Paulson's guide to investing in wine

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Jan- Erik Paulson,a fine wine merchant based in Waldkirchen, Germany, who has owned Paulson Rare Wine (www.rare- wine.com) for many years and also manages a Wine Investment Fund offers the following advice for would- be wine investors.

Wine is the most wonderful of drinks produced by the hard work of winegrowers to be enjoyed by wine lovers all over the world, but is it also suitable as a financial investment?

There are a number of arguments that speak for this, particularly after the negative experiences on the stockmarkets in the last couple of years. Wine is an asset just like gold or real estate. A great wine can never become worthless. If the worst comes to the worst you can always drink it. An advantage over real estate is that you can sell it bottle by bottle according to your needs. I have a customer who sells me a couple of bottles from his well- stocked cellar every year to finance his holidays. Anyone who has been buying the "right" wines at the right moment can show a very nice gain indeed.
There is a comparison where the increase in value of shares, gold and wine were compared over a period of 30 years. The prices of five selected Bordeaux wines, gold and the German share index was compared with a starting index of 1,000 units in the year 1971. The value of gold increased from 1,000 to 6,517 points from 1971 to 2001, the shares increased to 11,192 points and our selected wine portfolio to an amazing 162,323 points – more than tenfold the value of shares!

Which wines are suitable as investments?

Only wines of highest quality produced in limited numbers from a clearly defined area and with a long "life" ahead. The most important examples are the top wines from Bordeaux. These wines have proved their quality over centuries. Only a few wines from outside Bordeaux have investment potential, namely some great wines from Burgundy (e g Domaine de la Romanée Conti and Leroy) and Rhône (Jaboulet, Guigal and Rayas). White wines are only in very rare cases suitable as investments. Only the very best sweet wines come into question but these rarely obtain spectacular price increases due to their limited market.

Wines from the New World and fashionable new style wines do not in my opinion have the potential for a long term increase in value. The reason for this is the ability to produce an ever increasing amount of bottles and the lack of proof of their ageing potential.

Wine has been a source of speculation for centuries but the market for this has particularly in the last 20 years been very active.

The basic principle determining the value of a wine is the same as for just about everything else – the relationship between supply and demand.

What factors determine demand?

The demand for a wine first of all depends on its quality and the judgement of this by wine critics and other opinion makers. The American wine critic Robert Parker is still the single most important of his kind, particularly when it comes to determining the demand for en primeur trade where the wines of the latest vintage are offered in the spring after the harvest. The danger of investing in en primeur wines is the fact that the wines can develop quite differently and not live up to the promise of an early cask sample. It is no big secret that the most important wine journalists get to taste samples from selected rather than average casks. Another factor adding to the insecurity is that no one knows what following vintages will be like. The demand for a young wine will decrease if an even better vintage is to follow.

What factors determine supply?

The supply is the number of bottles of a wine available at a particular time. This is first of all determined by the amount of wine originally harvested – Pétrus or Le Pin are good examples of wines obtaining extremely high prices because of their very limited production. Secondly, the supply is determined by the age of the wine. A top wine from Bordeaux usually needs about 10 years to reach maturity, before this time only relatively few bottles will be drunk. The supply during the first years after the harvest is high and only after reaching maturity does the supply drop with each bottle enjoyed at dining tables all over the world. A third factor is the number of bottles actually being offered on the market – as long as the wine is being kept in private cellars rather than in the warehouses of wine merchants or wineries there will be increasing prices. Another determining factor is the willingness of private collectors to part with their treasures. This happens as a rule when they urgently need money, particularly after having made losses on the financial markets.

There are a number of important rules that one should follow to be succesful in this field:

1. Buy the right wines – a good knowledge about wine is of utmost importance.

2. Provide good storage condition – wines in imacculate condition will obtain better prices.

3. Buy and sell wine in their original cases. An unopened original case of a wine will achieve a higher price than a split case will.

4. Your profit will obviously depend on your ability to buy as cheaply and sell as expensively as possible.

A private person buying his wines from the trade pays the wine merchant's mark- up as well as VAT. On selling back to the trade the same factors will be taken into account in establishing the price being paid. It is clear that a wine needs to increase about 50% in value before any profit remains for the investor. By buying and selling at auctions a bit more gain is possible but there are insecurities regarding the condition of the wines and the final prices achieved.

Increasingly popular alternatives are the few Wine Investment Funds on the market. Their advantage is that experienced wine professionals are in charge of buying and storing the wines. These have good contacts in the trade and can therefore buy at better prices than the private individual. Some funds will also sell the wines and can as a rule achieve better prices.

There are two basic types of funds, those investing in mature wines and those speculating on the en primeur market. Anyone lucky enough to invest in a great vintage will see nice price increases during the first year but then nothing much happens over the following decade until it reaches drinkability. It could therefore make sense to buy at this point instead. First, because the quality of the wine is known and the future demand for it is therefore easier to judge. Secondly, as the prices only start to increase steadily from this point as we have seen above.

It is important in respect of all these funds to inform yourself of the seriousness and reputation of the persons in charge.

(Jan presumably would nominate himself as being extremely serious in this respect, though I have to say that he also does a nice line in circulating better jokes than most online. Football seems to be a specialist subject although parrots and golf occasionally feature.)