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HD **Treasury is ripe for the picking**

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The performance of Treasury **Wine** Estates (TWE) over the past year has had more than a few shareholders reaching for the bottle so it should not be a huge surprise that an opportunistic private **equity firm** has as come knocking.

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The winemaker, which produces Penfolds and Lindeman's, dropped a bombshell on Tuesday with news that it had knocked back a $3.1 **billion** takeover offer from Kohlberg Kravis Roberts (KKR).

The sudden decision to reveal an approach made more than a month ago is even more intriguing given the **company** has spent the past week denying reports it had received approaches from Constellation Capital and others for its struggling US **operations**.

The trigger was KKR's decision to talk a number of TWE's shareholders about the approach, which chief executive Michael Clarke describes as a "leak" which obligated the **company** to inform the market.

TWE has been a constant subject of takeover speculation since the day it was spun out of Foster's in 2011 but there is a sense of inevitability it will be taken out this time round.

KKR is the latest in a string of private **equity** and potential trade buyers linked to a **company** which has lost the confidence of investors following a string of profit downgrades, a pricing stuff-up over Christmas and a messy management transition under chairman Paul Raynor.

Another private **equity firm**, Cerberus, offered Foster's $2.3 **billion** to $2.7 **billion** for the **wine business** when it was still owned by Foster's in 2010. TPG, which made a packet selling Beringer to Foster's in 2000, and TPG have also reportedly looked at the **company**.

More recently, the talk has focused TWE's troubled US **operations**. TWE last week played down reports Constellation Brands and premium beverage **group**Pernod Ricard were looking at its North American **business**. At the time, TWE did not see the need to mention the fact that KKR had made an offer for the entire **business**.

That approach was rejected, but the **company** looks riper than ever for a takeover bid. This is reflected by an 18 per cent jump in the **company**'s share price which closed at $4.80 on Tuesday following news that KKR had come knocking.

Comparisons will be made to **bread** maker Goodman Fielder which last week bowed to a modest takeover offer from two Asian investors who took advantage of the **company**'s weak share price. A string of earnings downgrades and lack of confidence in the future meant key Goodman Fielder investors were willing to sell their stakes even though the premium was not as high as they would have liked.

The difference with a suitor such as KKR is that the private **equity firm** does not have a track record of engaging in hostile takeover bids. It prefers to avoid bad blood and negotiate on good terms with a target **board**, although talking to shareholders has had the opposite affect.

KKR made a non-binding and indicative $4.70 cash bid for the **company**, one that would imply a value of $3.05 **billion**. That was rejected by TWE on April 16 when the stock was trading a $3.70, which meant the offer represented a 27 per cent premium at the time.

While both sides agreed to keep the engagement confidential, TWE spat the dummy after KKR spoke to a number of its investors about the offer. Both sides have different opinions about whether the cone of silence has been breached or not.

TWE chief executive Clarke says by doing so KKR broke the terms of that confidentiality and it decided to announce the approach to ensure the market was informed. In a conference call late on Tuesday he said TWE did engage with KKR and suggested there would have been continued dialogue if there had not been a "leak".

KKR disputes this, saying there was never a formal non-disclosure agreement with TWE in the first place. Second, talks between its advisers and the shareholders were on a confidential basis and would not have been made public anyway.

Whatever the motive was for going public, the process highlights the minefield companies face when it comes to disclosure obligations. While it was not technically obligated to disclose the approach, the **company** selectively left out the fact it had been sitting on a $3 **billion** offer while denying talk Constellation was looking at the US **operations**.

A hastily issued press release, which initially said the proposal was received in 2016, highlights how quickly things moved from being an amicable discussion to a dispute over confidentiality.

The key now is TWE's shareholders who can pressure Raynor to engage with the private **equity firm**, hopefully to agitate for a higher offer. Clarke appeared to be leaving the door open for further talks.

There are several schools of thought. The **company** could take the money and run, sell of the US **operations** or pursue Clarke's promise to turn things around.

The decision to disclose the KKR approach also forced Clarke to fast-forward an announcement around cost cutting and plans to ramp up its consumer market spending. It is targeting $35 **million** in cost savings in financial 2015, which will involve cutting 5 per cent of its 3500-plus workforce. The **company** has not exactly issued an earnings downgrade but it may as well have given the downbeat tone of Clarke's commentary, which avoided committing to the numbers either way.

The next six weeks of trading are crucial for the **company**'s outlook, but at the same time Clarke wants investors to take a longer-term approach when judging the **company**'s potential value. UBS is forecasting 2014 earning of $182 **million** compared with TWE's guidance of $190 **million** to $210 **million**.

Clarke's strategy rests on investing in the **company**'s luxury brands and has identified spending priorities for 20 of its 83 brands. He still views the US **business** as a growth platform.

It is still early days for Clarke, who has only been in the top job for seven weeks and Tuesday's conference call with investors will do little to resurrect confidence in the **company**. He says there are still some other structural changes he is working on but not ready to announce yet, while trading in Australia is challenging.

The strategic rationale behind KKR's interest is TWE's strong luxury brands with Penfolds the absolute jewel in the crown. The private **equity firm** does not view the **company** as an Australian-specific **acquisition** but likes TWE for the ability to sell its brands more effectively into Asia and **China** in particular. A break-up is inevitable under private **equity** ownership and there appears to be no shortage of buyers for the US **operations**.

There is clearly scope for KKR to go higher. Morgan Stanley analysts note that **wine** assets tend to trade on high multiples given their strategic value. The median of the past 24 **wine** transactions is 13.2x trailing EBITDA, which imply $5.18 a share for TWE.The bid will put the spotlight back on to Raynor-installed director Warwick Every-Burns as an interim chief executive after sacking former chief David Dearie in mid-2013. This followed an embarrassing $160 **million** write-down on the US **business** where six **million** bottles of low-priced **wine** were destroyed.

Goldman Sachs is advising Treasury **Wine**, while Nomura is advising KKR.

Unable to afford to take out Duet **Group** in a takeover bid, Spark Infrastructure is positioning itself for next round of consolidation in the **energy** space by buying a strategic **stake** in its rival.

Spark boss Rick Francis has been keen to do a big deal since he came on **board** in 2012. After losing out on the NSW desalination plant **sale** and passing on the Moomba-Adelaide gas line deal, Francis has been scouting the market for deals.

While some analysts question Spark's motives, the deal looks like it gives them a seat at the table if there is another round of consolidation.

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