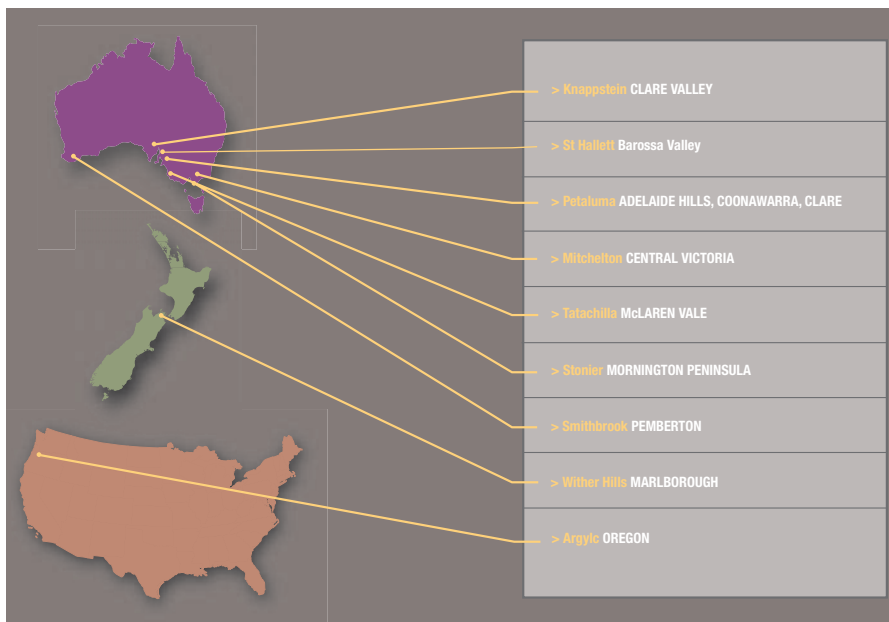


LION NATHAN ROARS

While Foster's writes down the value of its wine division, another important Antipodean brewer is finding that wine suits it very nicely. Felicity Carter looks at how taking a different approach to wine has helped Lion Nathan succeed.



Lion Nathan has wineries in outstanding regions in the New World, including Marlborough, New Zealand, Oregon, USA and the Barossa, Australia.

It wasn't that long ago that two Australasian brewers – Foster's and Lion Nathan – were buying up wineries, thinking to take advantage of the massive growth projected in overseas sales. Of the two, Foster's was bigger and more aggressive; by 2001, the *New York Times* estimated that A\$6 out of every A\$10 the company invested went into wine. And then came the biggest investment of them all: Foster's bought Southcorp for A\$3.2bn (\$3.05bn/€1.96bn), an acquisition that was meant to turn Foster's into a beverages colossus.

And it did, but not in the way they intended. Foster's didn't find the wine business as palatable as it thought. Insiders spoke of wine division employees who felt their expertise was ignored by managers more comfortable with beer, while the on-trade objected to Foster's 'multi-beverage' strategy, where one salesperson would present an entire

portfolio of wines, spirits and beers, often without having any particular knowledge of the wines they were selling.

In June, Foster's chairman David Crawford admitted to the Australian media that the company had paid too much for Southcorp. Foster's wrote down the value of its wine assets by A\$700m (\$667m/€430m). Chief executive officer Trevor O'Hoy, who had been instrumental in the expansion, fell on his sword and resigned.

Rival Lion Nathan took a different, but equally difficult road. By 2001 they had controlling interests in Petaluma and Banksia, which brought nine brands into the company, including Argyle Winery in Oregon. A year later, Lion Nathan bought New Zealand's Wither Hills – at the peak of the market. But things did not go well, as the small scale of the wine division meant they couldn't generate the returns they needed.

Yet today, Anthony Roberts, general manager of the wine division, reports that his business saw profit growth of 40% in 2007 and that he expects similar profits this year.

In a meeting at ProWein in March, Roberts sat down with *Meininger's* editor-at-large Robert Joseph and myself to have a coffee and explain – in a surprisingly lucid way, considering he had just got off a long haul flight – why he believes Lion Nathan is unlikely to suffer the same fate as Foster's.

A snapshot of the company

Lion Nathan has a long history; LD Nathan was founded in New Zealand in 1840 and over the years acquired a series of brewers, including Australia's Tooheys brand and New Zealand's own historic Speight's brewery. By 1990, the forerunner to Lion Nathan was a major Australasian company. Today, Lion Nathan is listed on both Australia and New Zealand's stock exchanges and trades not just in beer and wine, but also in spirits and 'ready to drinks' (RTDs), which are mixtures of spirits and soft drinks largely consumed by the young.

Roberts readily admits that the wine division is "kind of the outsider of Lion Nathan", run as a stand-alone business, with little relationship to the New Zealand liquor business or the Australian beer business, despite the fact that all three report to the same board of directors. It has a strong portfolio of wine brands, largely made up of critically regarded wines from many of Australia's better known regions, including the Barossa, along with New Zealand winery, Wither Hills, in Marlborough. The prestigious Argyle Winery remains the lone US brand.

Despite getting into the wine business late, Lion Nathan has continued to

invest, particularly in distribution. In 2005, when its Australian wine volumes were declining, it created a joint venture with distributor Tucker Seabrook, Australia's oldest fine wine importer, then 10% owned by Bollinger. The venture, called Fine Wine Partners, instantly became one of the largest fine wine distributors in the country, with first year revenues of A\$100m. Today, Lion Nathan owns Fine Wine Partners outright and in June also acquired US importer Cumulus Wine Inc.

The outlay seems to have paid off, as the wine business, which represents less than 10% of Lion Nathan's total business, seems in healthy shape, with strong volume improvement this year (up 8.5%) plus rising revenues, up 12.1%.

In his earnings presentation on 19 May, CEO Rob Murray told the market that despite concerns about the 2008 vintage in Australia, supply and demand for grapes was in balance, plus there has been a bumper harvest in Marlborough. Overall, he said, profitability was up 25%, despite failing to grow in the American market as they had hoped.

"Really, one of the best elements is that we have seen strong growth in our sweet spot: really strong growth in Australia in our portfolio above A\$15 a bottle," Murray finished.

A regional multinational

Roberts says the really smart decision Lion Nathan made soon after they entered wine was to work only with premium wines, or wines that would retail above £7 in the UK market. As part of this, the individual wineries have been allowed a high degree of autonomy. "There's no group winemaking resource or group viticultural resource," says Roberts. "Where group roles come into it is around capital management, or bottle buying."

So the wine businesses are run as separate units, with their own management. "While they're a collection of professionals with the benefit

of a peer group, there's no actual wine style direction."

Roberts says that keeping the units separate brought criticism from the market, because the strategy means the wineries miss out on some of the benefits of a big business. Which raises the question of why Lion Nathan got into wine in the first place, given that the cash flow cycle for beer is so different: production levels can be controlled in line with market demand, and bottles of beer can be out the door and profits put back into the bank within a short space of time. Wine, on the other hand, means not only investing for the long term, but also issues of over- and under-supply.

"There was one enthusiast in the company," says Roberts. "They had big aspirations for what we might be able to do in the Australian wine space."

He says the company realised fairly quickly after they had moved into it that they had bought in at the peak of a boom, and settled on the strategy of making premium wine, because they identified that as where the long term profits would be. "If you look globally

where the money has been over hundreds of years, and generation after generation," says Roberts, "it's been at the premium end of the spectrum." He says the wine group hasn't faced a culture clash with the brewers, because the company recognises that the fast moving consumer goods approach to wine simply won't work.

Roberts, who was originally a chartered accountant, has been with Lion Nathan from the beginning of its wine ventures. Although he initially joined the company on the brewing side, he brought wine trade knowledge with him. "Previous to (Lion Nathan) I was with Yalumba in various capacities," he says. "Obviously I'm not a winemaker, but I've been very involved in operations through to sales. I've seen the good times and the bad times and hopefully the good times again."

The bad times are certainly upon the Australian wine industry, thanks to the drought, the recent grape glut, rising costs and the rising Australian dollar. And as Robert Joseph points out, because the commodity end of Australian wines is in particular trouble, many producers are scrabbling for a share of the premium market - the 'distinguished vineyards' area. Roberts agrees it's a challenge, but says Lion Nathan has an advantage over the big brand players, who need to begin injecting authenticity back into their wines, because they're already in that area.

"If you look at the UK, for instance, in that above seven pound space, it will become very crowded with wines coming up from the lower price points," he says. "I guess it comes back to the fact that we don't play a volumetric game. We're not about to double the size of Petaluma or triple the size of St Hallett's. I guess our faith is convincing the gatekeeper that having the personalities and the consistent style and the message that it's all about region, is what sets us apart."



It just so happens that the company's emphasis on regions has come at the same time that Australia itself has decided to promote regionality heavily, so the company is working in synch with the industry. Lion Nathan is also prepared to be ruthless when it suits, as the closure of the historic Tatachilla winery in the McLaren Vale demonstrates. So how does that fit with the philosophy of maintaining heritage?

"The winery needed significant investment in terms of capital to get it back to where it needed to be," says Roberts. "I guess that while the winery part is different, viticulturally it's no different. We own vineyards in the McLaren vale and have growers that we've had for a long time. Stylistically the wine is the same, so we do still very much stick to that regional presence."

Strong distribution

Robert Joseph, who understands the trade very well, challenged Roberts with a series of (somewhat cynical) observations, pointing out that while UK consumers are willing to pay for "overpriced New Zealand wine without blanching", the same people were unwilling to pay higher prices for Australian wines. At which point, Roberts sighed.

"Certainly. Internally it is frustrating to see the success that New Zealand has had," he said. "If I took an example of something like St Hallett, which is quintessentially Barossa, versus Wither Hills, which is quintessentially Marlborough, it is sad to see the [lower] price we can command for a bottle of St Hallett wine. All we can do is to continue to push that Barossa expression and maybe those fiscal differences will correct over time."

One of the strong advantages the company has is its partnership with A-list distributor Bibendum, which has links with the on-trade in both the UK and Europe. This has meant that Lion Nathan's wines have been less dependent on the off-trade than other major Australian companies.

"Last year in the UK we grew the on-trade at over 50% and I think the benefit

without doubt of being associated with Bibendum has been their on-trade success," says Roberts.

Although sales in the US have been disappointing, Roberts says the company believes there are strong gains to be made in that market if regionality is emphasised, especially when coupled with the fact that the US's consumer dynamic is changing. "There's this whole 25 to 30-plus wine consumer



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*Anthony Roberts,
general manager, wine division*

whose portfolio is made up of 50% of imported wines."

Future growth

Despite the evils of global inflation and depressed consumer sentiment, Roberts says he believes the company's wine sales will keep growing. One reason is the changes to liquor licensing laws in New South Wales, Australia, that are expected to result in the growth of wine bars and increased opportunity for

sales. "Premium wine is just beginning to hit its straps and I think that's exciting. The Australian market is growing at double digits in terms of the above A\$15 segment. Thankfully we're not exposed to the lower price points."

Major growth in sparkling wines is also a bright spot, with sales of up-market brand Croser growing at 40% last year. "We actually thought that with the explosion of French Champagne at much lower price points in Australia, that Australian premium sparkling wine might suffer and we have been pleasantly surprised at the reverse."

The interest in premium sparkling has led them to explore new projects, including the acquisition of New Zealand sparkling wine brand Daniel Le Brun, plus securing distribution rights to Gosset, Duval Leroy and Nicholas Feuillate. There may be further investment in the Adelaide Hills, with a view towards ramping up Croser production.

Lion Nathan, being a publicly listed company, will always be under pressure to return shareholder value, a business model which sits very uncomfortably with wine. And there are already strong calls from the market for Foster's to split itself into a wine and beer company, as the sum of each individual company would be greater. But for now, the financial soothsayers are smiling on Lion Nathan, if only because its beer division is so profitable, and because wine represents less than 10% of overall company revenues. Still, the performance of the wine division is being carefully watched. As ABN Amro's Matt Hoult recently told the Australian media: "If I could get Lion without their wine business, I would be very happy."

Roberts reacts stongly to that comment: "We have no plans to sell our wine business," he says.

Roberts says he takes the long-term view. "I guess that the benefit of coming from a private company that's had generations of involvement in the wine industry [Yalumba] is that it does shape your thinking as to how to be successful in the wine industry," he says. "Just stick to that family approach to running the business." ■

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