

# Wine a good investment, if you don't quaff the profits

Kevin Hassett

Wine lovers had a great year in 2006. First, we found out that resveratrol, a key ingredient in wine, may prevent ageing. Later, a study suggested that it may help prevent obesity and diabetes as well.

But now the news gets even better. If you are heading out to the store to buy a case of wine for a holiday party this week, you might want to have a look at the latest economic literature before you depart. If you do, you might buy a few extra cases. Maybe even a truckload.

Wine, it turns out, may be more fun to invest in than to drink. The only thing better would be the discovery that it induces kids to eat their vegetables.

A new paper by economists Lee Sanning, Sherrill Shaffer and Jo Marie Sharratt at the University of Wyoming investigated the returns that wine investors got. They collected "hammer price" data for auction results of red Bordeaux vintages rang-

ing from 1893 to 1998. They studied auctions between 1996 and 2003 and estimated risk-adjusted returns for individual wines.

The results were stunning. The holy grail for investors is an asset that delivers healthy annual returns, but doesn't have a great deal of associated risk.

The authors found that wine investments had almost no correlation with the market as a whole, yet had high returns. The average annual return for those who invested in Bordeaux was between 7.5 and 9.5 per cent higher than would have been predicted by factors that account for risk.

This meant fine wine, over that period at least, was about as good an investment as you could find.

Why? Economic reasoning suggests a number of answers.

First, fine wine is a luxury item. As societies get wealthier, citizens can be expected to consume more. Since 1996, the world economy has grown faster than anyone could

have predicted and this has driven up demand and prices.

Second, the finest wines have a scarcity value, which can snowball over time. Think of it this way: If you get a big positive shock to your income this year, you might celebrate with a fine Haut-Brion. If lots of people get positive shocks, then they will celebrate in the same way, and suddenly there is very little remaining Haut-Brion, and prices go through the roof.

This pattern is confirmed by data reported in the study, which details the excess returns are largest for the wines that have always been considered investment-grade splurges. The champion vintage was found to be 1966 Haut-Brion, which posted an average monthly return of about 7.5 per cent during their sample period, but 75 wines were found to have average monthly returns in excess of 1 per cent per month.

So should you invest in wine?

Maybe. A key problem with the study is that the biggest risk facing home wine collectors was excluded. After all, the authors' methods analysed the performance of buy-and-hold wine strategies. Holding risk, in my household at least, is very significant, indeed. No, it's not the lack of a quality cellar. The problem is, someone (I won't say who) keeps drinking the stuff.

It is one thing to buy a fine wine and cellar it with the intention of auctioning it off at a later date. It's another thing to successfully walk by it year after year without giving in to the temptation to uncork it.

Behavioural economics teaches us that individuals may buy with the intent not to consume, but then have a hard time maintaining discipline. Imagine what may happen to the value of your wine portfolio when you and your college chums head down to the cellar near the end of an already convivial evening.

If your friends are like mine, it would make the 1929 crash look like a hiccup. That lack of discipline cer-

tainly explains the high returns. Enough people have been uncorking the best vintages that their scarcity value has skyrocketed.

Wine returns might be positive even if most investors are losing money while consuming their profits. That's why alternative wine-investment vehicles have begun to pop up. For example, the Vintage Wine Fund is based in the Cayman Islands and managed by OWC Asset

Management Ltd, a London-based company.

The fund invests directly in top wines, most significantly from the Bordeaux region. According to its latest monthly report in October, 90 per cent of its assets were in red Bordeaux. The fund claims to have produced a return of 46 per cent since inception in 2003.

Given the latest research, one might expect funds like Vintage

would begin to hang their shingles in the US and subject their books to the scrutiny of US regulators. When that happens, it might not be a bad idea for everyone to put a little bit of wine in their portfolio.

One caution is in order. If wine-investment funds become widespread, it may actually lower future returns. After all, if every wine investor has his wine locked away safely in a mutual fund, then fewer

individuals will capriciously quaff their treasures, and scarcity values will surprise on the downside. The expected return in the future may be quite a bit lower than the high returns reported in the study.

In the meantime, it can't hurt to stock up.

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Fine wines, especially Bordeaux reds, have been sound investment since 1996 with returns of up to 9.5 per cent. Photo: AP

