

# WINE FINANCING AT THE RABOBANK

Although fine wine is a capital intensive business, there is little talk of the banks that make it possible. The Dutch Rabobank, surprisingly, is one of the largest in that sector. Cees van Casteren and Joel B. Payne spoke with their global wine analyst, Arend Heijbroek, at his Utrecht office just after he returned from Australia and New Zealand.



The Rabobank's headquarters in Utrecht belies the bank's farming roots

Rabobank Group is, at its heart, a cooperative that provides financial services internationally. Its origins are in the local loan cooperatives that were founded in the Netherlands in 1895 by enterprising individuals who had virtually no access to external funding. The 183 local Rabobanks in the Netherlands and the international branches that evolved from them have

always had a particular affinity for the agricultural sector, with wine now accounting for €1 billion in loans. With its 60,000 employees, the Rabobank currently serves more than 9 million clients in the Netherlands and a growing number abroad, where it is represented in 41 countries.

The local cooperative banks and their clients make up the Group's core busi-

ness. In turn, the local Rabobanks are founding members and shareholders of Rabobank Nederland, which advises the banks and supports their local services. Further, Rabobank Nederland acts as an international bank, one of the three remaining world wide with the highest credit rating (AAA), awarded by Standard & Poor's, Moody's and Dominion Bond Rating Service. In terms of Tier I capital, the organisation is among the world's twenty largest financial institutions. In the first half of 2007, Rabobank Group exceeded its target and earned a net profit of €1.4b, up 14% over last year.

Arend Heijbroek, who is a well-known personality at international wine symposiums, is the global industry specialist for wine and spirits at the Rabobank, where he has been for all of his professional career. Trained as a horticulturalist, he was the natural choice for the role of wine industry analyst as the Group gradually moved into this sector in 1980 when it expanded beyond the capital market into international financial services. His reports on both the global wine industry and individual wine producing countries are appreciated by those in the trade.

**Meininger's:** What has changed most since your last trip to Australia and New Zealand?

**Arend Heijbroek:** First of all, there is the impact of drought. Water rights are becoming ever more expensive as they are traded between growers, other industries or city councils. Some of those who do not obtain access to greater rights have thus started buying filtered 'grey' water for irrigation.

## COMPANY PROFILE

Casella is investing in a huge water recycling facility based on reverse osmosis and some city councils have bought purification plants to use seawater for irrigation. I spoke to a grower in Mildura who told me: "I am even more puzzled now than I ever was before, and it isn't positive. We have a major challenge. Last year I was paid A\$200 for my grapes, but shelled out A\$300 for the water rights."

**Meininger's:** What will this mean for Directions to 2025?

**Arend Heijbroek:** Just like Strategy 2025, the implementation of Directions to 2025 is a comprehensive approach based on extensive research. In addition to the generic Wine Australia umbrella brand, it developed a clear plan to promote the 'Regional Heroes'. They were and remain a cornerstone in the plan. Regional Heroes should have increased consumer interest in the different regions as typified through specific varieties and styles at super premium price levels; five years later, though, we must conclude it hasn't happened. Exports of these wines have been stagnant; all of the growth has come from the lower segments, notably the popular premium one. While I was in Australia, I spoke with many producers who asked me how I would sell more super premium wines. My answer was to focus more actively on creating regional identities - like Coonawarra Cabernets, Yarra Valley Pinots and Hunter Valley Semillons - than is currently done.

**Meininger's:** Is this really Rabobank's business, consulting to wine producers? **Arend Heijbroek:** Yes, very much so! We need to support our customers! We help them any way we can. Thanks to our research centre we can share knowledge, statistics and information on both other winemaking countries and export markets. We provide contacts to help them to become better informed, more stable and thus stronger. This research is also useful for our own credit applications. The advisory centre is Rabobank's commitment to industries like wine, beer, spirits, milk and other food products.

**Meininger's:** How important is the wine industry for Rabobank?

**Arend Heijbroek:** Food and agriculture make up approximately 25% of the bank's annual turnover. We have 75 food and agricultural analysts, with three wine research specialists stationed in Australia, New York City and myself here in the Netherlands. Our reports on both the global wine industry and individual wine producing countries distinguish us from other banks, helping us to advise and consult to individual wine businesses.

**Meininger's:** What is your exposure in the wine industry?

**Arend Heijbroek:** Rabobank is involved in almost all winemaking countries, including both China and India, and has some 500 clients in the wine business. Although we are more deeply involved in New Zealand, where we are number one, and Australia, where we are number two, we deal with many large wine producers around the globe, including some spirit companies with a wine division. Rabobank's total investment in the wine industry is currently just over €1b (\$1.42b).

**Meininger's:** And in Europe?

**Arend Heijbroek:** We are also very involved in Spain, a dynamic market where traditional, fragmented production exists alongside the large, modern, branded wine producers that are emerging. In Italy, we are more selective. We stay at the high end of the market with export oriented branded companies. In France it is not easy; Credit Agricole has a virtual monopoly and literally owns many wine businesses. That is not our model. We prefer financing the individual entrepreneurial spirit.

**Meininger's:** What about Germany?

**Arend Heijbroek:** As Germany is virtually owned by discounters such as Aldi, it is not much of a market for us. So many companies are so locked up in the game of staying cost competitive that their margins do not generate any capital to invest.

**Meininger's:** In both of your last reports, you've written about global oversupply and the lack of willpower



Arend Heijbroek is openly critical of the European Union's approach to wine

on the part of the industry to deal with the problem.

**Arend Heijbroek:** Oversupply is clearly not being addressed globally, which naturally has an impact on our business. The notable exception is California, where growers voluntarily uprooted 45,000 hectares of unprofitable vineyards in recent years. Elsewhere, in particular in Europe, growers are buying time. They continue producing grapes, whether their farms are sustainable or not, as long as they have enough cash flow to keep going; but that's not a very long term strategy. In France there is absolutely no demand for vineyards, and subsequently no incentive to sell. Their problems of oversupply, which put undue pressure on successful producers, would be solved if the unprofitable vineyards - especially those of legal heirs being farmed by third parties - were taken out, but nobody is acting. The French government, which has already taken a step in the wrong direction by banning wine advertisements, is not showing any leadership.

**Meininger's:** What does this say for the future of the French wine industry?

**Arend Heijbroek:** I wonder? The French are clever, but they are not salesmen.

They prefer allocating to demand. Further, their future looks muddled. A few months ago, for example, I lectured at the university in Montpellier and asked a class of final year food and beverage students how many were planning a career in the wine industry. Out of the 40 present, only one person raised his hand - and then apologized that he had to take over his father's winery.

**Meininger's:** Isn't this a European problem?

**Arend Heijbroek:** Yes, but the European Union is looking at the issue of oversupply far too simply, and only from the perspective of growers and volumes. The problem, however, is way more complex, and it can only be solved if government intervention in the form of subsidies and crisis distillation is eliminated.

**Meininger's:** You have criticised the European Wine Policy in Changing Competitiveness in the Wine Industry.

**Arend Heijbroek:** The European wine policy is obsolete. We need to decouple production and subsidies, like in the dairy industry. There, farmers receive a subsidy per hectare, but if they are unsuccessful in selling their milk, it is their problem. The current European wine policy doesn't clearly communicate responsibility to growers. The result is that in five years we will be stuck with the same problems we have today. Crisis distillation, which in the 1999 wine policy reform was only to be used in response to an actual crisis, has already become structural. The current policy provides neither growers nor producers a future - and without clear perspectives, they cannot prepare themselves for the long term.

**Meininger's:** What does this mean?

**Arend Heijbroek:** While the wine industry has changed from agriculture to a fast moving consumer goods business, legislation and increased bureaucracy have only added new layers of complication. We are now in a buyers' market - and at the entry level price point the consumer does not really care where the wine comes from. Nevertheless, the bureaucrats think

they know more than the buyers in importing countries. As I have often said, the Eurocrats are part of the problem, but they will not be part of the solution.

**Meininger's:** Are Italy or Spain different from France?

**Arend Heijbroek:** Not really, they are all mature markets in which per capita consumption is still falling. Italy is so fragmented and so individualistic that consolidation is almost impossible. That may be fine in fashion, but not in wine. In Spain, Europe aggravated the problem by supporting a replanting programme that doubled production as demand was in free fall. Further, the wine industries of these countries haven't been able to capture the attention of younger consumers. If you ask the youth in France or Spain what they drink at lunch, they'll tell you water. Wine is the drink of their parents, or worse, their grandparents. Wine is not a lifestyle statement.

**Meininger's:** Isn't that the industry's fault?

**Arend Heijbroek:** Yes, the industry is far too traditional. It should make wines that people want to drink. If countries like France, Italy and Spain hope to maintain their position, they will have to revamp their business plans and develop models which turn their current intrinsic weaknesses, like fragmentation, into strengths. In any case, they will need to develop a more entrepreneurial spirit. However, in order to make that happen, the bureaucracy needs to backtrack a step or two. Maybe a teetotaller like Sarkozy can play a refreshing role.

**Meininger's:** Supermarkets sell more to younger people. Could they be part of the solution?

**Arend Heijbroek:** Supermarkets have indeed contributed to making wine available to the average consumer and their offerings are more transparent. However, at least in Holland, buying wine at supermarkets is becoming increasingly boring. There is no excitement. Consumers still don't know a lot about wine. The supermarkets need to bring back the fun factor.

**Meininger's:** What about the Internet?

**Arend Heijbroek:** I doubt the Internet will change much. It is not personal enough. Foster's recently sold their e-commerce business. There isn't merely one solution for all problems, but personal approaches are more likely to succeed. Business needs to reward loyalty and provide incentives to those who keep buying, like they do in Italy. As each winemaking country has a lot to offer in terms of tourism, the industry needs to combine wine and travel. Europe, however, is not strong at thinking outside the box.

**Meininger's:** What role will emerging markets like the BRIC countries play?

**Arend Heijbroek:** Brazil, Russia, India and China will not be easy to conquer. As a bank, we are strong in India. However, it takes long term commitment. Most brand managers and traders are more opportunistic than those markets allow for. As the risks are high, I would not currently invest in any BRIC country unless I had a reliable local partner who knows his market. Russia, which once drank almost 30 litres of wine per person, at least understands wine as part of its lifestyle, at least much more so than India with only a teaspoon annually.

**Meininger's:** Isn't China different?

**Arend Heijbroek:** Given its size, China is considered the swing factor in many agribusiness industries. If China buys, it will have a huge impact; if China doesn't, it's over. Many of the business models, though, are not as transparent as the industry requires. We finance two companies there.

**Meininger's:** Rabobank is also a major player in spirits and beer. How does wine compare?

**Arend Heijbroek:** Spirits not only have advantages in brand building, but like beer have developed distributional power, which would make most wine producers jealous. Some spirit companies have a wine portfolio to protect market share and offer a full range to satisfy their customers; but selling wine is completely different from moving cognac or gin - and most of those companies are struggling with this.