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M&A INTERNATIONAL INC.

Wine Industry M&A Outlook: Will 2011 and 2012 Be Good Vintages?

2011

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Executive Summary

The last few years have been challenging for the wine industry. Companies have had to overcome a supply glut, weaker demand and increasing cost pressures. Many players have turned to M&A in order to counteract these headwinds. In the near term, such cost-driven M&A is likely to continue as key players attempt to right-size their businesses and improve their market position in growth markets.

The industry's long-term growth story remains intact. Wine consumption will continue to grow, driven largely by strong economic growth in the Asia Pacific region as well as a growing appreciation for wine in the US. Encouragingly, wine supply and demand will likely reach an equilibrium in the near term. We believe that improving industry fundamentals will encourage both wine producers and distributors to pursue M&A in order to position their businesses to better capitalize on this uptrend.

Reasonable valuations

"In our opinion, M&A opportunities exist in both emerging and mature markets, with an increasing demand for international appealing brands that have had limited exposure so far. We see many acquisition opportunities which are reasonably valued although it must be said that valuations are recovering."

Ruud van Hoek
Head of M&A International Inc.'s Food & Beverage Group

M&A activity overview

Despite the global financial crisis, deal flow within the wine industry has been surprisingly robust. From 2007 to 2010, there were 399 deals targeting wine producers with a combined value[1] of $6.5bn in the sector. Most of these deals have been relatively small in size, with the notable exception of Pernod Ricard's $9bn acquisition of V&S Vin & Sprit in 2008. This is unsurprising, as the industry is highly fragmented and a number of smaller companies have been struggling with a difficult operating environment. Decreasing wine demand as a result of the financial crisis and overproduction have exacerbated preexisting supply/demand imbalances, placing companies under financial stress and serving as a catalyst for M&A.

The challenging macroeconomic situation has encouraged companies to adopt varying approaches to investment in the industry. The most significant determinant of a wine producer's strategy towards M&A seems to be its size. Most large players in the spirits sector saw significant growth in their lower-end brands during the recession as consumers traded down. However, these companies are now seeking to shift their focus towards the development of more premium product lines (with higher margins) by divesting many of their lower-end assets. For example, Constellation Brands, Fosters and Pernod Ricard have sold wine assets in order to concentrate on developing premium product lines. In contrast, medium-sized producers have doubled down and are aggressively expanding their product portfolio by acquiring new wine assets. This is being done in an attempt to achieve economies of scale. Unsurprisingly, a number of smaller producers have been struggling to operate in the current environment and have explored offering themselves up for sale. Historically, the catalyst for M&A for wine producers has been an attempt to achieve economies of scale in order to combat the sector's higher cost structure when compared with the spirits industry.

Over the past decade, M&A within the wine distribution sub-sector has focused on addressing the logistical issues present in selling and distributing wine. These largely stem from the fact that wine companies tend to have a large number of SKUs (stock keeping units) due to a wide variety of grapes and vintages. This leads to sizable amounts of inventory and higher storage, distribution and marketing costs. Deal flow within the sector has also been the result of distributors attempting to diversify their key brands and wine producers seeking to integrate distribution into their existing operations. Between 2007 and 2010, a total of 130 deals targeted wine distributors with an overall deal value exceeding $1bn.

[1] Deal values throughout this report refer to Enterprise Value = value of the shares + value of the incorporated debt.

Future M&A prospects

The ongoing economic recovery and an improving supply/demand balance will encourage wine producers to once again attempt to derive economies of scale through M&A. The highly saturated traditional wine markets of Western Europe and Australia seem to be the best candidates for consolidation.

Though cross-border M&A was very low during 2007–2010, we believe that this will be a major driver going forward as wine producers seek to increase exports to existing markets and broaden the geographical diversification of their production facilities in order to limit their exposure to country-specific risks such as poor harvests or overproduction. While opportunities exist in both developed and emerging economies, those in developed markets are more attractive from a valuation perspective.

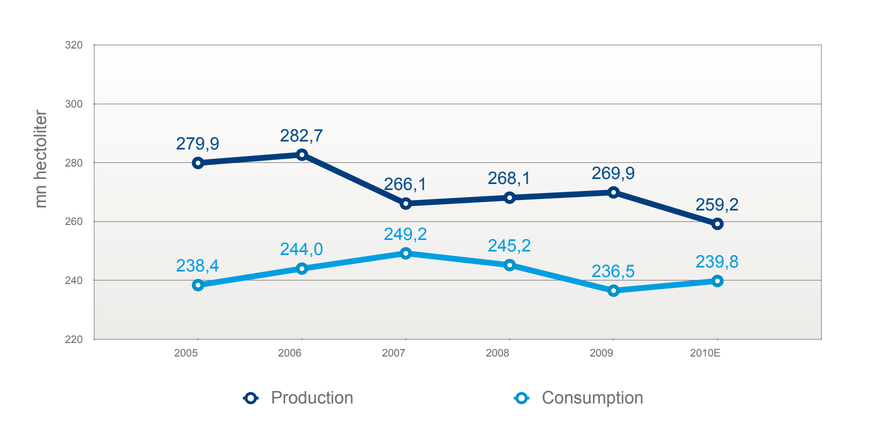
The wine distribution industry is likely to continue to consolidate. However, companies are now taking a more nuanced approach to their M&A strategy.

They are focusing more heavily on pure-play distributors instead of companies that operate across the value chain (i.e. marketing operations). Therefore, the focus for future acquisitions will likely be on asset rich companies, such as those with significant delivery networks and storage facilities.

Wine Industry: Just a Bump on the Road

The recession hit wine sales hard, widening the gap between production and consumption. Consumers not only cut back and consumed less but also traded down to cheaper brands. With the worst of the economic downturn now over, wine demand is expected to recover. We believe that the industry has a bright future as a result of an improving supply situation, the growing success of New World wines, increasing demand in the Asia Pacific region due to westernization and a renewed interest in home consumption.

Figure 1: Wine industry: moving towards an equilibrium



Source: OIV

Wine producers: recent trends and developments

(i) An improving supply situation

Western Europe is the world's largest wine producing and consuming region, accounting for 47% of total sales volumes and 49% of total sales value in 2009. However, changing drinking habits have led to decreasing consumption in the region, particularly in mature markets such as France, Spain and Italy. This situation has been further exacerbated by the recession and associated reductions in discretionary spending. Such weak demand dynamics have led to oversupply. Recently, the EU has intervened to help restore the supply/demand balance. According to Euromonitor, approximately 35% of the EU's annual wine budget is spent on the disposal of surplus production. This comes largely in the form of payments which are offered to wine producers to destroy vines. For example, France has provided €47.2mn ($64.7mn) in compensation for over 7,000 hectares (17,000 acres) of vine removal. As a result, production in France, Italy and Spain fell faster than sales between 2006 and 2009, with production falling by 10% and sales dropping by 6%. Over the past few years, Australia has suffered from overproduction as well, although the country's production declined by 12% in 2009 due to the financial crisis. North America has enjoyed a steady increase in both consumption and production, with overall consumption far exceeding production while Latin America reported a decline in both production and consumption between 2006 and 2009.

(ii) Recession and recovery: moving towards a supply/demand equilibrium

Wine sales were lackluster in both 2008 and 2009, declining for the first time in decades. Aggressive pricing by manufacturers and retailers via heavy discounts improved affordability and stemmed the decline although to the detriment of margins. According to the International Organization for Vine & Wine (OIV), global wine output is estimated to have fallen by 3% to 6% in 2010 (Figure 1), resulting in the lowest production levels since 2002. OIV expects these production declines to go a long way towards resolving the supply surplus in the near term: the US is projected to report a production decrease of 9% in 2010 and Europe is expected to see a decline of 6%.

(iii) Global alcoholic beverage firms reassessing their wine strategy

The wine market is very fragmented. The top 10 companies accounted for just 13.5% of total sales by volume in 2010. The largest player is Constellation Brands, which has a 3% market share. While consolidation has been these companies' long-term M&A strategy, players have recently tweaked their approach in order to lessen the impact of the recession. Their discount brands have been selling well. However, this segment is very competitive with a number of unbranded and private label wines available in many markets. As a result, global alcoholic beverage companies (e.g. Diageo, Pernod Ricard and Bacardi) and major wine producers such as Constellation Brands have recently experienced margin degradation. In order to counteract this, producers have begun to divest their lower-end offerings to focus on premium brands, i.e. over $12/liter. For example, Pernod Ricard recently sold its wine business in New Zealand while Diageo entered into a sale-leaseback transaction for its wine business. In addition, Fosters is considering disposing of its wine operations.

(iv) New World wines — the threat from down under

Wine sales grew an unimpressive 1% CAGR between 2004 and 2009. However, during this period sales of New World (i.e. wines from the US, Argentina, Chile, Australia and South Africa) have seen significant growth. New World wines have built a strong reputation as high-quality products at attractive price points. These wines have gained share at the expense of more expensive wines from traditional Old World wine-producing countries such as France, Italy and Spain.

New World producers have used aggressive marketing and simplified labeling to make their products more appealing to young urbanites, a market segment that has been largely responsible for their strong sales growth. Wine producers have attempted to make wine more accessible and convenient by using a wide range of sizes and alternative packaging formats. In contrast, Old World producers have been reluctant to experiment with either their labels or packaging, fearing that this would undermine their premium status. We believe that in the near term, most of the growth in wine sales will occur at the lower end of the price spectrum ($4-13.5/liter) though demand for premium wines should also recover in tandem with the economy.

(v) Looking east for new opportunities

China has been a stellar example of the growing appetite for wine in developing countries. According to Euromonitor, wine sales in China increased at a CAGR of 12% between 2006 and 2009 compared with only 1% for the industry as a whole. In addition, 2010 sales growth is expected to come in at 13%. Chinese producers have focused largely on value offerings (at lower price points) leaving the premium niche open to foreign brands. Between 2003 and 2008, imports increased by 299% in volume but 856% in value, indicating that domestic consumers have been trading up from locally produced to foreign brands as

well as drinking more wine as a result of increasing westernization.

A number of international brands have been taking note and tailoring their strategy to take advantage of China's growth potential. A number of elite vintners, including Spain's Torres and France's Lafite, are either establishing their own vineyards in China or partnering with local producers to gain access to the country's medium-high quality wine market.

(vi) Stocks, bonds, derivatives…and wine?

Investors have increasingly come to recognize the lack of correlation between the value of wine and changes in the prices of financial assets. This has made the inclusion of wine in investment portfolios increasingly common. With older wines irreplaceable, vintage wine prices increased even during the worst of the financial crisis in 2008 as evidenced by various wine indices. Portfolio managers and cash rich investors were active in the market, with auctions in Hong Kong during 2009 and 2010 setting new price records.

The outstanding 2009 vintage, rising demand from Asian investors and a weak Euro will likely ensure continued interest in wine as an investment.

(vii) A newly found focus on value

Wine sales can be broadly broken down into off-trade sales (i.e. from supermarkets and retailers), which account for approximately 70% of sales by volume, and on-trade sales (e.g. in hotels, bars and restaurants), which account for the remaining 30%. The recession has led to an increase in consumption of wine in the home. This has led global off-trade sales to increase modestly in contrast with a decline in on-trade sales of around 1% in 2009.

The shift to off-trade sales has been particularly challenging for producers of premium varieties of wine (e.g. LVMH and Rémy Cointreau) as these wines tend to be consumed more frequently in public settings. In contrast, private label wines and companies, such as the Wine Group and E&J Gallo, have performed well as consumers have traded down. Consumers have increasingly come to prioritize aesthetic appeal, practicality and affordability. In response, the industry has increased its reliance on simplified branding, alternative packaging (e.g. bag-in-box and small barrel formats) and discounting. In order to encourage consumers not to trade down, several premium brands have introduced smaller bottles to make their product more affordable.

Wine distributors: recent trends and developments

(i) Shift to off-trade and discounting affecting margins

Distributors are largely at the mercy of domestic wine consumption trends outside of their control. Record low industry sales in 2008/2009 seriously impacted distributors. These companies were also hard hit by a mix shift towards off-trade channels and the use of heavy discounting in order to move inventory.

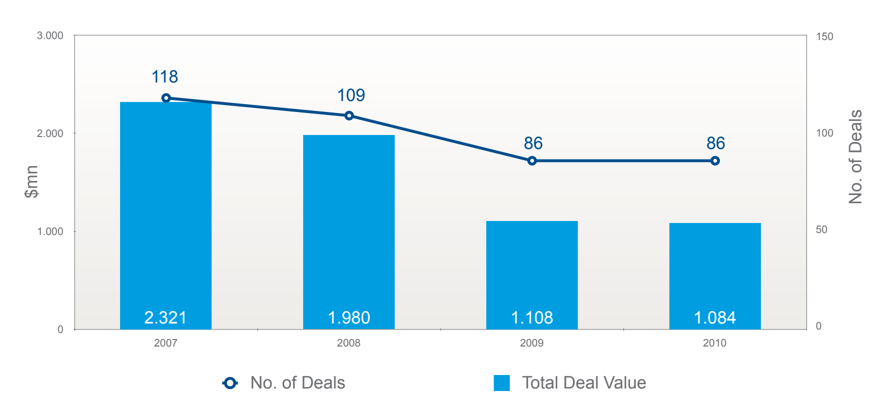
(ii) Threat from internet sales

Historically, distributors have not sold their products on the internet and are generally opposed to attempts by suppliers to direct-ship wine. However, internet retailing grew by a 20% CAGR between 2004 and 2009, posing a threat to distributors' business model.

(iii) Less of a focus on exclusivity

In response to the recession, a number of distributors have decided to forego exclusive relationships with major suppliers in order to avoid undue dependence on a single brand. This has led to increasing competition among distributors and, in turn, a focus on consolidation. As a result, M&A activity in the space has remained high despite the recession.

Figure 2: Value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

Note: 1) Total deal value and average deal value in all figures excludes Pernod Ricard's $9bn acquisition of V&S Vin & Sprit in 2008.
2) The review period for all figures is 2007 to 2010 unless stated otherwise.

M&A Overview & Analysis: Wine Producers

The recession has had a material impact on M&A activity in the sector, with the total deal value declining at a CAGR of 22% and total deal volume falling at a CAGR of 10% between 2007 and 2010 (Figure 2). Average deal size has also fallen significantly. We believe that many sellers are sitting on the sidelines waiting for improving valuations.

There are four key trends in the sector which are driving M&A activity:

(i) Large wine producers are restructuring and consolidating their operations by selling non-core assets, in particular lower-value brands and vineyards.

(ii) Premium wine brands are diversifying their portfolios by acquiring wine which sells at lower price points ($10–19.99/liter).

(iii) Smaller companies that are struggling to cope with the increasing effort required for selling and marketing are shedding assets.

(iv) Opportunistic bottlers and distributors are taking advantage of lower valuations to acquire premium wineries, offering wines at prices exceeding $20/liter.

We expect that these four drivers will continue to underpin M&A activity in the near term. Additionally, we believe that there will be a significant increase in M&A activity targeting cash generative standalone wineries located in prime wine producing regions.

Assets attractively valued but sellers holding out

Both M&A volume and valuations have been significantly affected by the recent credit crisis, an oversupply of wine and declining consumption. Deal valuations have fallen significantly since 2007, declining at a CAGR of 15% to an EV/Revenue (EV =Enterprise Value, i.e. value of the shares + value of the incorporated debt) ratio of 2.7x (Figure 3). Over the same period, deal volume has decreased by 10%. Average deal value has also fallen at a CAGR of 11% to $35mn.

After declining steadily for three years, deal volume in 2010 remained unchanged compared with 2009 at 86 deals. Average deal value also remained steady in 2010. On the other hand, valuations (EV/Revenue) continued to decline. We believe that M&A activity has bottomed and will likely increase in the near term.

The current environment seems to be an ideal time for opportunistic buyers looking to acquire choice assets and brands, especially if they are willing to offer a slight premium to induce sellers.

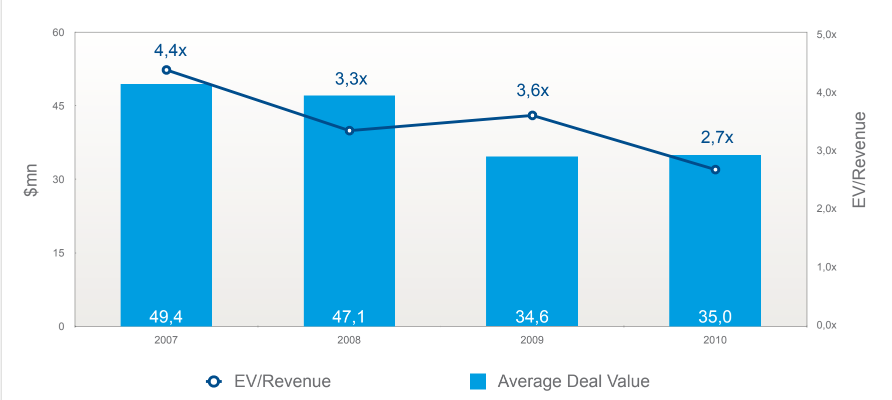
M&A Trends & Opportunities by Region: Wine Producers

Most M&A activity has been concentrated in Europe, which accounted for 56% of total deal volume between 2007 and 2010 (Figure 4). This is largely in line with the region's share of total wine sales (57% of total 2010 sales according to Euromonitor). Deal activity has been concentrated in the traditional wine producing countries of France, Spain and Italy. Asia Pacific reported the second highest level of M&A activity, accounting for a 21% share, with Australia accounting for the highest number of deals in the region. During this same period, 17% of transactions were in North America, which had the highest average deal value due to extremely strong demand for wine.

Europe: leading M&A activity

Western Europe, one of the world's largest wine producing regions, accounted for 55% of total wine production, 47% of total sales volume and 49% of total sales value in 2009. Despite significant global demand for wine produced in these countries, the industry is mature in Western Europe leading to declining consumption. Additionally, the oversupply situation worsened as consumers reduced consumption during the recent recession as a result of changing drinking habits and economic headwinds. M&A activity in the region also declined. Between 2007 and 2010, total deal value and volume decreased annually by 49% and 15%, respectively (Figure 5). Despite this, Europe continues to remain the leader in terms of deal volume.

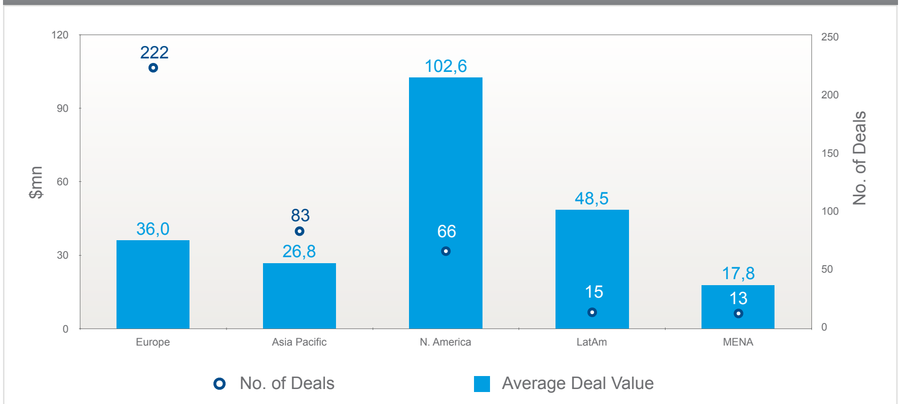
Figure 3: Average deal value and valuation



Source: Copal Analysis, Capital IQ

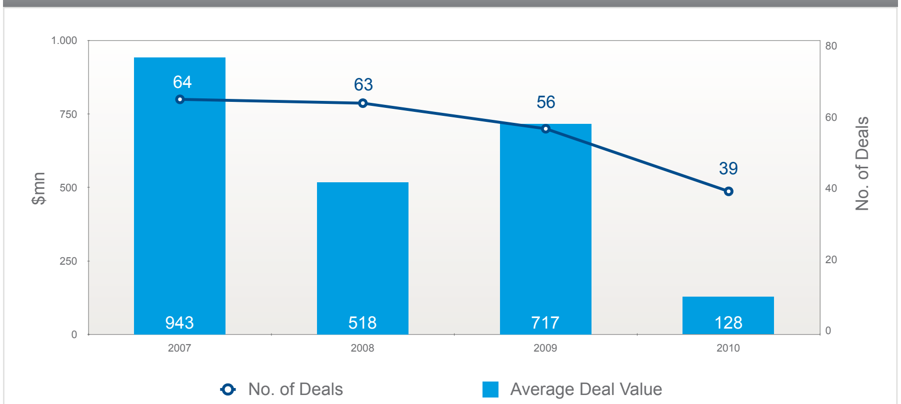
Note: EV = Enterprise Value, i.e. value of the shares + value of the incorporated debt

Figure 4: Value and volume of M&A transactions by region 2007–2010



Source: Copal Analysis, Capital IQ

Figure 5: Europe: total deal value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

France: trading up despite the recession

M&A deal volume in France accounted for 42% of all such transactions in Europe and 35% of total deal value between 2007 and 2010.

➜ Average deal value has fallen sharply since 2007 (Figure 6) despite Société Paul Ricard's $443mn acquisition of an additional 3.74% stake in Pernod Ricard from Kirin International Finance, Netherlands in 2009.

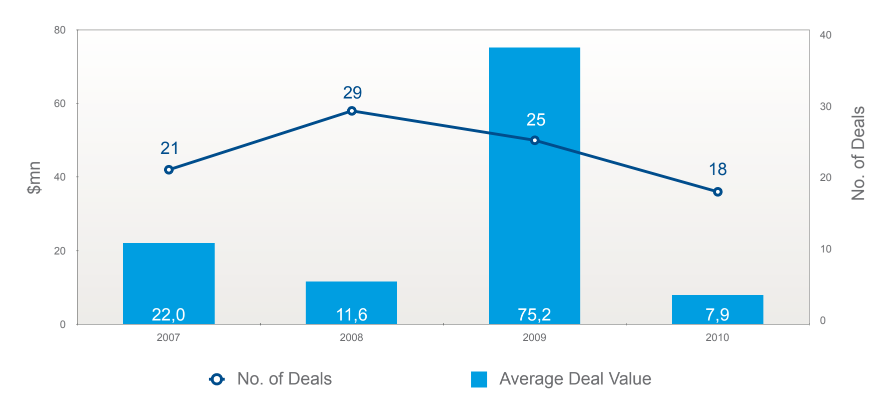
M&A activity in 2008 was supported by a general decline in valuations due to the economic recession. The most noteworthy deal in 2008 was Moet Hennessy's (LVMH) $38mn acquisition of Champagne Montaudon, a premium champagne producer.

Switch in consumption

"The switch in consumption away from bars and restaurants to the home has significantly affected premium brands which tend to benefit most from on-trade sales."

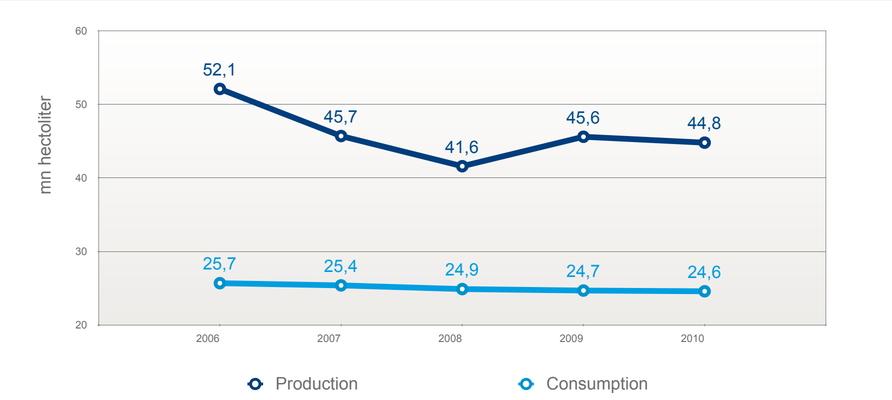
Thibaut de Monclin
Food & Beverage Specialist
M&A International Inc., France

Figure 6: France: average deal value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

Figure 7: France: wine production and consumption



Source: Copal Analysis, Capital IQ

Key characteristics

The economic recession, increased wine production and flat sales resulted in slower M&A activity in France. The French wine industry continues to suffer from oversupply (Figure 7), putting downward pressure on average deal value.

In general, French consumers are drinking less and trading up. In 2010, sales of expensive wines increased compared with 2009, to the detriment of cheaper labels.

Total sales by value declined 1% in 2010, mainly due to lower on-trade wine sales as a weak French economy discouraged discretionary spending, particularly the amount of wine that is consumed on-trade in cafés, bars and restaurants.

➜ Moët Hennessy (LVMH) sold Champagne Montaudon in December 2010 after having acquired it only two years earlier.

➜ Large French wine producers such as Groupe Castel and Domaines Bonfils have sought to capitalize on the overall decline in valuations to further expand their product portfolios. Between 2007 and 2010, Groupe Castel acquired four wine producers and a wine distributor, Friedrich S.A.S., specializing in alternative packaging formats (bag-in-box). Domaines Bonfils also concluded four M&A deals over the same period. Diversified product portfolios and alternative packaging have substantially contributed to Groupe Castel's success in the French wine market.

On the other hand, French-based global alcoholic beverage company Pernod-Ricard has shifted its focus towards developing premium wine brands and has been divesting non-core assets including brandy, port and cognac brands in Spain and France. The company also divested its wine operations in New Zealand.

We see significant room for consolidation in the French wine industry as the top 10 wine producers in France accounted for only 16% of the wine volume in 2010. In the near term, Euromonitor expects average wine prices in France to decline by at least 10% from their current €9.7/liter due to tougher competition and an increasing mix shift towards off-trade sales. We believe that lower profitability will encourage M&A as producers attempt to achieve economies of scale. In addition, given continued strong international demand for French wines, we expect overseas wine importers and producers to target mid-market-to-premium French brands and vineyards in the near future.

Spain: M&A to be driven by economies of scale and diversification

M&A deal volume in Spain accounted for 26% of all M&A deals in Europe and 28% of total deal value between 2007 and 2010. Deal volume in 2008 fell to 11 deals from 20 in 2007, although valuations remained high as shown by the increase in average deal value in 2008 (Figure 8).

Deal volume increased from 11 deals in 2008 to 16 in 2009 largely as a result of attractive valuations.

➡ The largest transaction in Spain between 2007 and 2010 was J. García Carrión's $117mn acquisition of Grupo de Bodegas Vinartis in 2008 from Rabobank. The deal enabled J. García Carrión, Spain's largest wine producer in sales volume, to further increase its market share from 8.5% of sales by volume in 2007 to 11.5% in 2008.

Overall, the Spanish wine industry has developed in much the same way as its French counterpart.

Key characteristics

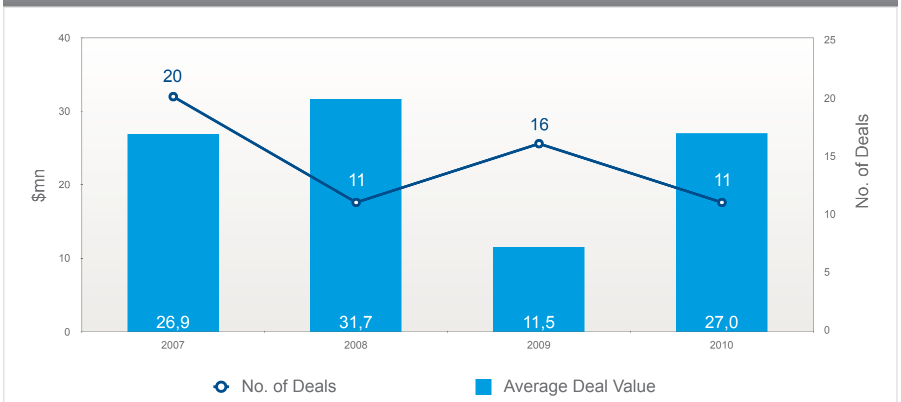
Wine consumption in Spain has fallen steadily (Figure 9). This decline accelerated as a result of the recession, with sales declining by 6% in 2008 and 5% in 2009. Such a negative trend was attributable to increased consumer price sensitivity as a result of the economic downturn.

Wine sales are also suffering in Spain from a change in drinking habits. Younger consumers increasingly prefer beer or spirits for standalone drinking.

In response to declining demand, Spanish producers are focusing on exports (Figure 10). For example, in 2007 and 2008 increased wine exports more than offset the decline in domestic sales.

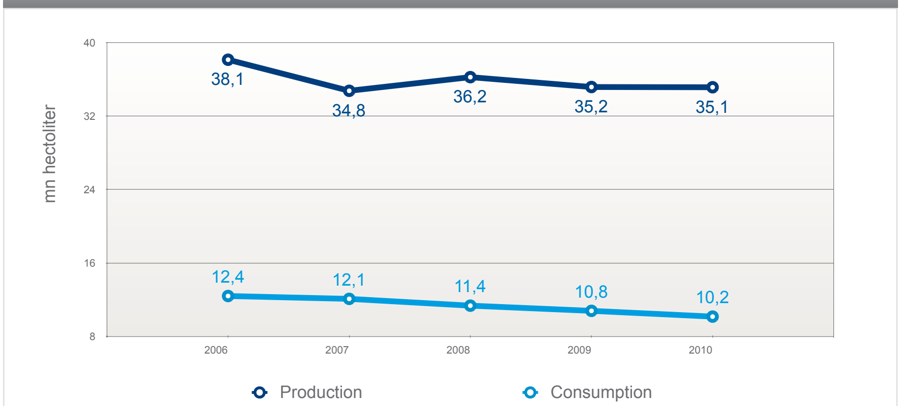
➡ An increasing focus on exports prompted J. García Carrión to acquire Grupo de Bodegas Vinartis in 2008. At the time, Bodegas Vinartis was Spain's fourth largest wine producer, with products distributed throughout Spain and internationally.

Figure 8: Spain: average deal value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

Figure 9: Spain: wine production and consumption



Source: OIV, Euromonitor

While Spanish per capita wine consumption is declining, demand for higher quality and locally produced wines is increasing, especially for still red wine.

➜ Moët Hennessy bolstered its presence in the super-premium wine category with its $39mn acquisition of Bodega Numanthia Termes, which produces high-end wines such as Termanthia, Numanthia and Termes.

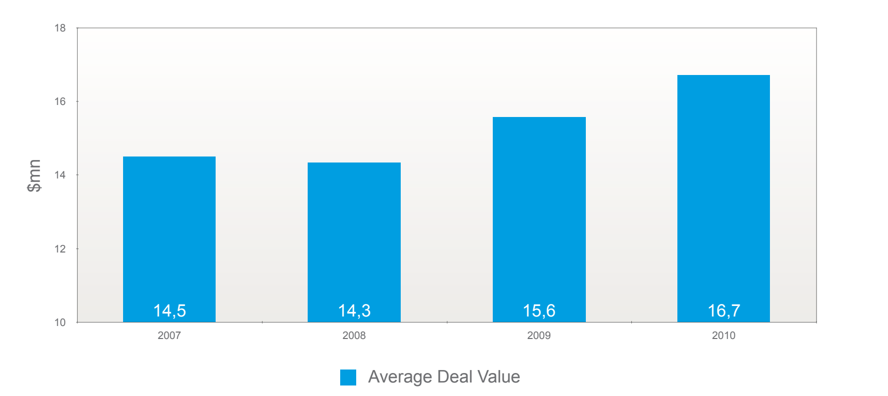
Stable market shares

“Despite the decline in sales, large wine producers have retained their respective market shares, even reporting a slight increase in some cases, mainly due to their higher penetration with leading grocery retailers and extensive range of wines. This, together with the increasing significance of exports for the Spanish wine industry, leads us to expect increased local M&A activity, predominantly driven by scale and diversification.”

José María Romances
Food & Beverage Specialist
M&A International Inc., Spain

The Spanish wine industry remains highly fragmented, with the 10 largest wine producers accounting for just 28.3% of market share by volume in 2010.

Figure 10: Spain: quantity of wine exported



Source: Euromonitor

Italy: intense competition is likely to lead to consolidation

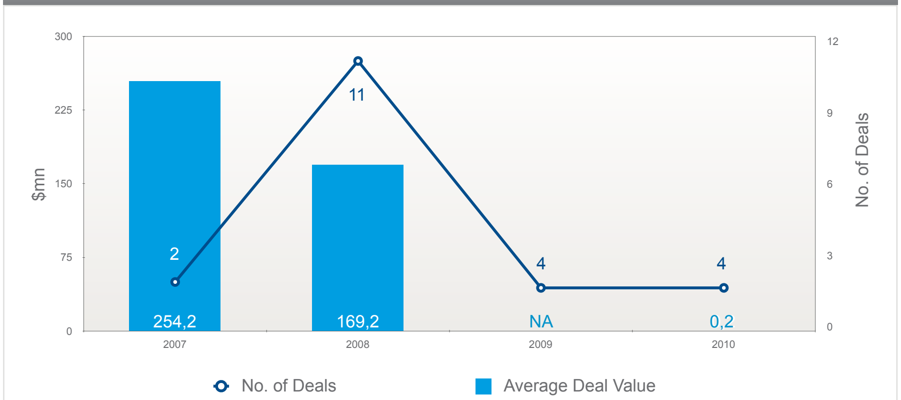
Despite being one of the world’s largest wine producers and the third largest wine consumer behind France and the US, M&A deal activity in Italy was significantly lower than in France and Spain during 2007–2010. M&A deal volume in Italy accounted for 9% of all M&A deals in Europe and 18% of total deal value between 2007 and 2010. Deal volume was highest in 2008 due to a sharp correction in valuations (Figure 11).

➜ The largest deal between 2007 and 2010 was Private Equity Partners’ $254mn acquisition of F. Giordano in 2007, which was the eighth largest wine producer in Italy at the time. Further, total deal value in 2008 was high due to the $142mn acquisition of Fontanafredda, an Italian wine producer which distributes and retails its products through wine shops and partners in Italy and internationally, by Fondazione Monte dei Paschi di Siena, a diversified support services firm.

Key characteristics

Like France and Spain, Italy’s wine industry is oversupplied. This has been further exacerbated by the recent economic crisis which caused consumers to reduce wine consumption (Figure 12).

Figure 11: Italy: total deal value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

Additionally, Italy is experiencing a change in drinking behavior, with young people increasingly regarding wine as an aperitif rather than a drink to be consumed during meals.

➡ The Italian wine sector is very fragmented, with the 10 largest companies accounting for only 17% of volume sales in 2010. The leading wine producer in both 2009 and 2010 was CAVIRO (Cooperative Agricole Viti-Frutticoltori Italiani Riuniti Organizzati scarl), and the second largest Cantine Riunite & CIV, established following the acquisition of Cantine Cooperative Riunite by C.I.V. (Consorzio Interprovinciale Vini) in 2008.

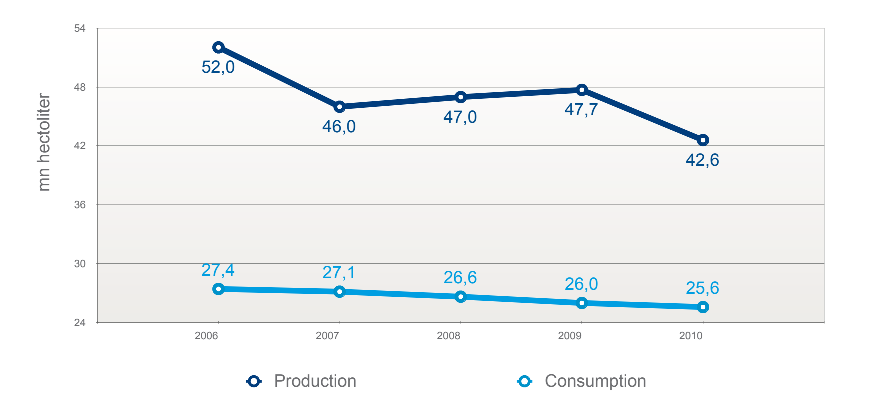
Further consolidation occurred in 2010 as Gruppo Italiano Vini Scarl, a subsidiary of C.I.V., acquired Cavicchioli U. & Figli and Carpene' Malvolti Spumanti, both in 2010. In addition, Gruppo Italiano Vini Scarl acquired the Italian wine brands of Brown-Forman Corporation, a company based in Louisville, Kentucky.

Joining forces

"I expect a reduction in fragmentation in the industry, with different producers combining to form larger groups to achieve economies of scale and better compete with imported wines."

Enrico Arietti
Food & Beverage Specialist
M&A International Inc., Italy

Figure 12: Italy: wine production and consumption



Source: OIV, Euromonitor

Italian consumers' demonstrated preference for domestic wines has limited cross-border M&A activity.

➡ However, one notable deal was Gruppo Campari's $8mn acquisition of Argentina-based Sociedad Anónima de Bebidas Internacionales.

Italian consumers typically tend to prefer to buy less expensive wines. As a result, Italian wine producers typically have lower profit margins and tend to avoid or minimize marketing expenditure.

Not surprisingly, New World wines have increased their market share in Italy. However, Italian wine producers are finally taking steps to strengthen their marketing activities in order to compete more effectively with the new entrants.

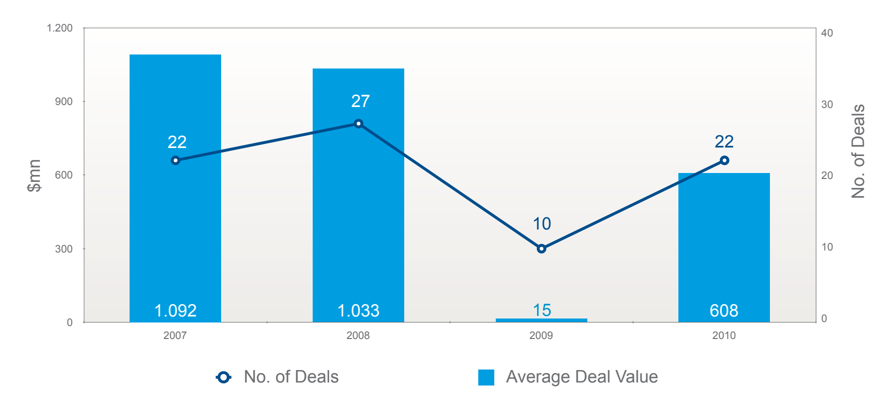
Americas: strong demand in the US offsetting oversupply in Argentina and Chile

In the Americas, the principal wine producers are the US (8% of 2010 expected production), Argentina (6%) and Chile (4%), according to the OIV. Total wine sales in the US increased steadily in both value and volume terms from 2002 to 2008. Even during the recession, wine volume sales in the US continued to grow. On the other hand, sales volume in Argentina has fallen though sales value has increased due to high inflation. Wine sales (in both value and volume terms) declined in Chile in 2008 and 2009 as a result of the economic recession.

Regional M&A activity has remained stable except during 2009 as a result of the credit crunch (Figure 13). In 2010, deal values and volumes recovered in tandem with the economy.

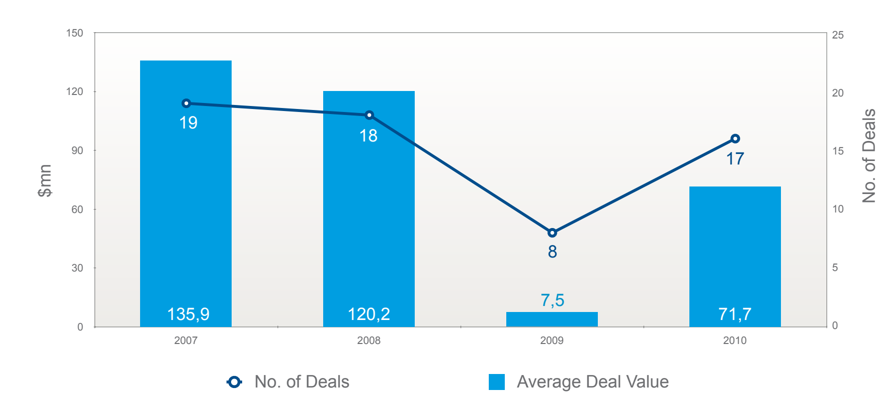
➜ Average deal value was highest in 2007 (Figure 14) due to the $877mn acquisition of Beam Wine Estates by Constellation Brands from Fortune Brands. The acquisition was consistent with Constellation's new wine strategy, which focuses on growing its position in the US premium wine business.

Figure 13: Americas: total deal value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

Figure 14: US: average deal value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

US: a bright spot in the Americas

The US accounted for 76% of all M&A deals in the Americas and 86% of total deal value between 2007 and 2010.

Average deal value reached a trough in 2009. Despite a recent recovery, valuations remain low compared with their 2007 levels. We believe that this makes the environment attractive for acquisitions.

Prior to the recession, wine sales were growing strongly across all channels and price points. The wine industry was expected to see continued growth due to strong wine consumption growth among young consumers. While many of these new drinkers entered the market at lower price points, large wine companies believed that they would eventually move up market as they became more interested in wine. As a result, a number of companies acquired premium wine producers in 2007 and 2008.

➜ E&J Gallo, the world's second largest wine producer (the largest in the US, with a 21% share of total volume sales) acquired premium wine producer William Hill Napa, Inc. in 2007. Diageo Chateau & Estate Wines Company also acquired a premium wine producer Rosenblum Cellars, Inc. in 2008 for $105mn. Private equity firms took notice too, with GI Partners acquiring Duckhorn Wine Company, a super-premium wine producer, in 2007.

In contrast, major wine producers have been divesting their value brands. Since its acquisition of Beam Wine Estates in 2007, Constellation Brands has continued to sell its lower-end brands. In 2008, it sold its popular Almaden and Inglenook economy wine brands and Paul Masson Winery to The Wine Group for $134mn. As a result, The Wine Group became the second largest wine producer in the US. Constellation also recently sold 80% of its operations in Australia, the UK and South Africa to Australia's CHAMP Private Equity fund for $230mn, enabling it to focus on its most profitable brands and strengthen its balance sheet.

Key characteristics

The recession hit the industry hard as consumers switched to non-premium products, reversing the previously steady growth in sales value, which in fact fell by almost 4% in 2009. Value sales declined by almost 2% in 2010.

At the same time, volume sales rose 1% in 2009 and 2010 as people traded down for less expensive brands rather than cutting back on their consumption of wine. Sales of wines priced at or above $25 were especially hard hit given total value and volume declines.

Wine sales in on-trade establishments were adversely affected between 2008 and 2010, reversing six years of volume growth of between CAGR 4–6%.

Early signs indicate a volume-based recovery for the premium wine segment in 2010 although it may prove temporary, with premium wines currently offered at a potentially unsustainable discount.

It remains to be seen whether producers can successfully persuade consumers to abandon discounted wines for wines selling at higher price points.

Unlike most other wine-producing regions, the US market is very consolidated, with the 10 largest producers currently accounting for 72% of total volume sales. Therefore, the scope for large deals seems to be limited. However, there are many smaller vineyards in the US which do not benefit from the same economies of scale and distribution networks as those of large producers. So, we expect higher deal volumes albeit with a smaller average value as many minor players either conclude deals with each other or with larger companies over the near-to-medium term.

Argentina: slump in domestic sales offset by international demand

Argentina accounted for 9% of all M&A deals in the Americas and 12% of total deal value between 2007 and 2010.

➡ The largest deal was BI Argentina's acquisition of a 50% stake in Penaflor, the country's largest wine producer with a 21% share of total volume sales in 2010, for $300mn. Another significant transaction was Finca Flichman's purchase of Pernod-Ricard's winery in Perdriel (Lujan de Cuyo).

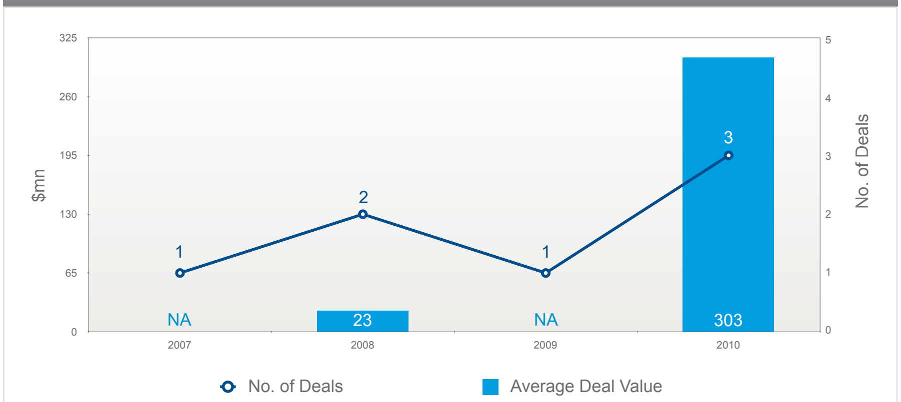
Despite being one of the world's largest wine producers, M&A activity in Argentina has been surprisingly limited, with only seven deals closed during the period (Figure 15).

Key characteristics

Wine consumption has declined steadily for many years (Figure 16) due to the increasing substitution of beer for wine. Beer is regarded as more fashionable and preferred by consumers aged between 18 and 25.

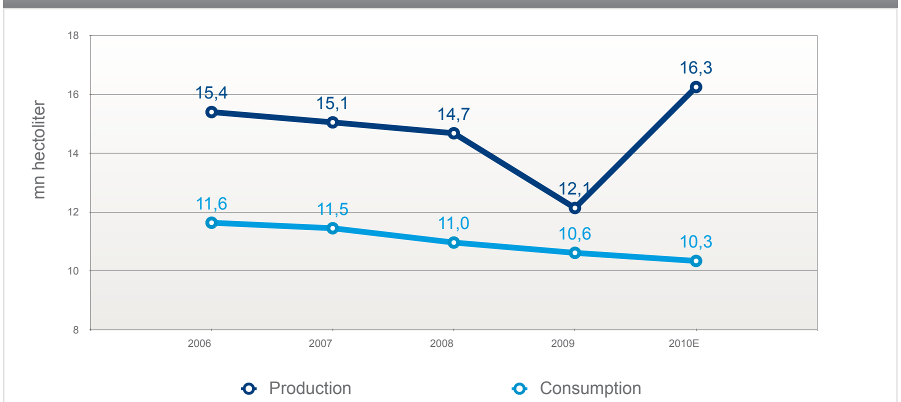
Although Argentina was largely unscathed by the recession, the country is currently suffering from high inflation, reducing disposable income and, in turn, wine sales.

Figure 15: Argentina: total deal value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

Figure 16: Argentina: wine production and consumption



Source: OIV, Euromonitor

Inflation has also led to a higher number of consumers purchasing wine in lower price bands, with a stronger concentration of sales in the Argentinean Pesos 2.51–8.0 range for red, white and rosé wines.

Demand for Argentine wine remains strong internationally, particularly in Russia and the US. Wine exports have doubled since 2005, more than offsetting the decline in domestic sales.

In contrast, wine imports remain negligible as Argentine consumers tend to prefer domestic wine.

➡ In order to gain entry into the market, Italy-based Gruppo Campari acquired Sabia (Sociedad Anónima de Bebidas Internacionales y Argentinas) in 2008. Previously, the company was represented by Cepas Argentinas S.A., a competitor of Campari and therefore disinclined to develop Campari's brands to the best of its ability.

Chile: quality wines attracting international buyers

Chile accounted for 9% of all M&A deals in the Americas and 2% of total deal value between 2007 and 2010. In this period, there were only seven deals in Chile with a total deal value of just $63mn (Figure 17).

➡ The largest deal was Vina San Pedro's 2008 acquisition of Vina Tarapaca, a producer and distributor of wine for $33mn.

Key characteristics

Chile is the world's seventh largest wine producer and is expected to account for approximately 4% of global wine production in 2010 (OIV). However, the country's own wine consumption is relatively low (Figure 18).

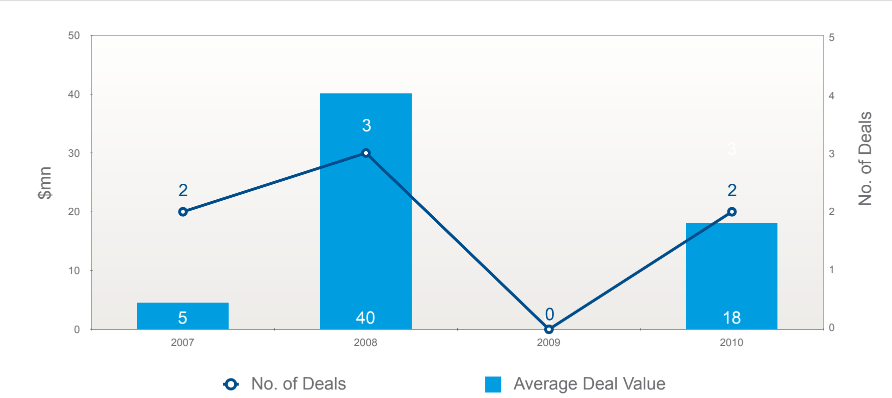
Most Chilean wine producers concentrate on exports. The country was ranked fifth in terms of wine exports, with 8% of global shipments (6mn hectoliters) in 2009.

Globally, Chile is regarded as offering good-quality wines in the economy and mid-priced segments. However, more recently winemakers have sought to raise the profile of Chilean wines by concentrating on developing premium and super-premium wines.

Most M&A activity has involved acquisitions of well established wine producers exporting wine to various international markets.

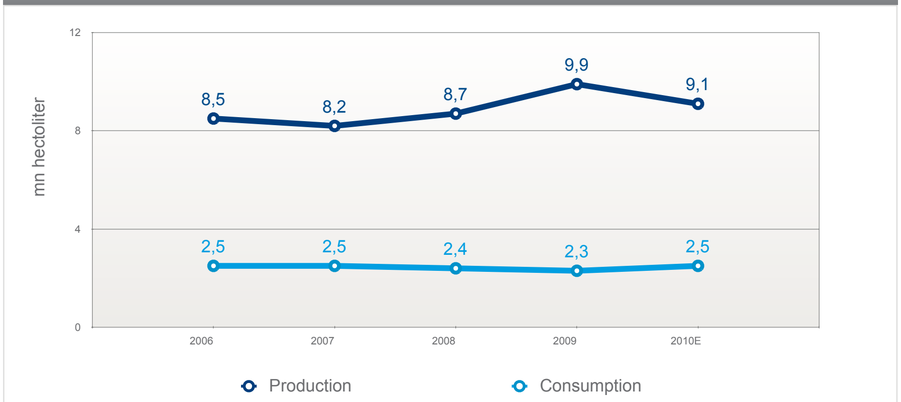
➡ The Chilean market leader in both domestic sales and exports is Viña Concha y Toro SA, which accounted for 30% of volume sales in Chile in 2010. To further solidify its position in the super-premium export market, the company's subsidiary, Vina Cono Sur, acquired Vina Los Robles in 2008 for $7mn. Vina Los Robles produces premium and super-premium wines for Chile and international markets including France, Spain, Italy and the US. Other wine producers have also targeted a larger share of the premium export market, which resulted in the acquisition of premium wine makers and exporters Chateau Los Boldos Ltda. in 2008 and Viña Leyda in 2007 by Sogrape Vinhos and Viña Tabalí respectively.

Figure 17: Chile: total deal value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

Figure 18: Chile: wine production and consumption



Source: OIV, Euromonitor

Chilean wines gain popularity

"Due to the increasing importance of exports and strong demand for Chilean wines worldwide, M&A activity is expected to be driven by the acquisition of various Chilean wine producers by international producers and distributors."

Pablo Larrain
Food & Beverage Specialist
M&A International Inc., Chile

➡ Recent examples include the $18mn acquisition of Bisquertt Vineyard's four fields and wineries by China-based COFCO Xinjiang Tunhe Co. Ltd., a food processing company.

Asia Pacific: the Chinese and Australian wine industries are likely to be M&A targets

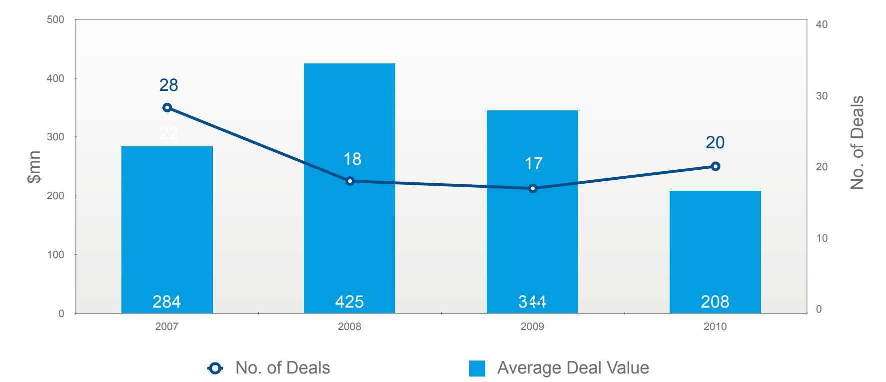
In Asia Pacific, Australia and China are both the largest producers and consumers of wine. For the last few years, the Australian wine industry has suffered from an oversupply of cheap wine. Despite a slight increase in exports and volume sales in 2009 and 2010, the industry continues to struggle from a glut of cheap wine putting downward pressure on prices.

In contrast, the Chinese industry has been a global focal point. Light grape wine volume sales grew by 23% in 2008 and 17% in 2009 as a result of greater consumer sophistication and awareness, and improved shelf visibility and higher investment.

➡ Regional M&A activity fell significantly in 2008 and 2009 but is showing signs of recovery (Figure 19). Total deal value increased in 2008 due to South Korean-based Lotte Chilsung Beverage Co.'s $383mn acquisition of Doosan Liquor in 2008. This was the largest deal in the Asia Pacific region between 2007 and 2010.

In 2009, CITIC Guoan Group Corp. purchased a 21.69% stake in Suntime International Vine Co. Ltd. for $137mn. Excluding these two transactions, total and average deal values have declined significantly from their 2007 highs.

Figure 19: Asia Pacific: total deal value and volume of M&A transactions

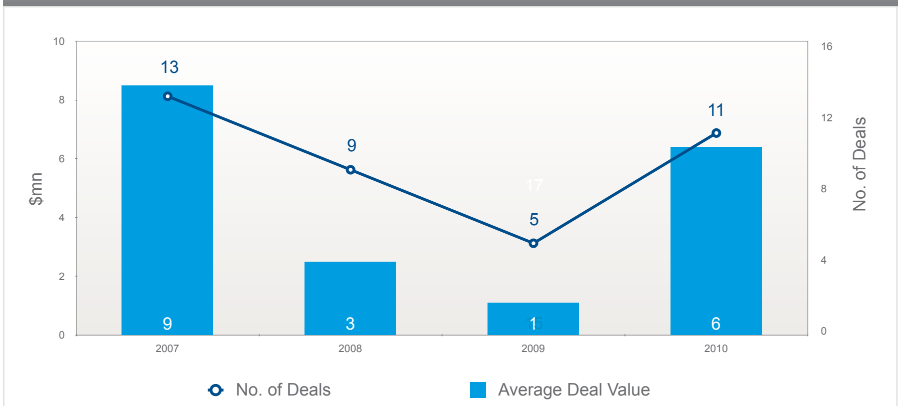


Source: Copal Analysis, Capital IQ

Australia: oversupply decreases; divestments exceed investments

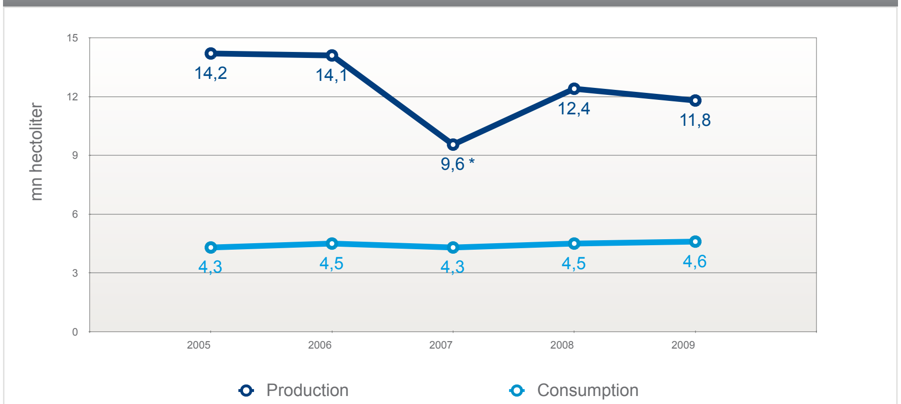
Australia accounted for 46% of all M&A deals in Asia Pacific and 10% of total deal value between 2007 and 2010. Average deal value was the highest in 2007 but declined sharply in 2008 and 2009, mainly due to oversupply issues plaguing the domestic wine industry. M&A activity rebounded sharply in 2010 on strong deal volumes and value (Figure 20), indicating early signs of recovery in the industry. Valuations remain low compared with their highs in 2007, which should further encourage M&A activity.

Figure 20: Australia: average deal value and volume of M&A transactions



Source: Australian Wine and Brandy Corporation

Figure 21: Australia: wine production and consumption



Source: Australian Wine and Brandy Corporation

*There was a huge dip in wine production in 2007 due to one of the worst bush fires in Australian history that destroyed more than one million hectares over a period of 69 days.

Key characteristics

The Australian wine industry is characterized by a very large number of vineyards and wineries. Many smaller Australian wineries are having trouble competing in an increasingly competitive export market. As a result, the majority of M&A activity in Australia has targeted smaller standalone wineries and wine estates.

Historically, Australia has suffered from an oversupply of cheap wine due to overproduction by the country's wine industry (Figure 21).

While cheap wine is readily available, the consensus within the industry is that the most promising area for wine consumption growth is in the A$10–20/liter price point.

Due to its status as a major commodity producer, the impact of the financial crisis has been relatively limited in Australia. This has kept consumers from trading down for cheaper brands of wine or cutting back on wine consumption. As a result, wine sales have continued to increase throughout the financial crisis. Nevertheless, production has still outstripped growth in consumption. Overproduction has put pressure on already low margins, especially in the case of larger wine producers who maintain a diversified product portfolio and are represented across the value chain.

However, Australia's oversupply of wine is slowly being resolved as production has moved closer to actual consumption, a development mainly driven by increased exports and decreased production. Production is expected to decline by a further 8% in 2010 (OIV).

➔ Constellation Wines Australia, which holds a 23% market share by volume sales in Australia, has already offered several hundred hectares of vineyards and agricultural land for sale. The company has also announced its intention to reduce SKUs and to focus on higher-quality wines.

Constellation sold Kamberra Wine Company in 2007 and Amberley Estate Pty Ltd. in 2010. Most recently, it sold 80% of its wine business in Australia to CHAMP Private Equity. The company retained several premium brands.

Foster's Group Ltd., Australia's second largest wine producer, announced a demerger of its wine and beer businesses in May 2010, receiving a $2.5bn offer from Cerberus Capital in September 2010. The offer was described by management as grossly inadequate and promptly rejected.

However, the company has stated that it is willing to consider higher offers. Foster's sold its Cumbandry Vineyard in 2009 and a vineyard in the New South Wales Riverina in 2010.

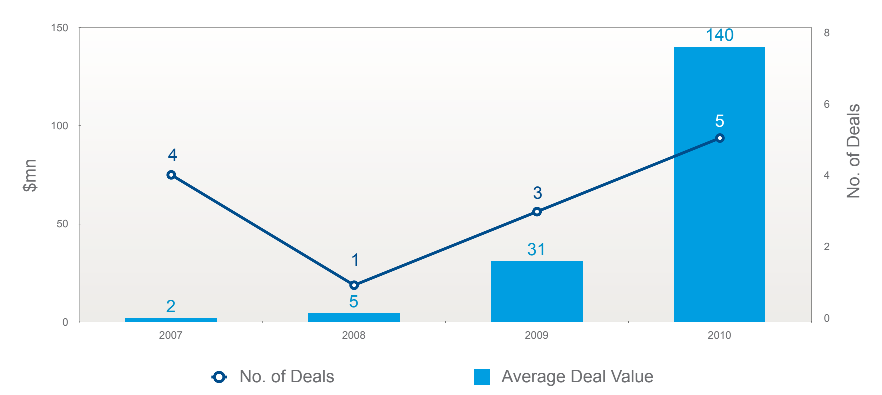
Critical examination

"Despite the expected decline in production, major wine producers are critically examining their wine-related assets, brand portfolios, involvement in packaging formats and price brackets."

Paul Young
M&A International Inc., Australia

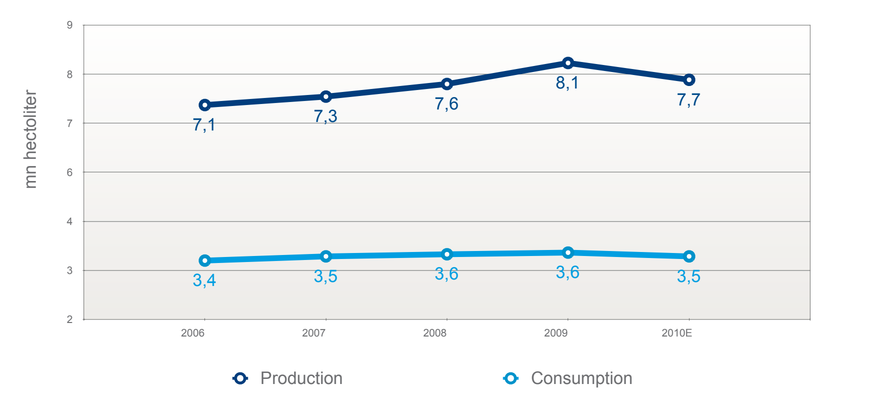
We expect Australian M&A activity to increase as major producers continue to divest assets. In addition, the country's smaller wineries also face an uncertain financial future which is likely to result in an increasing number of "marriages of convenience."

Figure 22: South Africa: total deal value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

Figure 23: South Africa: wine production and consumption



Source: SA Wine Industry Information & Systems, Euromonitor

Africa

Between 2007 and 2010, a total of 13 deals were done with a total deal value exceeding $175mn (Figure 22).

South Africa: limited M&A activity

The economic recession has had only a limited impact on wine consumption in South Africa (Figure 23). Exports in 2009 accounted for 49% of total production. Euromonitor expects that this will increase to 50% in 2010 due to a weaker South African Rand, continued strong brand positioning in the UK, Sweden and Canada, and the emergence of new buyers in developing markets (including Angola and Southeast Asia).

➡ Distell Group Ltd. is the South African market leader with a 32% share by volume sales. In 2009, the company acquired the remaining 50% stake in Lomond Wine Estates Limited for $1.3mn to further solidify its position in the South African wine market. Between 2007 and 2010, a total of six acquisitions occurred including Capevin Holdings Limited and Capevin Investments Limited as a result of their interest in Distell Group. The latest transaction in a series of bids to control Capevin Holdings Limited includes an $119mn offer by Pioneer Food Group Ltd. to acquire Capevin Holdings Ltd. from Zeder Investments Ltd., Remgro Ltd., Phetogo Investments Limited and VinPro Ltd.

As shown by the country's limited M&A activity, little consolidation has occurred in the South African wine industry, with the market remaining highly fragmented.

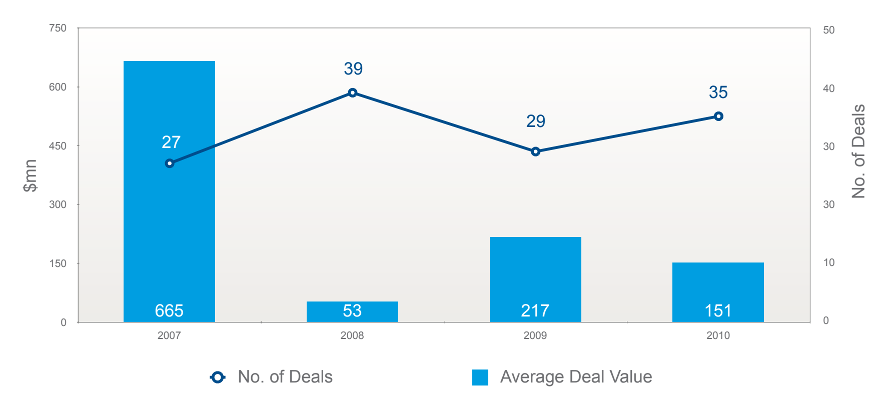
Diversify rather than consolidate

"In order to increase relative competitiveness, local wine producers have decided to diversify their portfolios rather than consolidate. We therefore do not expect a significant increase in regional M&A activity."

Yaron Zimbler
Food & Beverage Specialist
M&A International Inc.,
South Africa

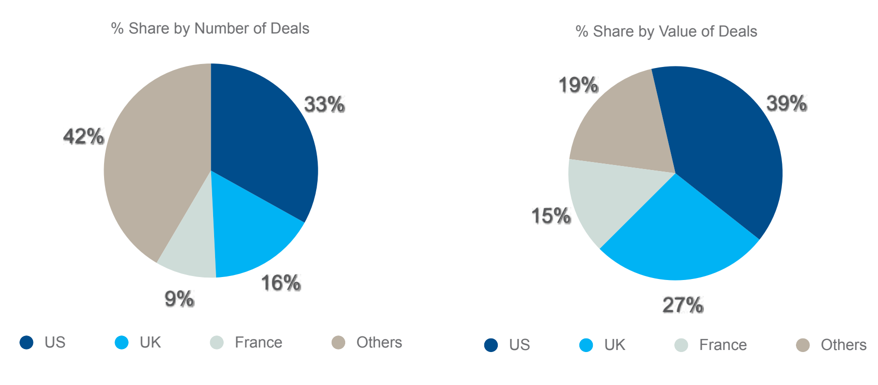
However, global wine producers may target inorganic expansion in South Africa as the increasingly affluent black middle-class market has not been adequately targeted by wine companies, leaving this significant growth market wide open.

Figure 24: Wine distribution: total value and volume of M&A transactions



Source: Copal Analysis, Capital IQ

Figure 25: M&A deal volume and value by country



Source: Copal Analysis, Capital IQ

M&A Overview & Analysis: Wine Distributors

M&A activity in the wine distribution industry has remained robust despite the recent economic recession. Between 2007 and 2010, a total of 130 deals were completed involving wine distributors (Figure 24). Over the same period, total deal value exceeded $1bn, reaching a record high in 2007 before correcting sharply in 2008 (total deal value was highest in 2007 due to Constellation Brands' $384mn acquisition of Spirits Marque One). At the same time, deal volume increased 44% in 2008 when compared with 2007. However, in 2009 the trend reversed with deal volume decreasing although deal value increased.

The industry is currently consolidating. Lower total deal value is a result of industry leaders consolidating their market position by picking up smaller players. Cash generative distributors are strategically acquiring smaller companies unable to manage slow growth, discounting and the economic recession. Industry M&A activity has been mainly focused on the US, the UK and France, which jointly account for 58% of deal volume and 81% of total value (Figure 25).

M&A Trends & Opportunities: Wine Distributors

We expect distributors to change how they operate as a result of increasing competition from direct sales by suppliers and wholesaler chains as companies such as Costco take steps to develop their own brands. We believe that companies within the industry will continue to consolidate and focus increasingly on core distributional activity (i.e. fleet management and storage facilities), and delegate functions including marketing and branding to the supplier and retailer. In addition, we believe that forward integration by distillers and vintners will drive future M&A activity.

Distributors consolidating to improve margins

Between 2007 and 2009, alcoholic beverage distributors acquired other distributors in a total of 51 deals. These deals were largely focused on the US (25) and the UK (11). In the US, the beer and wine distribution industry has so far benefited from state alcohol regulations which prohibit producers in most states from selling directly to consumers. These regulations were designed to prevent brand movement between distributors and ensure satisfactory distributor margins in any economic climate.

Over the past 10 years, wholesale consolidation has accelerated because wholesale margins have been squeezed by new overhead costs involving technology, retailer-required merchandising and advertising. As a result, large distribution companies have focused on expanding both their distribution network and the SKUs offered via acquisitions. Southern Wine & Spirits of Minnesota, one of the largest distributors in the US, and its subsidiaries alone were involved in a total of five transactions from 2007–2010. The most recent was its acquisition of World Class Wines, a Minnesota-based importer and distributor of wine. The Southern Wine & Spirits' distribution network currently covers the US, where it is the country's largest distributor.

Other major wholesaler transactions included the 2007 merger of Republic Beverage Company and National Distributing Company to form Republic National Distributing Company, LLC, making it the country's second largest distributor. US-based beverage distributor Glazer's is also targeting growth by aggressively acquiring wine distributors. A similar trend is occurring in the UK where a margin squeeze has been exacerbated by a recent increase in alcohol taxes, resulting in extensive consolidation. The largest transaction involved Dutch bottler and European wine distributor Baarsma Wine Group's $25mn acquisition of John Armit Wines, a UK-based wine merchant, a deal which M&A International Inc. members advised on.

While most US states now allow direct-to-consumer sales, restrictions on direct sales across states remain in place. The repeal of these regulations will further affect distributor margins, with most of the smaller wineries preferring to bypass distributors and sell directly to consumers. In addition, margin pressures are causing wholesalers and distributors to focus increasingly on transporting and delivering product and shifting the responsibility for marketing, selling and merchandising to producers. We therefore expect distributors to continue to consolidate to improve margins and gain control over distribution networks. We also expect distributors to target asset-rich companies, such as those comprising of delivery trucks, storage facilities, forklifts and IT systems.

Large wine producers acquiring distributors

Extensive consolidation within the distribution business has unsettled a number of large producers as larger distributors enjoy significant negotiating power over producers. Consolidation ensures that distributors are no longer exclusive to any one producer and may therefore not necessarily act in a producer's best interest. To offset this, some large producers have decided to establish strong distribution networks of their own, particularly in core markets. In addition, vertical integration of distribution systems by large wineries has also improved profitability. From 2007 to 2010, there were a total of 30 such deals, the largest being the $384mn acquisition of Spirits Marque One, an importer and seller of wine in the US, by Constellation Brands. Another major deal involved Davide Campari-Milano's $40mn acquisition of Daucourt Martin Imports, an importer and distributor of French spirits in the US. Recently, however, deal flow has fallen off as a number of wine producers have shifted their focus to restructuring their own businesses.

Private equity will target established companies

From 2007 to 2010, financial services companies (including private equity, asset management and investment holding firms) concluded 12 deals in the space. The most significant deal was the acquisition of Kahn Ventures Inc., parent company of Empire Distributors, by McLane Company, a subsidiary of Berkshire Hathaway. McLane has also signaled its intention to acquire "other similar high-quality wholesale distributors". We expect ongoing consolidation in the wine distribution industry to attract further interest from private equity companies, particularly targeting well established distributors which exert significant control over regional distribution networks.

Conclusions

With supply/demand dynamics expected to achieve equilibrium in the near term, we expect the wine industry to enjoy a very positive outlook over the next two years. During the past 3–5 years, value offerings from New World countries, strong demand from Asia Pacific, renewed interest in home consumption and increased online sales have fundamentally changed the way in which the industry operates. At the same time, producers and distributors remain adversely affected by slow growth in sales and consumption. Nevertheless, these factors together with an expected reduction in supply, projected economic recovery in developed countries and the industry's increasing penetration in emerging markets justify our optimistic assessment concerning the industry's long-term growth prospects.

In the near term, we expect the following developments:

Large producers will continue restructuring. While several large wine producers, including E&J Gallo, have benefited from maintaining a large, diversified portfolio of wines across the value chain, other large producers such as Constellation Brands and Foster's Group are being adversely affected by continued margin deterioration due to lower consumption and trading down. Consequently, we expect these firms to continue restructuring their respective wine businesses and selling non-core assets and economy brands while simultaneously acquiring premium brands. Such a development could offer attractive potential for small-to-medium sized producers seeking to expand operations.

Cross-border M&A activity to increase. Despite strong international trade in wine with many producers exporting products to a wide range of countries, cross-border M&A activity has been surprisingly limited. However, we expect this to change as wine producers seek to increase exports to existing markets and also target new regional opportunities, possibly also making selective acquisitions in such markets. With valuations recovering but still well below historical highs, we see many attractive opportunities at present to buy key assets.

Distributors to focus on core operations. The current margin squeeze is forcing distributors to focus increasingly on doing what they do best — transporting and delivering products. We therefore expect them to continue to consolidate, with a focus on increasing assets such as warehouses, delivery trucks and IT systems.

About M&A International Inc.

M&A International Inc.

"M&A International Inc.'s members actively represent buyers and sellers in the Food & Beverage M&A market as well as those seeking to raise private equity and debt capital. We possess significant Food & Beverage sector expertise, industry relationships and experience in successfully executing complex transactions on behalf of our clients."

Ruud van Hoek
Head of M&A International Inc.'s Food & Beverage Group
rvanhoek@hcfinance.nl

Case Studies of Transactions Closed by Members of M&A International Inc.

Role of M&A International:	Advisor to APEX
Sector	Foods and Beverages
Target	Shares in Apex Cellars
Our role	Advisor to Seller
Seller/Location	Private shareholders of Apex Cellars, United States
Activity	Winery
Acquiror/Investors/Location	Precept Wine Brands, United States
Activity	Produces, markets and sells wine
Description of Transaction	Advised award winning Apex Cellars on its sale to Precept Wine Brands for an undisclosed sum. Precept has an extensive distribution network throughout the US, Asia, Europe, New Zealand and Australia.

Role of M&A International:	Advisor to baarsma wine group
Sector	Foods and Beverages
Target	Armit
Our role	Advisor to buyer
Seller/Location	Private shareholders of Armit, United Kingdom
Activity	Fine wine merchant
Acquiror/Investors/Location	Baarsma Wine Group, Netherlands
Activity	Wine distributor
Description of Transaction	Advised Baarsma Wine Group on its $25 million acquisition of Armit. Armit is a leading fine wine merchant in London, with a customer portfolio of several famous clients including the Dorchester restaurant, Gordon Ramsay's Claridge's and the Savoy Grill. Baarsma Wine Group Holding is a European wine distribution company and market leader in the Benelux countries.

Role of M&A International:	Advisor to CELLAR FORCE
Sector	Multi-line Retail
Target	51% stake in Cellarforce Pty Limited
Our role	Advisor to seller
Seller/Location	Private shareholders of Cellarforce Pty Ltd and Wine IQ Pty Ltd, Australia
Activity	Outsourced wine sales
Acquiror/Investors/Location	Cellarmasters Pty Limited, Australia
Activity	Direct wine sales
Description of Transaction	Advised the shareholders of Cellarforce on the sale of a 51% stake to Cellarmasters for an undisclosed sum.

Role of M&A International:	Advisor to CHEVIOT BRIDGE®
Sector	Foods and Beverages
Target	Winepros Limited
Our role	Advisor to buyer
Seller/Location	Shareholders of Winepros Limited, Australia
Activity	Online wine business
Acquiror/Investors/Location	Cheviot Bridge Limited, Australia
Activity	Wine company that markets and distributes a select range of owned brands
Description of Transaction	Introduced a listed cash shell, Winepros, to Cheviot Bridge thereby completing a A$16 million capital raising which has resulted in the establishment of a well capitalized, modern, dynamic wine group. With its new and existing stakeholders, Cheviot Bridge could explore opportunities including growth in brand management and distribution, organically and by acquisition, asset management opportunities, and the provision of wine industry services.

Role of M&A International:	Advisor to EXWORKS AS
Sector	Foods and Beverages
Target	Excellars AS
Our role	Advisor to buyer
Seller/Location	Kiwiik Holding AS, Norway
Activity	Private holding company
Acquiror/Investors/Location	Exworks AS, Norway
Activity	Private holding company
Description of Transaction	Advised Exworks AS on its acquisition of 30% of Excellars AS, a Norwegian wine wholesaler, from Kiwiik Holding AS for US$4 million. Exworks AS and Kiwiik Holing are private holding companies.

Role of M&A International:	Advisor to HESS GROUP
Sector	Foods and Beverages
Target	Münsterkellerei AG
Our role	Advisor to seller
Seller/Location	Hess Group AG, Switzerland
Activity	Produces and distributes wine
Acquiror/Investors/Location	Eichhof Getränke AG, Switzerland
Activity	Brews beer and distributes beverages. The company is active in the wine trade through Kellerei St. Georg.
Description of Transaction	Advised Hess Group on the disposal of the prestigious Münsterkellerei AG in Liebefeld-Bern to Eichhof Getränke AG, which is active in the wine trade through Kellerei St. Georg. This transaction allows Hess Group to focus on its core business of wine production in the New World and on the wholesale wine trade.

Role of M&A International:	Advisor to HESS GROUP
Sector	Foods and Beverages
Target	Peter Lehmann Wines Limited
Our role	Advisor to buyer
Seller/Location	Shareholders of Peter Lehmann Wines Limited, Australia
Activity	Produces and distributes wine
Acquiror/Investors/Location	Hess Group AG, Switzerland
Activity	Produces and distributes wine
Description of Transaction	Advised Hess Group AG on the strategic acquisition of 85% of Peter Lehmann Wines Limited for US$120 million via a public company takeover.

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