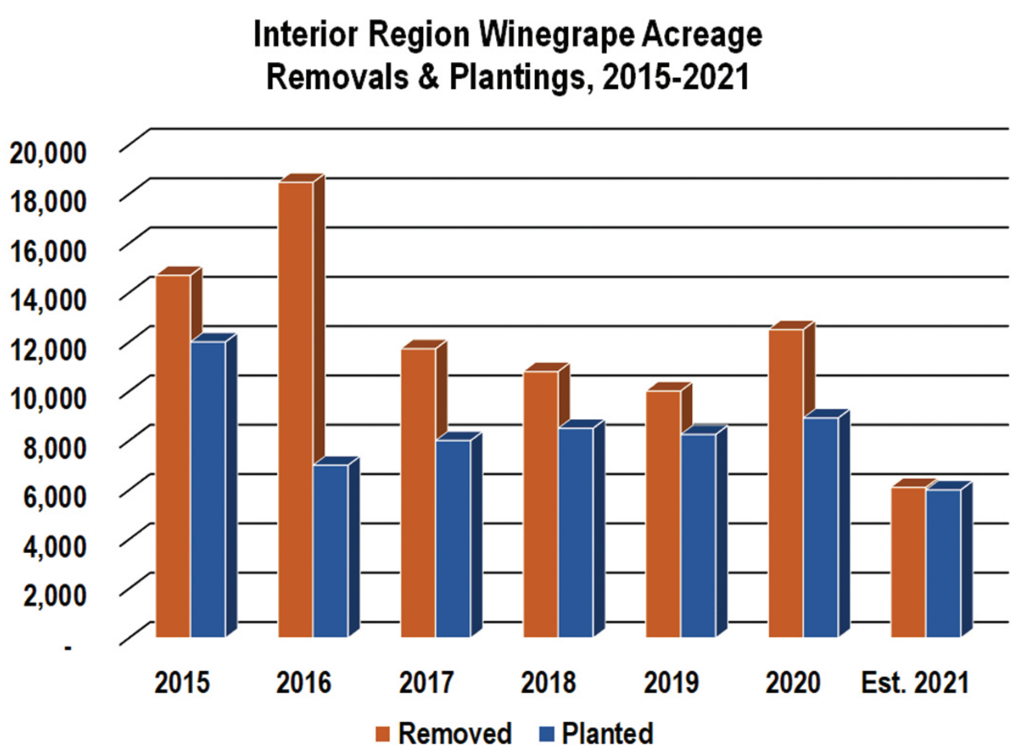
Lastly, as a factor playing into the health of the interior regions market, the largest transaction of assets ever in the California wine industry (between Gallo and Constellation Brands) was closed in early 2021. This brought back market stability and confidence after a period of two years of regulatory review. We will loosely call those two years a "lame duck" period, as many market players (even those outside of the two parties involved in the deal) were somewhat paralyzed by the lack of deal closure and all the possible implications it had on the market, depending on the outcome.

Overall, the interior regions market is relatively healthy, and it appears it will remain that way for at least the immediate future, if not beyond.

Prognosticating the Coastal Markets

Coastal grape markets are much more bifurcated, due to the plethora of market segments and price categories that are served by the supply. The most oversupplied segment of the grape/wine market prior to the pandemic and the two short crops of 2020 and 2021 was the coastal segment producing wines under $20 per bottle. While the small crushes of 2020 and 2021 certainly eased the supply pressure, that segment today remains the most likely to be cast into a position of oversupply with one big crop.

Simultaneously, huge challenges and opportunities exist as higher-end, AVA-based wine programs are very hot right now. For whatever reason, the pandemic seems to have spurred people into buying more high-priced wine (greater than $20 per bottle),



***(Standing - left to right)* Ed Nikssarian, Kevin Rogers, Joe Osterman, Kyle Collins, Jeff Bitter, Karl Lehman, Michael Haddox, Joey Biscay, Chad Clark**
(*Seated - left to right)* Marcia Silva, Alesia Zion, Pam Bond, Irene Ybarra

much of that being through DTC (direct-to-consumer) channels. Connected to this is the fact that the 2020 wildfires had the most devastating impact on the coastal regions of Napa and Sonoma, where a majority of the state's highest-priced wines come from.

Additionally, in Napa in particular, a very short 2021 crop contributed to a lack of supply to meet demand. Also, growers at the high end of the market have only been planting new vines at a rate quick enough to back-fill for attrition (i.e.: replants, not new additional acres). So, all these factors have caused the perfect storm to bring the higher end of the market into a well-balanced position. At this point, it seems highly unlikely one large crop would have detrimental effects on that segment of the market.

Now, back to the coastal segments producing wines priced mostly in the "teens." Demand for grapes and wines in this segment of the market strengthened significantly from that in 2019. But this segment of the industry continues to be faced with the reality of an extremely competitive marketplace, where margins are significantly squeezed. The demand for the product is there, but growers struggle to justify selling grapes at prices commonly offered by coastal buyers looking to preserve margins.

Because of the short crop, most grapes in this segment (perhaps with the exception of Pinot Noir) ended up being traded at levels acceptable to growers last year. But this segment remains on the edge of economic sustainability, with growers looking for prices to support rising costs and buyers looking to maintain margins in extremely competitive conditions.

Crop size, as the most important factor, will likely determine economic sustainability for growers in this segment in 2022 and beyond. With "shorter" crops, it is likely that prices hold and growers have a chance at covering costs. With "longer" crops, it is likely that markets become softened and growers (particularly those with grapes available in the end) are subject to prices mostly viewed as economically unsustainable.

It would be a fair and accurate assessment to say that the top and bottom segments of the grape market are in the healthiest positions moving into 2022 and beyond, with the "middle" of the market being in the most precarious at this point.

Winter Report - 2022

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ALLIED GRAPE GROWERS

Written for the growers and customers of
Allied Grape Growers

Inside This Issue

Allied Grape Growers (AGG) is a 500-member grower-owned winegrape marketing association. We exist for the purpose of effectively selling our members' winegrapes to grape buyers of all kinds throughout California. AGG is the leader in understanding supply-side dynamics in the California winegrape sector and uses that expertise to maximize results for its member-growers as well as to work with our buyers to properly plan for their growing supply needs. AGG has been in existence since 1951, with decades of proven leadership and value in the California wine industry.

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