Wine Business Solutions

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Time to Buy or Sell?

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A difficult question. The consensus of the research I've done in this area may not be what you'd think. Accounting firms, small business sales agents and specialist winery brokers all seem to agree that the horizon to sell even a small business is such that by the time you're ready, circumstances will inevitably be different. All seem to agree, therefore, that there is no ideal time. Anybody who was in the US around the time of the GFC knows that only too well. Accolade certainly found this out when Brexit scotched their IPO plans.

It's been hard for our clients, most of whom are based in Australia, New Zealand and South Africa, to sit on the sidelines and listen to how buoyant US wine business sales are. When you look at Gallo and Constellation paying a quarter of a billion US dollars each for either side of what was the Orin Swift wine business, you could be forgiven for asking – "Well then - where's my half billion?"

But with business picking up and most wine business owners, in the three countries we mostly service, in dire need of an exit plan in any case, I felt it important to write about buying and selling wine businesses.

We are wine business consultants, not real estate agents. This is an important distinction to make, I feel. Yes, we do get approached regularly to assist with the wine business sales process but WBS does not actively seek out wine business / brand sale transactions. There are businesses that specialise in that.

We prefer to stick to providing best quality advice rather than risk 'slipping over to the dark side' as those businesses so often tend to do. Better always, I feel, to;

- provide strategic advisory as to how to prepare a business for sale,
- determine who the logical buyer / seller set is,
- make relevant introductions,
- vet interested buyers / sellers and
- assist the family through the sales or acquisition process

than get directly involved in the sales transaction.

Our interest lies exclusively with that of our clients and our commitment is loyalty, beginning to end. (I may not end up as rich as I otherwise might, but at least I sleep well at night).

So, having reviewed literally hundreds of businesses from the buyer's side during my corporate career and having assisted numerous clients and their families through the sales process, what are the key things to understand when contemplating your exit from your wine business or part thereof?

Number one - Sustainability of sales. Many businesses fail to understand the critical nature of brand building. The ultimate consequence of this is that, when a potential acquirer scrutinises the sales histories of your various lines, by channel and by market (and they will), if there is not a steady build-up of sales driven by consumer demand then they will have trouble believing that any future sales will be sustainable. It's the football equivalent of going 'one out from the ruck' versus a sustained well-constructed strategic game plan.

Even if you're not planning to sell, the same rules apply. When dealing with investors, your bank, quality importers and other key business stakeholders - show them that you have a brand building plan. Show them how you apply it consistently. Prove to them that you're winning.

You would be amazed at how many clients we have, including some highly prestigious names, that say they are "in export", for example, when even a cursory glance at their sales figures shows that they are in fact in 'trading'. A Systembolaget (Swedish monopoly) listing, an airline supply contract or even, sad to say, a deal with a major US retailer, does not necessarily constitute sustainable sales.

Not that there is anything wrong with trading per se. Jim Moularadellis has built a world class bulk trading business that is the envy of his South African and South American competitors. His brother Bill has done the same in the own label space. DGB, does have good brands like Boschendal but when all is stripped back, it's pretty much a trading company.

Many businesses like Yalumba have strategically gone about setting up separate trading companies just to supply tactical opportunities. And that is the point. If not done strategically, if trading is simply the product of opportunism, then your brands and business are not going to be considered to be worth very much.

Number Two - Earnings. EBITDA (Earnings before Interest, Tax, Depreciation and Amortisation) is the most commonly used measure. Somewhat counterintuitively, businesses are not usually bought, as property is, based on the value of your assets. They are bought on their ability to generate sustainable cashflows utilising those assets or the assets of the new owner.

In most major business or brand sale transactions, you can almost think of the assets as incidental. The buyer can acquire assets any way they like. They may already have them. What they are really interested in is - can the business under consideration generate profits above and beyond the cost of capital invested? For most wine businesses (and for agribusiness in general, globally) that answer is "no", but it may be that the business and brands are more valuable to the acquirer than the owner.

That is why most businesses are bought on a multiple of earnings. Times 10 is the most bandied about figure in the wine industry but this can vary widely based upon just how much growth potential the acquirer sees.

Constellation paid the right price when it shelled out nearly $US300Million each for the Meiomi and Prisoner brands. They knew the current sales figures and trajectory, they knew what their own distribution network was capable of and they could add up. The billion-dollar question then becomes – "will they be able to sustain price?" – something that listed company's sales teams are notoriously bad at.

Why 10? Well think of it as buying ten years' worth of a company's future profits. Think also that it takes around 8-10 years to build up a sustainable business and that you are effectively paying the owners for that.

The discounted future cashflow methodology (which works out the value of future earnings based on the idea that a dollar earned tomorrow is worth less than a dollar earned today) is a way of 'idiot proofing' any multiple of earnings number suggested and should produce roughly the same figure, if calculated properly.

For the average wine business with turnover of $1Million or less, however, the discounted future cashflows methodology isn't applicable as there are simply too many variables to produce a reliable result. So, what do you do then? What if your business doesn't even make a profit – could it still be worth something?

If someone is looking to buy your brand, they may have a different cost base and it may be highly profitable for them. In that case, a simple figure of one times revenue could be used (revenue being around 10 times EBITDA for the average wine business). If they are buying stock, then a figure of 2 times Gross Profit could also be used as a benchmark (given that most wine businesses run a 50% Gross Margin or 5 times EBITDA).

There is always a way to come up with a number. And if the buyer is keen enough, they will. Take Lion's acquisition of Wither Hills. At the time of sale, Wither Hills was only selling around 45,000 cases. They had plenty of wine in tank so had room to grow. Wither Hills produce an EBIT figure based on forward projections and Lion were prepared to accept it. Brett and John Marris walked away with $NZ54Million.

Lion got to go to the press and say that they bought at the right multiple of earnings, after being badly beaten up in the media for paying too much for Petaluma, and the Marris family got what they wanted.

The key was that they were ready. They had the brand, they had the stock, they could guarantee medium term supply and they could demonstrate that the business could be highly profitable especially when a low level of corporate overhead was applied. Most importantly, they understood what that was worth to Lion. And they asked for it.

Number Three - Synergy – Whatever that means… It's an expression the gets thrown about a lot but it is one that, as an acquirer, you need to be extremely careful about.

It has often been suggested that the way forward for South African co-ops is mergers and acquisitions. Sometimes this can work. Those of us with long memories will recall how a broken-down co-op (the Berri Renmano Loxton Co-operative) merged with a near to broke Australian family company (Hardys) and within 10 years, became the world's largest wine company headquartered in Reynella, South Australia. Not bad. Constellation, of course, didn't understand what they had bought and thereafter destroyed around a $ABillion in shareholder value whilst doing nothing for the image of Australia but that is beside the point.

Most of the time, however, so called 'synergies' fail to be realised. This is one of the key reasons why most acquisitions destroy shareholder value. A wise man once said to me that in every M & A deal, there is a train and there is a tunnel. Best not to be the tunnel, if you catch my drift...

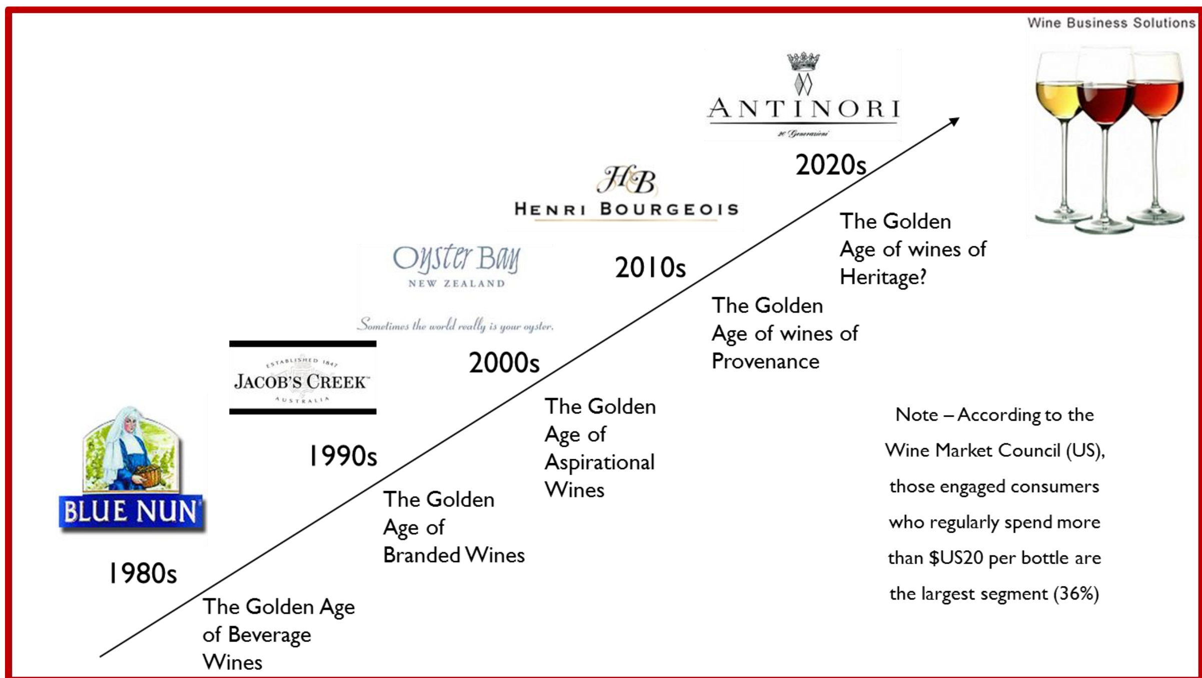
This is especially true where key personnel are concerned. It's often worst when sales people get involved. Where, on paper, there appears to be a perfect match between one business's sales team and the other, what often happens is more akin to a lion killiing every male in the pride. All of that 'synergistic business value' thereafter gets blown out the window.

Where M & A can work beautifully is between neighbours. We were advisors to the merger of the Wellington and Wamakersvallei Co-ops, a company with a total crush now around the size of McWilliams'. Working together started with the simple pulling down of a fence between the two production plants. With one professional management team, their overhead was immediately lowered and all outputs improved.

This of course gets harder when looking to merge disparate wineries. The large, listed global companies are shutting those down, all the time, in order to achieve ever greater scale in primary production facilities.

A better strategy, I think, is the relentless pursuit of quality and the use of acquisitions only ever in support of that single-minded goal. You can think of Willi Klinger's work at Domaine Wachau and that of La Chablisienne, the co-op responsible for around 25% of the production of Chablis, as prime examples.

This is because the way forward is not consolidation to compete within a part of the market that is dying. If, for example, your aim was to be the 2nd most 'successful' business after Accolade in the UK, sales volume wise, you could be AVL (McGuigan) with EBIT of less than $A5Million for the six months to December. Alternatively, if you were to aim up a level, in terms of consumer segment targeted, and chose to be the equivalent of Oyster Bay, their EBIT was $NZ50Million off roughly the same turnover during the same period. Now there's a ten times multiple for you...


Wine Business Solutions
ANTINORI
HENRI BOURGEOIS
Oyster Bay
NEW ZEALAND
Sometimes the world really is your oyster.
JACOB'S CREEK
BLUE NUN
1980s
The Golden Age of Beverage Wines
1990s
The Golden Age of Branded Wines
2000s
The Golden Age of Aspirational Wines
2010s
The Golden Age of wines of Provenance
2020s
The Golden Age of wines of Heritage?
Note – According to the Wine Market Council (US), those engaged consumers who regularly spend more than $US20 per bottle are the largest segment (36%)

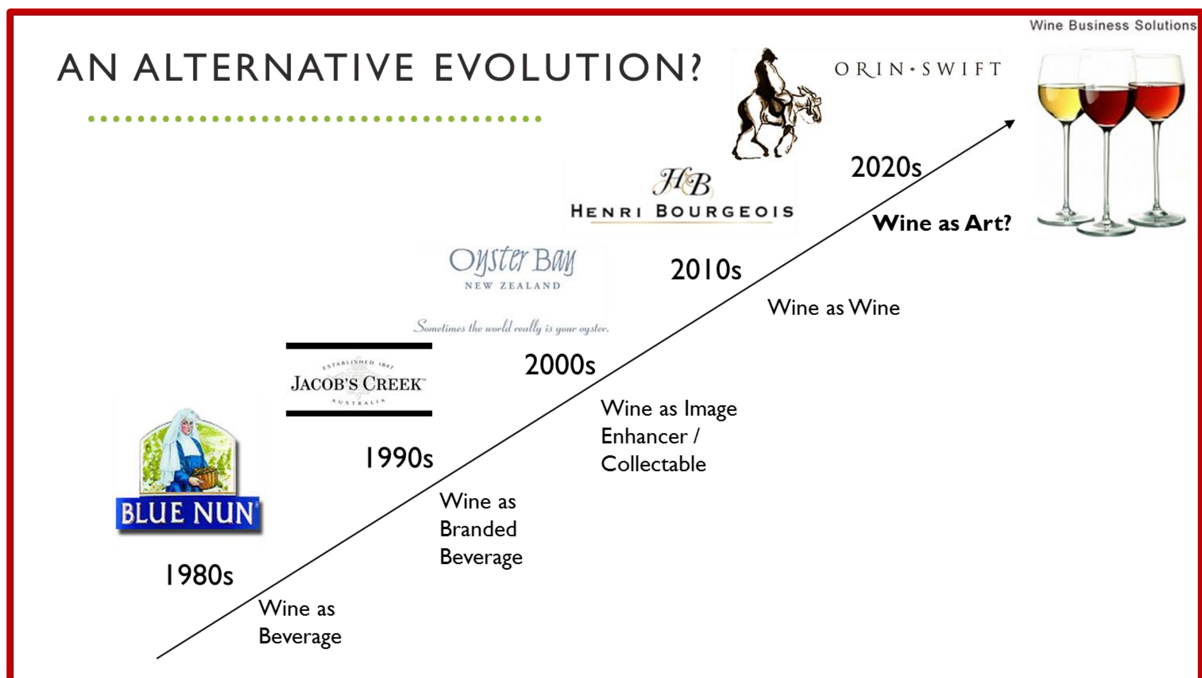

AN ALTERNATIVE EVOLUTION?
Wine Business Solutions
ORIN·SWIFT
HENRI BOURGEOIS
Oyster Bay
NEW ZEALAND
Sometimes the world really is your oyster.
JACOB'S CREEK
BLUE NUN
1980s
Wine as Beverage
1990s
Wine as Branded Beverage
2000s
Wine as Image Enhancer / Collectable
2010s
Wine as Wine
2020s
Wine as Art?

Photo taken at Orin Swift Tasting Room

1. Make selling your business a separate project to running your business. Allocate sufficient time to it. Know that there is a lot of work to do in setting your business up for sale.

2. Take family / personal objectives into account. Small differences now can build up nearer sale time and put the process at risk, or worse, lead to family conflict post sale.

   This typically involves putting in place a family succession plan well before broaching any sale. We're more than happy to facilitate the process. It's important to also realise that there is a legal component to this and as such, a law firm specialising in wine industry succession planning like Finlaysons is always a good idea. Wine Partner, Will Taylor, has a real passion for this and much experience in this area.

3. Know your buyer – the 'natural buyers' of your business will typically pay the highest price. They can often fully leverage those synergies referenced earlier. Identify who they are and how they assess value so you can prepare your business to maximise valuation and competitive tension when you sell.

   The market has been particularly tough in Australia. Realising this, a public listed company who was a partner in a brand joint venture with one of my clients thought that they, as 'natural buyer' and holding first option, could basically steal the company by not paying my client and causing them to run out of cash triggering a sale clause in their contract. (Hard to believe that anyone could be so evil, I know). My client cleverly introduced another buyer who was the market leader in the relevant product category (another type of 'natural buyer') and was able to achieve an excellent price as a result.

4. Make yourself redundant – if you are the key person running the business and your business operates at any sort of scale, you need to step away and hire management who can prove themselves for at least a year prior to sale. This will give future buyers comfort that the business won't fail without you.

   One of the saddest things I see, as I travel around the Southern Hemisphere, are 'Dads who won't let go'. Everyone needs to understand that there are more fun things to do in life than working. One of my clients has great respect for being both a brilliant winemaker and a humble man. When his Dad's contribution to our meeting was to serve us all bacon and eggs, it was obvious where that came from.

5. The best way to run any business is to operate it everyday as 'always sale ready'. So get some housekeeping done – sort out financial reporting and accounting, get your accounts audited, separate your affairs from the business and tidy up legal and operational risks.

Every business should have a set of management accounts that are different to your tax accounts in any case. Without proper management accounts, it is impossible for anyone to see where the business is going let alone for buyers to feel comfortable. Setting up a set of management accounts for a wine business is easy to do and we are happy to help. Very few accountants understand how do to this.

6. Work your EBITDA – Every sustainable dollar added to the EBITDA figure can be worth 10 times that or more in terms of the sale value of your business. Ideally, give yourself time to realise profit improvement initiatives and demonstrate their sustainability to buyers or investors.

   As we are always stressing, raising revenue is more important than cutting costs. Using those ratios that we have been working with throughout this paper, a 5% increase in revenue can easily mean an increase of 20% in EBITDA and, therefore, a 20% increase in the value of your business.

7. Leave something for the next owner. Buyers will pay more if there are opportunities for future growth, such as new products, geographic expansion, or new channels. Plan and partially implement these opportunities so that buyers can believe them and, therefore, be willing to pay for them.

   With few buyers about, one of the best ways to exit is leave some equity in the business so that aspiring young winemakers can get the start the banks usually won't let them have. It's how my father started and it's desperately needed. Fresh ideas and creativity are the lifeblood of any industry.

8. Don't be afraid to break up the assets. There is no disgrace in selling off the component pieces of your business rather than waiting, till you drop, for that person who will fall in love with the totality your unique dream. This can also be a neat way to scale down your involvement if there is no logical successor. In a struggling region in a depressed market, your land, equipment, buildings, restaurant etc. could be worth more than anyone is prepared to pay you for the total business.

9. Protect your sale proceeds. Proceeds you make from the sale will be after tax so make sure you have the right tax structure for sale. Draw up a wealth strategy to protect your proceeds for retirement and succession.

10. Above all do your homework – There are a relatively small number of people who are known to be in the market for wine businesses and brnads. Know who they are, know what they are looking for and why. Understand all the reasons people might find what you have for sale to be of value.

    You only get one shot at selling a wine business. Work it hard. We're here to help as always.

The "Top Ten Tips" for Building Better Wine Businesses.

One - Start by understanding your customer value proposition. Only part of this stems from your company's unique heritage and / or personality. To be successful, this needs to be strongly linked to what your customers ultimately want from the experience of your brands. There is some excellent research on this that is publicly available. Getting it right is therefore not out of the reach of small companies.

Two - Once you understand what customers value most, you can then remove what they don't want (thereby reducing costs and freeing up cash), focus your communication on what they do want (often at no additional cost), differentiate your company on the basis of fulfilling customer needs more accurately than any competitor (again, often at no extra cost) and raise prices (because your offering is more highly valued)

Three - Always be asking the question – "If I could start with a blank canvas today – what would our wine business look like?" It's all too easy to let existing assets, existing product lines and existing ways of doing things blind us to what it is that our consumers value most. Often, it's simplicity. Complexity usually adds to costs and often only serves to confuse customers. Retaining unnecessary or irrelevant product lines, assets or business processes is the worst contributor.

Four - Make everyone in the company accountable for securing customer preference. This is not just the job of marketing but of everyone in the company, the owner most particularly. Make this the focus of the way every employee innovates their job processes on a daily basis.

Five - Invest in relationships. This is particularly so with major distribution partners. Make sure sufficient time and money is invested before demanding results. Be prepared to invest up front in bringing them to your home base and entertaining them in order to build enduring friendships.

Six - Make all employees champions for profit. Develop a culture of honesty around net revenue. Make sure everyone knows the actual price achieved net of all discounts, rebates, bonus stock and anything else that might otherwise cloud the true profit picture. Keep them focused on reducing costs but let them know that a percentage increase in wine company revenue is, on average, twice as effective as the same percentage decrease in the cost of goods sold and 3-4 times as effective as the same percentage saving in operating expenses.

Seven - Optimise your pricing mix. Focus first on selling more, higher margin product in high value markets to high value customers. Beware of people in love with "big volume". Big numbers make for big stories but often mean a lot of running around for no additional profit.

Eight - Build better business intelligence gathering systems – most companies are good at monitoring their own press. Very few have effective systems in place to monitor competitors, track changes in consumer preferences and turn customer feedback into customer value added.

Nine - Build 5-10 year Strategic Plans, forecast rolling 12-month budgets, link them to the most relevant KPIs and tie remuneration to these, wherever possible. Everybody knows they should do this. Few do. The difference in the performance of companies that do is enormous.

Ten - Watch your cashflow – building a cashflow forecast is a relatively easy exercise with the right software and some quality assistance. Some people survive years of losses but you can only run out of cash once. In a cash hungry business like wine – Cashflow is not just King but Oxygen.

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