A CONVERSATION WITH

Robert Nicholson

A prominent deal-maker discusses the mergers and acquisitions climate

By Laurie Daniel

Robert Nicholson is a longtime player in the world of wine industry mergers and acquisitions, but he considers himself "first and foremost, a wine guy." Nicholson, who grew up southwestern England and studied enology at the University of Bordeaux, got his first wine job in 1972 as assistant to the export director of Louis Eschenauer in Bordeaux, where the company owned Chateau Rauzan-Segla and Chateau Smith Haut Lafitte, among others. From there, he went to work for Seagram's, then became vice president of Christian Brothers in the Napa Valley. After the winery was sold to Heublein in 1989, Nicholson decided to set up his own business.

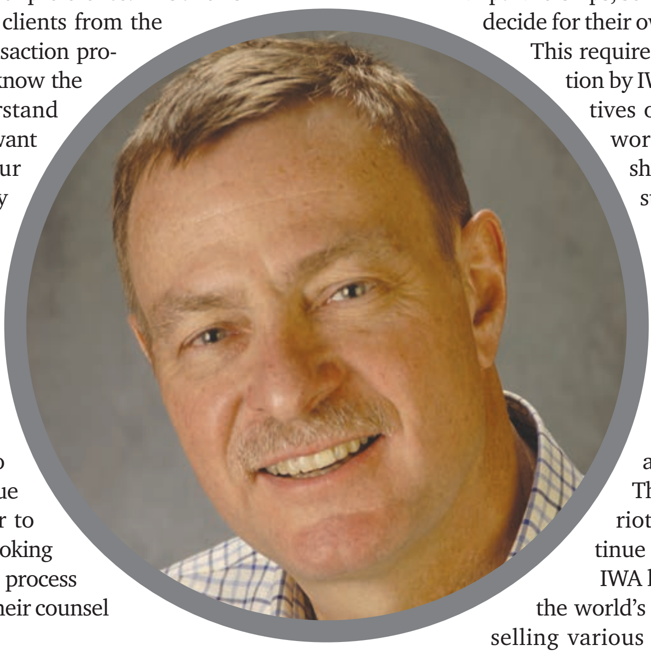
Nicholson founded International Wine Associates in 1990 as a wine industry consulting firm. Heublein asked Nicholson to help the company sell some assets in the Napa Valley, including the Greystone building that had been home to Christian Brothers (sold to the Culinary Institute of America) and the Oakville winery that's now Napa Wine Co. "That's how we started in M&A," Nicholson says.

International Wine Associates (IWA) has completed more than $1.5 billion in transactions to date (more than 60 separate deals, including prominent wine estates and more than 5,000 acres of vineyards) in California, Washington and Oregon. Recently IWA completed the sale of Calera Wine Co. to TSG/Duckhorn and the sale of Germain-Robin luxury California brandy to E. & J. Gallo.

Q International Wine Associates mostly represents sellers. Why?

Robert Nicholson: That's simply our preference. This allows our company to work with our clients from the beginning to the end of the transaction process. We take the time to get to know the sellers personally and to understand their businesses and what they want to achieve in a transaction. Our transaction process at IWA is highly personalized and confidential. Some steps we take with all our clients are the same; however, each project is very different.

Generally, this personalized transaction process includes first understanding the business thoroughly, valuing the different components of the business in order to help the sellers with realistic value expectations and help the seller to understand what the buyers are looking for in a transaction and how the process works. We assist our clients and their counsel throughout the process.



Winery valuations are based on brand scale, cash flow and margins, future volume potential, synergies for the buyer in their sales, marketing and production, and product types and origin. Brand strength is a combination of current margins, volume and the potential of the business for the buyer. Synergies are the savings that will accrue to the buyer post-close, giving buyers the option to use their own current resources more effectively in the acquisition of a business.

Q What are the reasons individuals or companies decide to sell?

Nicholson: As you can imagine, there are lots of different reasons why people and companies decide to sell their businesses.

Take family businesses: Sometimes a founder has developed a business, and then when the founder wants to retire, and other family members are not in a position to or don't want to continue managing the business. This can be a difficult decision for a small business. It is IWA's role to understand their objectives and to advise them accordingly. It can be challenging for the owners, as IWA makes them aware of the different steps required to accomplish a smooth transaction at an acceptable market value. Over the years, IWA has represented a number of prestigious family-owned wine estates for sale, including the Ladera Vineyards sale by the Stotesbery family to PlumpJack in 2016, the Talbott Vineyards sale to Gallo for Robb Talbott and his children in 2015, the Klipsun Vineyards sale on Red Mountain in Washington to Terlato in 2017, and the Hogue Cellars sale by Mike Hogue and his family to Canada's Vincor Group in 2001.

With partnerships, sometimes the partners in a business decide for their own reasons that they want to sell. This requires sensitive handling of the situation by IWA to achieve the different objectives of all the stakeholders. IWA has worked with a number of partnerships in the sale of their businesses, such as Beaux Freres Vineyard in Oregon, which was owned by Robert Parker and his partners. Beaux Freres was sold to the French group Maisons & Domaines Henriot earlier this year. One of the original partners wanted to stay on with Beaux Freres to manage the business and as a shareholder with Henriot. This worked out well, because Henriot was pleased to have him continue with Beaux Freres.

IWA has also represented a number of the world's largest listed wine companies in selling various brands, assets and businesses.

These projects typically include assisting the company in the process of how to achieve their objectives at the proposed valuations in the sale of a group of assets. For example, will a sale of the assets bundled together be more interesting to buyers (and to which buyer groups) than selling the assets individually? IWA represented Diageo in the sale of the Greystone Building in St. Helena (Calif.) to the Culinary Institute of America in 1993, the sale of Chalone Vineyards to Foley in 2016, and the sale of Edna Valley Vineyards to Gallo in 2011. We worked with Constellation to sell a group of wineries, brands and vineyards that included Geyser Peak, Buena Vista, Gary Farrell, Atlas Peak, Columbia Winery, Covey Run and Ste. Chapelle to a private equity group in 2008. More recently, we represented Treasury Wine Estates in the sale of the Blossom Hill Winery in San Benito County (Calif.) to Delicato this year.

Sometimes IWA works with privately owned or closely held wine companies in the sale of vineyards, brands and other assets. One example of this was Randall Grahm of Bonny Doon Vineyard's sale of the Big House brand to The Wine Group in 2006 and his sale of Pacific Rim Winemakers in Washington state to Banfi in 2010.

Q Walk us through the advice and guidance you give to sellers.

Nicholson: All transactions are complicated and require integrity, teamwork and planning, finesse, forethought, patience and commitment from all stakeholders.

The process of selling a family-owned or private business can be an emotional and stressful time for the owners. IWA's job is to stand with them throughout the transaction, from start to finish, and where possible to simplify what is a complicated process that inevitably has a number of twists and turns.

At the start, we help our client put together the "deal team." This includes IWA as the "quarterback" to manage the process for the seller. We often suggest that the seller identify someone in senior management who can be brought into the process. We work with that person on the in-house data collection, so we can understand the business. We recommend that the seller engage a transaction lawyer who has experience in the legal aspects of completing the sale of a business. The winery may have worked with a lawyer on regulatory issues, but that person often doesn't have experience with transactions. Generally, our initial preparation work with the seller includes improvement of the data collection, cleaning up the balance sheet, working with the company's CPA on financial statements, dealing with unsalable inventory, making sure all key agreements are in writing, reviewing and confirming trademarks and permits, guiding the seller to an appropriate estate- and tax-planning adviser to manage the proceeds from a transaction, reviewing and identifying assets that are to be retained by the seller and discussing the post-close plans for the seller. For example, do they want to remain with the business? The valuation or analysis of the brand and business is one of the first steps we take with our clients, followed by development of the information memorandum and offering documents.

Once IWA has completed the pre-planning, we finalize the target list and initiate blind approaches. IWA is very selective about the number and quality of targets we approach on behalf of our clients in order to maintain confidentiality, which preserves value for our clients. Following receipt of signed non-disclosure agreements from each target buyer, we send out the offering information memorandum. We then work with interested buyers as they develop their non-binding indications of interest, which summarize the details of their offers. We work with the seller to select the target (or targets), and with their legal counsel we work on drafting a letter of intent that commits the seller and the buyer to one another to complete the transaction. IWA manages the due diligence process, and we work with both sides to draft the sale agreement.

IWA works with the seller on preparing for the close of the transaction. This includes, among other things, managing the final inventory count with the buyer, working with the seller, their employees and the buyer on the transition to new ownership—and all other outstanding items to ensure a smooth transition. Typically, the whole process takes six to 18 months, depending on the complexity of the circumstances.

Teamwork throughout the process is critical to maintaining momentum and avoiding delays, because all deals have a life of their own. It is important to control the issues as they come up and, where possible, to pre-plan the different steps rather than reacting to issues as they come up.

The most fundamental requirement to complete a deal successfully is to maintain integrity and trust with all the stakeholders. Confidentiality is of critical importance to avoid erosion of value for our sellers.

Q What's the general state of mergers and acquisitions in the wine industry these days?

Nicholson: Generally, the U.S. wine market is strong. Valuations are firm and increasing in certain areas for some assets. Some super- and ultra-premium sub-segments of the market are stronger than other sub-segments, but wine consumption is generally increasing.

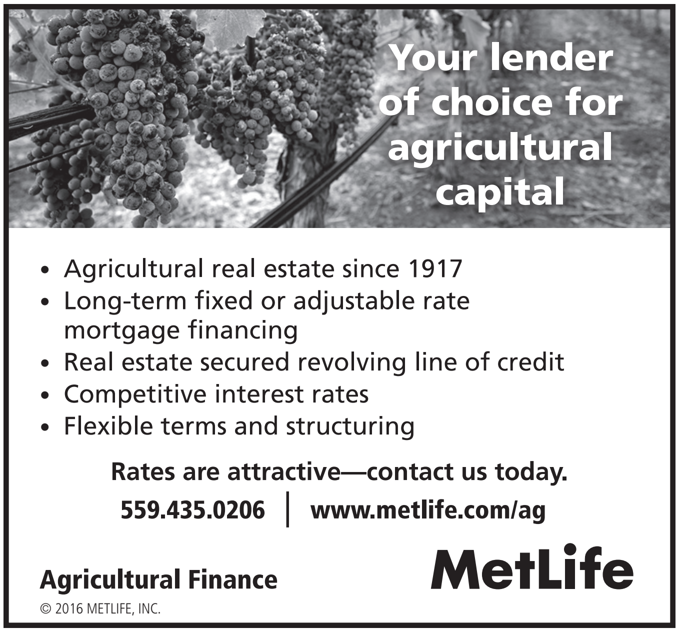
Wine companies are investing in vineyards to protect their supply and to maintain margins in a tight grape market. Financial groups are investing in vineyards

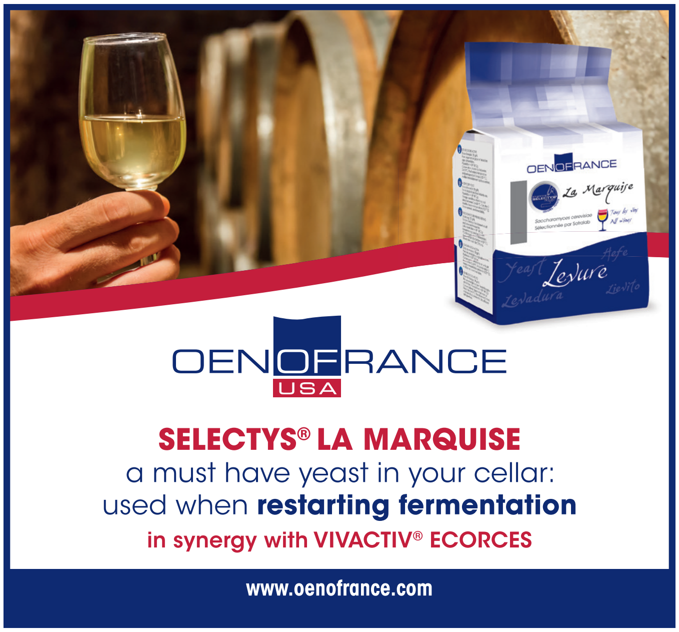
ON THE HORIZON

Robert Nicholson of International Wine Associates can't get into too many specifics about deals he has in the works, but he will say that he's representing "a variety of sellers" along the West Coast.

"We have a number of high-quality, ultra-premium wine estates in the Napa Valley, Sonoma County, Central Coast and Oregon," Nicholson says. He's also representing entities who want to sell vineyards in the Napa Valley, Sonoma County, the Central Coast and Washington, and he's working to sell "some substantial winery assets."

As for vineyards, Nicholson says buyers are particularly interested in Pinot Noir and Cabernet Sauvignon from prestigious AVAs—Russian River, Sonoma Coast, Santa Barbara, Santa Lucia Highlands and Oregon for Pinot; Napa Valley, Alexander Valley and Washington's Red Mountain for Cabernet. They also are looking for Chardonnay from "certain parts of Sonoma and the Central Coast."





to service the grape needs of wineries. Grape prices are increasing in super- and ultra-premium AVAs, and buyers are looking to protect their long-term supplies for growing brands. Wineries are faced with either buying and owning vineyards or securing supply with long-term contracts. Most wineries decide on a combination of both strategies. This is increasing pressure on land available for vineyards in certain AVAs.

As for wineries, many wine companies are looking to acquire wineries to expand their portfolios and compete more effectively in the market. In order to broaden values firm and increasing for most assets. For U.S. buyers, acquisitions improve their market leverage and are an opportunity for portfolio expansion into new categories. For international buyers, acquisitions improve their access to U.S. distribution and their asset diversification. All buyer groups are active now.

Q Who are the buyers?

Nicholson: IWA represents sellers. However, in order to manage the sale process in a confidential manner for our clients and make highly targeted approaches to select buyers on behalf of our

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their offerings to the market and to improve their leverage with both wholesalers and retailers, many wine companies are now looking to make acquisitions that complement their current offerings.

A shortage of winery production capacity in California's North Coast has resulted in some sizable transactions, such as the Jackson Family 2012 acquisition of Sonoma County's Carneros Hills (formerly Buena Vista Winery) as well as Gallo's acquisition of both Napa County's The Ranch Winery in 2016 and Sonoma County's Asti Winery in 2015. A smaller example is the Huneeus Vintners' acquisition of Sonoma County's VML Winery in 2016.

We see that public wine companies often prefer to buy brands only and to remain "asset light," keeping their assets off their balance sheet to improve ratios. Recent examples would be Constellation's 2016 acquisition of The Prisoner and Treasury's 2016 acquisition of the Diageo wine business, where they inherited a lease with a REIT (real estate investment trust) on most of the assets.

There are few distressed sales now. Since the Great Recession, the real market has returned, with clients, IWA is continuously in direct contact with all the different buyers to know what they want to acquire (and what they don't want to acquire) and why.

Owners of prominent wine companies and estates in the U.S. constitute one group of buyers. Multi-national companies like Constellation and Treasury are also buying.

There are also financial buyers and equity funds. For example, Farmland is a real estate investment trust that acquired Olsen Agriculture in Oregon. Other recent transactions involving this type of buyer include TSG's acquisition of Duckhorn and GI Partners' purchase of Far Niente.

Luxury goods companies are also buying. Chanel, for example, bought St. Supéry.

Finally, there are the owners of prominent overseas wine estates like Henriot in the Beaux Freres deal. IWA also sold two prominent Oregon vineyards to Louis Jadot, the Burgundy producer.

A resident of the Santa Cruz Mountains, Laurie Daniel has been a journalist for more than 35 years. She has been writing about wine for publications for more than 21 years and has been a Wines & Vines *contributor since 2006.*