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An Industry Consolidated

Value and Synergy Through Realignment.

by Mark D. Working

Value is created by profitably satisfying customer needs with quality products and services. It is helpful to keep this principle in mind, as you digest the non-stop chatter in the business media regarding securities-market volatility, scarce credit, and the moribund state of private equity investment. During the six-month period beginning in the last quarter of 2008, Columbia Distributing and The Odom Corporation meaningfully consolidated the distribution of alcoholic beverages in the Pacific Northwest, with the goal of improving industry efficiency.

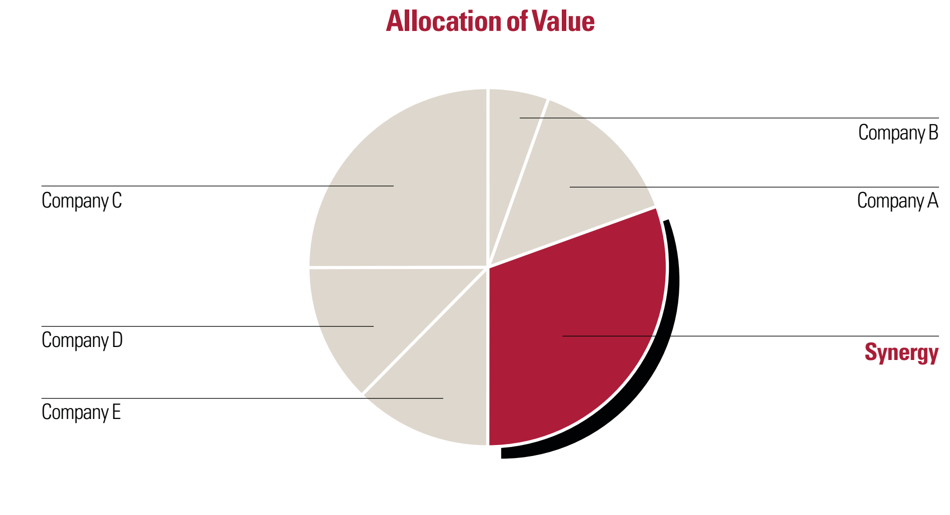
Until recently, Gold River Distributing, Mt. Hood Distributing, Columbia Distributing, Alaska Distributors, and The Odom Corporation each delivered beverages to overlapping territories and customers in Oregon, Washington, and Alaska. At the end of the consolidation, the five individual businesses had become two: Columbia Distributing ("CoHo") and The Odom Corporation ("Odom").

THE IMPETUS

The reason why this consolidation did not occur earlier can be attributed to the disparate personalities, rivalries, and strategies of the brands each firm managed. Miller distributors don't handle Budweiser. Coke distributors won't touch Pepsi. Similar alignments occur in the world of wines and spirits, making a more complicated labyrinth of supplier-distributor relationships than the casual observer could imagine.

Alcoholic beverage distribution is dominated by the major beer brands (Anheuser-Busch, Miller, and Coors) simply because of the volume of these brands, relative to others. Distribution networks across the country have developed to service these individual brands, often times adding craft beers, wine, and spirits (in open states) to the distribution product mix.

Over the recent past, beverage brands have been undergoing a process of consolidation to obtain synergies in production, marketing, and administration. Early in 2008, Miller Brewing Company and Coors Brewing Company merged their operations, including the management of their distribution networks. Their conclusion was that market consolidation of Coors and Miller distributors would reduce costs throughout the system. Encouragement by Miller-Coors management opened up the possibility of strategic distribution system networks in specific markets across the country, including the Pacific Northwest.



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THE VALUE PROPOSITION

In spite of dismal economic news, these mergers were not driven by business distress. Five successful firms were reconfigured to form two dominant players. The economic rationale for consolidation was more efficient utilization of distribution infrastructure. When the business owners and their advisors put their pencils down, the analysis confirmed that delivery fleet, warehouse, customer management, and accounting/IT infrastructure could best be leveraged at scale within a given geographic area. The conclusion was that two networks would represent the most efficient allocation of resources in this region.

In addition to the benefit of being a more important distributor to customers as a result of greater volume, the economic benefits were quite meaningful. As illustrated in the article, "Should Your Business Raise More Capital?" (*IN$IGHT*, Spring 2009), the elimination of duplicate costs and improved utilization of joint assets resulted in a value in excess of that of the individual stand-alone firms. The term may be shopworn, but that is "synergy," which is illustrated by the above chart. The synergy value created was shared among the parties, with those shareholders that decided to sell receiving a premium value, while still leaving a meaningful benefit for those having the task of execution.

THE DEVIL IS IN THE DETAILS

This brief description of a seemingly straightforward business combination does little justice to the difficulty of the transactions or the complexity of the change to be accomplished by the respective CoHo and Odom teams. Prior to the transaction, each of the five individual companies possessed unique portfolios of compatible beer and wine brands, and

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spirits (in Alaska). As a result of the transactions, the supplier mix was not fully aligned, which required migration of certain suppliers to establish a new equilibrium. Columbia Distributing long ago had established a joint venture with a major national wine distributor, Young's Markets, to help with the alignment and retention of brands. As part of its consolidation, The Odom Corporation also formed a wine and spirits distribution joint venture with another national powerhouse, Southern Wine & Spirits.

Both Coho and Odom have challenges ahead to realize their respective value potentials. Greg Christiansen, CEO of Coho, says, "We merged four entities into one, each having its own distinct culture. Now, there needs to be one consistent culture. Achieving that will be important to realize the potential value of the merger." At Odom, the theme is similar, but with its own twist. John Odom, CEO, noted, "This transaction doubled the size of our business. At the same time, we added a partner in Southern Wine & Spirits. By working together and using best practices, we expect to realize substantial efficiencies from our expanded scale."

ATTRACTING CAPITAL IN A STALLED MARKET

The capital markets were in the worst straits of the last 20 years as these transactions were coming together. To suggest that this element of the deal was a snap would fly in the face of reality. Nevertheless, banks and investors were attracted to these situations because they exhibited compelling economics, predictable cash flows, and strong management.

LESSONS FOR OTHERS

Business owners should continually contemplate how their businesses can be more successful in the future. Especially in light of reduced demand for products and services in many industries, a drive toward greater efficiency will move to the fore because of the compelling economics. And, that might mean aligning and consolidating operations with other entities that bring something to the value equation. Despite the tightened credit markets, combinations that improve business performance will attract capital. Concentrate on value creation; capital will follow. ❖

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ABOUT ZACHARY SCOTT

Zachary Scott is an investment banking and financial advisory firm founded in 1991 to serve the needs of privately held, middle-market companies. The firm offers a unique combination of in-depth knowledge of the capital markets and industry competitive dynamics, sophisticated analytical capabilities, and proven expertise in structuring and negotiating complex transactions. For more information on Zachary Scott, please go to ZacharyScott.com.

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