BRIGHT STARS

INTERVIEW WITH RICHARD SANDS

Constellation Brands has evolved from an almost imperceptible twinkle above upper New York state to a global star that now sells more wine than any other company on the planet. In 1991, annual corporate revenue was, in today's terms, a paltry $176 million, based almost entirely on sales in the States. By 1998 the company had morphed into a corporate giant that moved well over a $1.2 billion worth of goods per year, mostly wine. With its acquisition of Vincor International in 2006, the group now does over $5.2 billion in turnover with 200 brands in 150 countries. Joel B. Payne spoke with Richard Sands about where Constellation Brands would like to be on tomorrow's horizon.

------*Wine Business:* While Paul Walsh of Diageo has conspicuously declined to add significantly to his wine portfolio in recent years, Constellation has been on a spree. Is Walsh wrong to focus on a small range of wines and a growing set of spirits?

------***Richard Sands:*** Our companies are different. Diageo is primarily a spirits company; Constellation Brands is primarily a wine company. Although we are the largest wine-producer in the world, we do have a significant beer, wine and spirits cross-category presence, especially on our domestic market.

------*Wine Business:* Yes, but...

------***Richard Sands:*** Diageo is centralized, which seems to work for them. Wine is a different business to spirits or beer because consumers have so many wine choices. Our wine business is comprised of wines from many geographic origins, which requires a decentralized structure in order to remain close to production – and close to our customers in the core markets. Further, wine requires more capital and a longer lead time before there are returns, so wine is truly a long-term business.

------*Wine Business:* The US looks like a magic wine market at the moment, with growing value and volume. But are the retail value statistics really credible when retailers like Trader Joe's and Aldi aren't scanned? And is the growth sustainable?

------***Richard Sands:*** While scan data only captures about 20% of total wine sales in the US, when we look at all the available data we see trading up in all channels. Wine is aspirational. People want to feel better about themselves and want to drink higher quality wines to reflect their success. If you look at what wine retailers are stocking, they are generally moving up the price and quality scale – and their consumers are moving up. We see this in all channels throughout the country.

------*Wine Business:* Vincor was an expensive purchase. Will Kumala justify its cost? The recent slide in sales in the UK – its traditional market – is not encouraging.

------***Richard Sands:*** What people don't understand about the Vincor acquisition is that the real jewel is Canada, where there is 6% wine sales growth and fantastic trading-up activity. The acquisition gave Constellation Brands its fifth core market, Canada. Further, Vincor Canada has fantastic brands – including Jackson-Triggs, which is Canada's favorite wine – not to mention terroir! Wines are being produced in British Columbia's Okanagan Valley that rival the best appellations in France, Australia and Italy. This is a hidden secret. On the Niagara Peninsula, Le Clos Jordanne is producing Pinot Noir that is as great as any in the world. Canada is known for icewines, and Inniskillin is the icewine of the world. Although this acquisition was principally about Canada, there were other jewels, including Kim Crawford from New Zealand, Hogue in the US and Kumala from South Africa.

------*Wine Business:* You are proud of Mondavi being the American name for super-premium and icon wines, but your focus now appears to be at the entry-level price point. Why?

------***Richard Sands:*** Actually, there are no entry-level Robert Mondavi wines. Woodbridge is a premium wine in the US, and our emphasis on Robert Mondavi there has been on both Woodbridge and the super premium Private Selection. Additionally, we are building our wine stocks of ultra premium wines produced at the winery in Napa to build upon this iconic portfolio, which is based upon grapes from some of the best vineyards in the world, including the To Kalon vineyard.

------*Wine Business:* Restrictive European wine laws are easing, with Spain, Portugal and France all introducing the possibility of making and selling big, New World-style brands in the Old World. Gallo is already very busy in France and Italy. How tempted are you to get into production there?

------***Richard Sands:*** We have existing relationships with Ruffino in Italy and Baron Philippe de Rothschild in France. There may be future opportunities in countries such as Spain and Portugal, and we will look at those as we expand our presence in Europe. Additionally, we import the Red Guitar wine brand to the US from Spain.

“Wine requires more capital and a longer lead time before there are returns, so wine is truely a long-term business.”

CONSTELLATION BRANDS

Turnover 2007: $5,216 million

Turnover 2006: $4,600 million

Turnover 2001: $2.226 million

Turnover 1998: $1,200 million

Turnover 1991: $ 176 million

------***Wine Business:*** After your experience with Ruffino, could you imagine investing in brands that were built on European appellations rather than varietals?

------***Richard Sands:*** Yes. Ruffino has been a terrific relationship. Tuscany is truly a great combination of Old World wine traditions based on appellations – Ducale Oro Chianti exemplifies this – and New World wine styles – mostly IGTs, such as Modus and Romitorio.

------***Wine Business:*** How do you feel about the potential for growth in the BRIC markets (Brazil, Russia, India, China)?

------***Richard Sands:*** Eastern Europe is interesting. We’ve identified 14 European countries that represent long-term expansion opportunities for us in the region, with Russia, Poland and the Czech Republic all on the list. Although China and India are not well-developed wine markets, they are tempting because of the large potential consumer base. Eventually we may take a closer look, but not in the immediate future.

------***Wine Business:*** Diageo was mentioned in rumours about a wine investment in India. Does the idea appeal to you?

------***Richard Sands:*** We will always look at opportunities. Currently, our focus is on expansion in Europe, increased development for our premium spirits portfolio domestically and export among our other core markets.

------***Wine Business:*** Matthew Clark gave you great distribution into the British on-trade. Is this repeatable elsewhere?

------***Richard Sands:*** Yes, very much so. Matthew Clark was, and is, very strategic. In fact, the access to the on-trade channel that Matthew Clark gives us helps build on-premise brands such as Stowells. After buying Hardys, we used Matthew Clark to further develop those brands and make them even more important in the UK. Since out joint venture with Punch Taverns, Matthew Clark is even more strategic. We believe that this could be a good model for other parts of the world.

------***Wine Business:*** Do you believe the three-tier system in the US can survive?

------***Richard Sands:*** Yes. We believe that the three-tier system in the US is the reason that America is one of the greatest wine markets of the world, offering the consumer unprecedented selection across categories, varieties and appellations at the most reasonable prices in the world. The three-tier system will certainly evolve and change, but because it serves the consumer, it will continue to prosper.

------***Wine Business:*** What effect will the breakdown of restrictions on inter-state shipping have on your business?

------***Richard Sands:*** As it is quite an expensive way to get wine to the consumer, direct shipping has very little impact on our overall business. It does allow the consumer to access small, boutique wineries, which is good. This increases consumer interest in exploring wines. We take advantage of this through the many boutique offerings at our various hospitality centers.

------***Wine Business:*** The Australian wine industry is less attractive than a few years ago. Do you see it bouncing back?

------***Richard Sands:*** The Australian wine industry remains very attractive. We are in the midst of an interesting grape cycle, one of the most severe swings from shortage to surplus – and I believe eventually back to shortage – that I have seen in my 28 years of being in the wine business. But I believe Australia produces some of the highest quality premium wines at some of the most reasonable prices of any country in the world.

------***Wine Business:*** How does Constellation see its future in South America? What is of interest beyond Chile and Argentina?

------***Richard Sands:*** There are some excellent wines being produced in South America. We have both Chilean and Argentinian wines and are watching the rest with interest.

------***Wine Business:*** The wine brands you have in Australia appear to be a dysfunctional family: brands created and moulded by their previous owners to compete with – and cannibalise – each other. It’s a long way from the Procter & Gamble model.

------***Richard Sands:*** We see the wine business very differently than your question would suggest. It comes down to what is in the mind of the consumer. We would argue that

"Consumers of wine enjoy variety and we believe they make their selection from a set of trusted brands that vary based upon mood and occasion."

MAIN BRANDS: Robert Mondavi, Franciscan, Ravenswood and Simi (California); Columbia and Hogue Cellars (Washington); Taylors (New York); Hardys, Banrock Station and Leasingham (Australia); Nobilo, Selaks and Kim Crawford (New Zealand); Inniskillin and Jackson-Triggs (Canada)

there is brand loyalty, just not the same type as you might see with the P&G model. What do I mean by that? The traditional definition of brand loyalty is a one-to-one exclusive relationship. Consumers of wine enjoy variety, and we believe they make their selection from a set of trusted brands that vary based upon mood and occasion. For us, the issue is to have a number of brands in that selection set. We view our portfolio as optimising our opportunity to be with the consumer in as many moods and occasions as possible.

------*Wine Business:* The decision to make Lindemans into a multi-country brand has been poorly received in Australia. Do you think that it will work for Foster's?

------***Richard Sands:*** No.

------*Wine Business:* In many markets – particularly in Europe – the mid-market is looking weak, but that's precisely where Australia has traditionally been situated. Is that a problem?

------***Richard Sands:*** The mid-market is not weak. In the UK, the strongest price points are £3.49–3.99, which is the mid-market. In other European markets the discounters predominate, and it's in those markets where the consumer is not exposed to better wines at higher prices.

------*Wine Business:* The bigger brands in Australia have allowed their winemakers greater freedom and influence than has been the case in the States. Which model do you follow?

------***Richard Sands:*** We give winemakers a great deal of latitude to develop wine styles that differentiate their brands. The advantage we have is that we offer winemakers an uncommonly high level of support and resources to maximize the quality of their wines. The wine style for Kim Crawford New Zealand wines is very different than Ravenswood from California – and we want them to be different, each with its own personality.

------*Wine Business:* The greatest trend globally seems to be the growing power of a shrinking number of wholesalers and retailers. A big company like Constellation can benefit from this trend when negotiating with these giants, but aren't smaller-volume brands like Ravenswood harder to distribute?

------***Richard Sands:*** Ravenswood is a powerful, widely distributed brand. Because we have tremendous portfolio breadth, we maintain separate sales groups that focus on the smaller volume brands and can add value to both the distributor and retailer.

------*Wine Business:* Do you think that Zinfandel will ever have the pull in Europe, or elsewhere, that it does in the US?

------***Richard Sands:*** No, but I think people are interested.

------*Wine Business:* Your genome project made quite an impact. Do you have another study like this in the offing?

------***Richard Sands:*** Our consumer research is ongoing, although Project Genome certainly raised the bar.

------*Wine Business:* Philip Bowman, former CEO of Allied Domecq, once said that public ownership is inappropriate for wine companies, given the period required to establish vineyards, the hazards of the climate, the difficulty in switching styles, and the tendency of stockholders to demand improving results every quarter. How would you respond?

------***Richard Sands:*** We totally disagree. The breadth and diversity of our business helps offset the volatility caused by climate or grape cycles. Leadership and management talent, a clear set of values and goals, and a results-driven organization all help us stay on course to grow our business and increase shareholder value over the long term. A long-term view is important because the journey will periodically encounter rough spots in the road, which happens to every business.

------*Wine Business:* Constellation Brands has only 4.3% of the wine category, far smaller than its counterparts in beer and spirits. How large can it grow?

------***Richard Sands:*** With our focus on providing quality wines at all price points, the potential is unlimited.

------*Wine Business:* Constellation Brands just makes it into the Fortune 500, at number 480. Can you climb that ladder?

------***Richard Sands:*** If they had used our fiscal 2007 results instead of those from 2006, we would have been higher in the listing, but that is not what drives our decision making. ■