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# Australian Vintage Ltd (AVG)

## Cheap wine and three day growth

Recommendation
Hold (unchanged)
Price
$0.45
Target (12 months)
$0.50 (previously $0.65)

**GICS Sector**

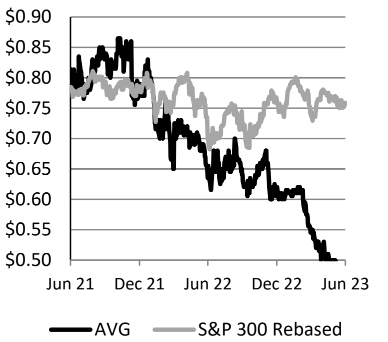
**Food Beverage and Tobacco**

| Expected Return | |
|---|---|
| Capital growth | 11.1% |
| Dividend yield | 0.0% |
| Total expected return | 11.1% |
| **Company Data & Ratios** | |
| Enterprise value | $247.7m |
| Market cap | $113.7m |
| Issued capital | 252.6m |
| Free float | 85.2% |
| Avg. daily val. (52wk) | $75,000 |
| 12 month price range | $0.49 - $0.715 |

**Price Performance**

| | (1m) | (3m) | (12m) |
|---|---|---|---|
| Price (A$) | 0.50 | 0.56 | 0.66 |
| Absolute (%) | -10.00 | -19.28 | -31.30 |
| Rel market (%) | -8.87 | -19.71 | -34.53 |

**Absolute Price**




SOURCE: IRESS

## Continued challenges in commercial wine channels

At headline level AVG's FY23e revenue and EBITDAS guidance were broadly in-line with BPe expectations. Group revenue in FY23e (subject to FX) is expected to fall in the range of $255-260m (vs. $260.1m FY22 and BPe prev. $262.3m), whilst underlying EBITDAS guidance is for $26-28m (vs. $43.7m FY22 and BPe prev. $27.6m). However, we note abovementioned guidance excludes the impact of a $9m fixed cost write off taken below the line which was necessitated by the magnitude of a lower 2023 vintage. AVG's net debt position at FY23e is forecast to be $52-57m and compares to BPe prev. $51.5m.

With growing conditions having worsened during key yield development months earlier this year, AVG's company owned and leased crush came in materially below previous guidance at ~80kt (prev. 96k), representing a ~20% yield decline vs. 2022 (although we note this compares to anecdotal reports from smaller Riverland growers of -30-50% YOY). At this stage the company expects EBITDAS to improve in FY24e to be "directionally" in-line with FY22 (i.e. $43.7m).

Outlook comments include: (1) AVG continues to win market share in premium product segments; (2) declining off-trade consumption trends in commercial wine segments and UK hyperinflation continue to offset branding progress; (3) AVG is targeting $9m cost out in FY24e; (4) a focus on reducing net debt, suspending the FY23e dividend and future dividends until ND/EBITDA (pre-AASB 16) is below 2x (currently ~3x); and (5) AVG flagged potential further asset sales to release value.

## Investment view: Maintain Hold recommendation

Our EPS changes are -10-20% off a low base across FY23-25e. AVG continues to shift its product mix up the value curve, with growth in higher value no and low alcohol categories sales (+44% in 1H23) continuing to effectively offset the company's top-line despite losses in commercial channels (McGuigan -11% in 1H23). However, whilst commercial wine for the meantime still represents the majority of the product portfolio (~65%), the delta on these lost volumes is likely to continue to have a greater absolute (negative) impact on earnings. We retain our Hold recommendation.

**Earnings Forecast**

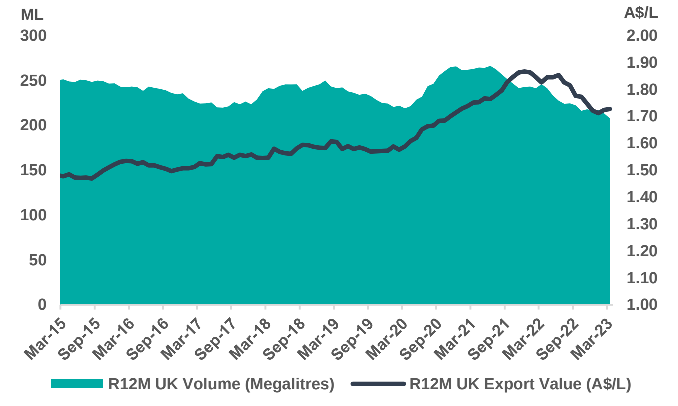
| Year end 30 June | FY22 | FY23e | FY24e | FY25e |
|---|---|---|---|---|
| Sales ($m) | 260.1 | 257.5 | 254.3 | 266.4 |
| EBITDA Total ($m) | 42.3 | 27.1 | 33.2 | 41.5 |
| NPAT (reported) ($m) | 17.3 | 8.2 | 7.8 | 13.2 |
| NPAT (underlying) ($m) | 17.3 | 3.8 | 7.8 | 13.2 |
| EPS (adjusted) (¢ps) | 6.9 | 1.5 | 3.1 | 5.2 |
| EPS growth (%) | -1.8% | -77.9% | 103.5% | 69.0% |
| Price/NTA (x) | 0.48 | 0.59 | 0.55 | 0.53 |
| PE (x) | 6.6 | 29.7 | 14.6 | 8.6 |
| EV/EBITDA (x) | 5.9 | 9.1 | 7.5 | 6.0 |
| FCF Yield (%) | 3.9% | -15.7% | -0.5% | 9.3% |
| Dividend (¢ps) | 3.4 | 0.0 | 1.5 | 2.0 |
| Franking (%) | 60% | #DIV/0! | 60% | 60% |
| Yield (%) | 7.6% | 0.0% | 3.3% | 4.4% |

SOURCE: BELL POTTER SECURITIES ESTIMATES

# Variable earnings drivers

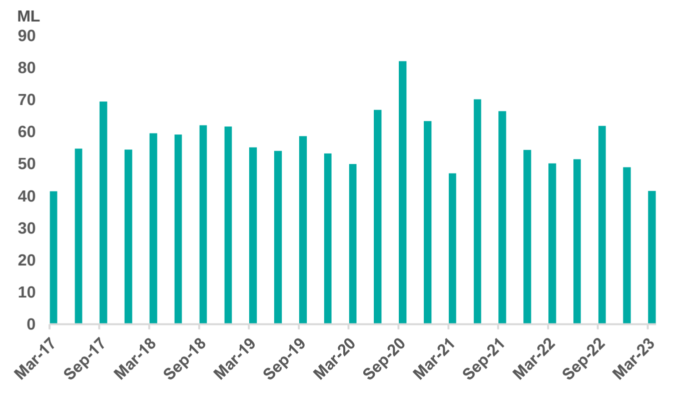
**Australian commercial wine into UK:** Off-trade consumption trends in the UK have continued to retrace from COVID-19 peaks, with sub-$7.50 per bottle wine exports impacted the greatest. AVG's commercial wine losses would appear to be improved vs. sector volume declines of -17% YOY through 1Q23 (-15% R12M). Rising duty taxes on wine in the UK (~20% or ~A$1 per bottle) effective in Aug'23 are expected to pose an additional challenge for lower value wine brands in FY24e (~65% of AVG).

Figure 1 - Australian wine exports to the UK




SOURCE: WINE AUSTRALIA, COMMTRADE

Figure 2 - Australian commercial wine to UK (<$7.50/bottle)

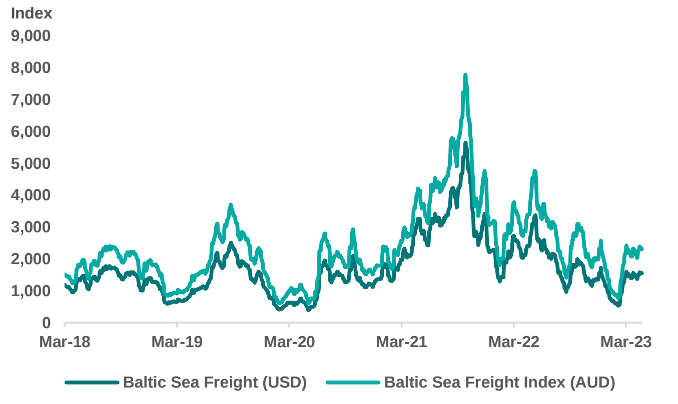



SOURCE: WINE AUSTRALIA, COMMTRADE

**Sea freight:** The majority of incremental FY23e costs called out by management relate to AVG's fixed FY23e sea freight cost and unfavourable AUD/USD movements in early 1H23 (noting AVG does not hedge AUD/USD exposure). Recent shipping trends look more supportive and should see some level of cost reset into FY24e as fixed contracts roll over.

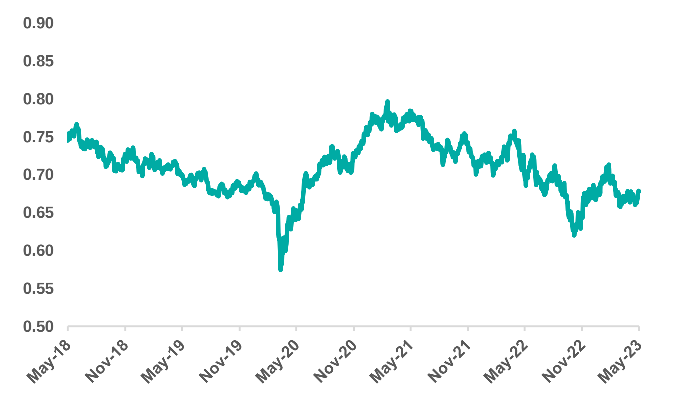
**Australian dollar swing:** Whilst lower for the majority of 2H23 the AUD/USD looks to be exiting FY23e at levels higher than 1H23 (0.68 vs. 0.67) and is continuing to strengthen relative to most new world wine regions.

Figure 3 - Baltic sea freight index




SOURCE: BLOOMBERG

Figure 4 - Australian dollar to USD



SOURCE: WINE AUSTRALIA

# Australian Vintage Ltd (AVG)

## Company Description

Australian Vintage Limited (AVG) is an Australian wine company with operations in vineyards, wine production, packaging, marketing and distribution. The company owns ~352Ha of vineyards (a further ~3,454Ha under lease) with annual crush capacity of 154kt across five key wineries in SA, NSW and VIC.

## Investment View and Thesis

Our AVG PT is $0.50ps and we are Hold rated. Whilst AVG's costs look to be approaching seasonal peaks, in our view this is unlikely to be fully reflected in COGS until FY25e. We are attracted to the secular growth trends AVG is exposed to and the excessive ~40% discount to liquidation value and with limited core asset debt, the potential to add a premium/luxury brand of material scale could generate further improvements in AVG's return profile.

**Strengthening brand:** Despite facing a number of sector headwinds, AVG's brand has improved materially under new management and the company's product premiumisation strategy. Since FY20, AVG has lifted branded wine +18ppts to ~78% of net sales and outperformed sector growth rates in Australia, US and the UK by an average of ~500bps.

**Trading below liquidation value:** Our valuation of the company's liquid assets including inventory, vines, land and mark-to-market water entitlements implies AVG is trading at a material ~40% discount to adjusted NTA ($0.77ps). We note in previous upgrade cycles AVG's valuation can and often does approach near book value.

**Majority of cost challenges transient:** Although volatile, we see most of the challenges faced by AVG as transient in nature. For example, the majority of incremental FY23e costs flagged by management ($17m) relate to the company's fixed FY23e sea freight cost and recent unfavourable AUD/USD movements. In our view, current easing of Baltic shipping prices and currency would support a level of reset in FY24e.

**Secular growth exposure:** As owner of the number one selling non-alcohol wine into the UK (McGuigan Zero +55% FY22), AVG is an early mover in the "better for me" consumer growth trend (e.g. no, low and ready-to-drink alcohol). AVG's recent $62.5m sale and leaseback of vineyards (exited at >100% premium to book value) provides a balance sheet to support acquisitions and future synergy opportunities within this market.

## Risks:

**Agricultural risk:** AVG's access to water and potential yield damage around frost events in company owned or third party suppliers are the largest risks to volume throughput and profitability. Fire, drought and excessive rainfall are also general risks to the sector.

**Australian oversupply risk:** Whilst AVG had negligible direct exposure to the China prior to the Nov '20 tariffs, Australian red wine inventories are currently being held at record levels impacting winemakers' across the price hierarchy. In FY23e we see heightened risk around grapes sold through bulk channels where some may need to be exited below cost.

**Currency risk:** 45-50% of AVG's sales in any given year are into UK markets, meaning the strength of the Australian dollar relative to the British pound can and does have a meaningful impact on the business, given its largely Australian denominated cost base.

**Major customer risk:** AVG operates in a market with a highly concentrated customer base and diverse supplier base. Three customers account for 30% of AVG revenues and as such there is risk around major customer contracts in private label and bottled wine sales.

# Australian Vintage Ltd
as at 15 June 2023

| | |
|---|---|
| Recommendation | Hold |
| Price | $0.45 |
| Target (12 months) | $0.50 |

## Table 1 - Financial summary

| Post-AASB 16 | | | | | | |
|---|---|---|---|---|---|---|
| **June year end** | **2020** | **2021** | **2022** | **2023e** | **2024e** | **2025e** |
| **Profit & Loss (A$m)** | | | | | | |
| Sales revenue | 267.1 | 274.0 | 260.1 | 257.5 | 254.3 | 266.4 |
| *... Growth %* | *-0.8%* | *2.6%* | *-5.1%* | *-1.0%* | *-1.3%* | *4.8%* |
| **EBITDAS** | **34.4** | **45.9** | **43.7** | **27.1** | **33.2** | **41.5** |
| SGARA | (1.8) | (0.7) | (1.4) | - | - | - |
| **EBITDA** | **32.6** | **45.2** | **42.3** | **27.1** | **33.2** | **41.5** |
| Deprec. & amort. | (14.6) | (14.8) | (14.9) | (17.8) | (18.3) | (18.6) |
| **EBIT** | **18.0** | **30.4** | **27.4** | **9.2** | **14.9** | **22.8** |
| Interest expense | (3.7) | (2.6) | (2.7) | (3.8) | (3.8) | (4.0) |
| Pre-tax profit | 14.3 | 27.8 | 24.7 | 5.5 | 11.1 | 18.8 |
| Tax expense | (4.6) | (8.2) | (7.3) | (1.6) | (3.3) | (5.6) |
| *... Tax rate %* | *32.0%* | *29.5%* | *29.7%* | *30.0%* | *30.0%* | *30.0%* |
| Minorities | - | - | - | - | - | - |
| **Net Profit** | **9.7** | **19.6** | **17.3** | **3.8** | **7.8** | **13.2** |
| Abs. & extras. | 1.2 | - | - | 4.3 | - | - |
| **Reported Profit** | **11.0** | **19.6** | **17.3** | **8.2** | **7.8** | **13.2** |
| AUD/GBP assumption | 0.54 | 0.55 | 0.55 | 0.57 | 0.56 | 0.56 |
| AVG crush volume (kt) | 1,014 | 1,166 | 1,014 | 800 | 950 | 950 |
| **Pre-AASB16 operating results:** | | | | | | |
| **EBITDASL** | **27.9** | **39.1** | **36.8** | **17.5** | **21.6** | **29.9** |
| **Balance Sheet (A$m)** | | | | | | |
| Cash | 7.7 | 3.7 | 2.5 | 8.1 | 17.4 | 20.5 |
| Inventories | 149.9 | 153.5 | 179.8 | 153.3 | 164.6 | 166.4 |
| Receivables | 56.2 | 51.6 | 44.8 | 48.9 | 48.3 | 50.6 |
| Other | 1.4 | 0.5 | 1.6 | 1.6 | 1.6 | 1.6 |
| **Current assets** | **215.2** | **209.2** | **228.8** | **211.9** | **232.0** | **239.1** |
| Fixed assets | 114.1 | 111.8 | 114.4 | 92.6 | 97.2 | 101.5 |
| Lease assets | 51.5 | 46.1 | 41.6 | 58.0 | 58.0 | 58.0 |
| LT Inventories | 32.9 | 37.2 | 42.6 | 42.6 | 42.6 | 42.6 |
| Intangibles (excl. goodwill) | 13.0 | 13.8 | 13.4 | 8.3 | 8.3 | 8.3 |
| Goodwill | 37.7 | 37.7 | 37.7 | 37.7 | 37.7 | 37.7 |
| Other | 30.0 | 23.0 | 19.5 | 68.5 | 58.8 | 59.8 |
| **Non current assets** | **279.2** | **269.6** | **269.2** | **307.7** | **302.7** | **307.9** |
| **Total assets** | **494.4** | **478.9** | **498.0** | **519.6** | **534.7** | **547.0** |
| Creditors | 50.6 | 57.7 | 63.2 | 60.0 | 61.0 | 65.3 |
| Lease Liabilities | 6.9 | 5.9 | 6.4 | 6.4 | 6.4 | 6.4 |
| Borrowings | - | - | - | - | - | - |
| Other & provisions | 6.7 | 8.7 | 8.8 | 8.8 | 8.8 | 8.8 |
| **Current liabilities** | **64.2** | **72.4** | **78.5** | **75.3** | **76.3** | **80.5** |
| Borrowings | 75.0 | 46.5 | 77.0 | 59.5 | 69.5 | 69.5 |
| Lease Liabilities | 50.5 | 46.4 | 42.0 | 76.2 | 76.2 | 76.2 |
| Other | 1.3 | 0.9 | 0.7 | 0.7 | 0.7 | 0.7 |
| **Non current liabilities** | **126.8** | **93.8** | **119.7** | **136.4** | **146.4** | **146.4** |
| **Total liabilities** | **191.0** | **166.2** | **198.1** | **211.6** | **222.7** | **226.9** |
| **Net assets** | **303.4** | **312.7** | **299.9** | **308.0** | **312.0** | **320.1** |
| Share capital | 465.5 | 465.5 | 441.5 | 441.5 | 441.5 | 441.5 |
| Reserves | 5.7 | 3.0 | 3.7 | 3.7 | 3.7 | 3.7 |
| Retained earnings | (167.8) | (155.8) | (145.3) | (137.1) | (133.1) | (125.0) |
| Outside equity Interests | - | - | - | - | - | - |
| **S/holders' funds** | **303.4** | **312.7** | **299.9** | **308.0** | **312.0** | **320.1** |
| Net Debt (Cash) | 67.3 | 42.8 | 74.5 | 51.4 | 52.1 | 49.0 |
| Factored payables | - | - | - | - | - | - |
| AASB-16 Operating leases | 57.4 | 52.4 | 48.4 | 82.6 | 82.6 | 82.6 |
| **Group indebtedness** | **124.8** | **95.2** | **122.8** | **134.0** | **134.6** | **131.6** |
| **Performance Ratios** | | | | | | |
| EBITDA Margin (%) | 12.2% | 16.5% | 16.3% | 10.5% | 13.1% | 15.6% |
| EBIT Margin (%) | 6.7% | 11.1% | 10.5% | 3.6% | 5.9% | 8.6% |
| OCF Realisation (%) | 108.9% | 143.2% | 59.4% | -9.4% | 98.8% | 104.6% |
| FCF Realisation (%) | 63.3% | 163.6% | -13.7% | -691.0% | -8.0% | 52.0% |
| ROIC (%) | 4.8% | 8.4% | 7.5% | 2.5% | 4.1% | 6.2% |
| FCF Yield % | 9.3% | 31.4% | 3.9% | -15.7% | -0.5% | 9.3% |
| Capex/Depn (x) | 1.25 | 0.83 | 1.47 | 1.39 | 1.72 | 1.64 |
| Interest cover (x) | 8.84 | 17.26 | 15.73 | 7.18 | 8.75 | 10.30 |

| | |
|---|---|
| Share price ($ps) | $0.45 |
| Target price ($ps) | $0.50 |
| Rating | Hold |
| Issued capital (m) | 252.6 |
| Market cap ($m) | $113.7m |
| Enterprise value ($m) | $247.7m |
| Free Float (%) | 87.1% |

**Note: Enterprise value includes operating leases.**
**EBITDASL is pre-AASB 16 lease accounting less SGARA.**

| **June year end** | **2020** | **2021** | **2022** | **2023e** | **2024e** | **2025e** |
|---|---|---|---|---|---|---|
| **Segments (A$m)** | | | | | | |
| Australia & New Zealand | - | 121.9 | 118.5 | 115.4 | 112.2 | 118.4 |
| UK/Europe/Americas | - | 145.9 | 134.5 | 134.3 | 133.2 | 137.6 |
| Asia | - | 6.1 | 7.1 | 7.9 | 8.9 | 10.4 |
| **Group revenue ($m)** | **267.1** | **274.0** | **260.1** | **257.5** | **254.3** | **266.4** |
| Pillar brands as % of total sales | 65% | 71% | 78% | 77% | 78% | 75% |
| Australia & New Zealand | - | 12.6 | 14.2 | 8.4 | 7.8 | 10.5 |
| UK/Europe/Americas | - | 17.2 | 11.6 | 0.4 | 6.3 | 11.2 |
| Asia | - | 0.0 | 0.4 | 0.4 | 0.8 | 1.1 |
| Other | - | 0.5 | 1.2 | - | - | - |
| **Group EBIT ($m)** | **18.0** | **30.4** | **27.4** | **9.2** | **14.9** | **22.8** |
| EBIT Margin % | 6.7% | 11.1% | 10.5% | 3.6% | 5.9% | 8.6% |
| **Cash Flow (A$m)** | | | | | | |
| EBITDA | 32.6 | 45.2 | 42.3 | 27.1 | 33.2 | 41.5 |
| Net Interest Expense | (3.4) | (2.2) | (2.6) | (3.2) | (3.8) | (3.9) |
| Tax Paid | - | - | (1.8) | (4.5) | (2.5) | (4.5) |
| Change in Wkg Capital | (9.2) | 8.2 | (14.1) | 19.2 | (9.7) | 0.2 |
| Other | 6.5 | (2.0) | (4.7) | (40.6) | 8.5 | - |
| **Operating Cash Flow** | **26.5** | **49.2** | **19.2** | **(2.0)** | **25.8** | **33.2** |
| Lease Payments | (5.9) | (6.5) | (6.4) | (9.6) | (11.6) | (11.6) |
| Lease interest | (4.2) | (4.2) | (3.8) | (3.8) | (3.8) | (3.8) |
| **Lease Adjusted OCF** | **16.4** | **38.5** | **9.0** | **(15.5)** | **10.4** | **17.8** |
| Capex | (10.2) | (6.4) | (11.4) | (11.0) | (11.0) | (11.0) |
| **Free Cash Flow** | **6.1** | **32.1** | **(2.4)** | **(26.5)** | **(0.6)** | **6.8** |
| Dividends paid | (5.6) | (7.6) | (6.8) | (8.6) | - | (3.8) |
| Acquisitions | - | - | - | - | - | - |
| Disposals | 0.1 | 0.0 | 1.9 | 58.1 | - | - |
| Share issues | (4.2) | (4.2) | (27.9) | - | - | - |
| Other | 8.7 | 4.2 | 3.6 | - | - | - |
| **(Inc.) /dec. in net debt** | **5.0** | **24.5** | **(31.6)** | **23.0** | **(0.6)** | **3.1** |
| **Valuation Ratios** | | | | | | |
| Reported EPS (¢ps) | 3.9 | 7.0 | 6.9 | 3.2 | 3.1 | 5.2 |
| Underlying EPS (¢ps) | 3.5 | 7.0 | 6.9 | 1.5 | 3.1 | 5.2 |
| *... Growth (%)* | *23.5%* | *101.9%* | *-1.8%* | *-77.9%* | *103.5%* | *69.0%* |
| PE (x) | 13.0 | 6.4 | 6.6 | 29.7 | 14.6 | 8.6 |
| EV/EBITDA (x) | 7.6 | 5.5 | 5.9 | 9.1 | 7.5 | 6.0 |
| EV/EBITDASL (x) | 8.4 | 8.9 | 6.3 | 6.7 | 14.2 | 11.4 |
| EV/EBIT (x) | 13.8 | 8.1 | 9.1 | 26.8 | 16.6 | 10.8 |
| NTA ($ps) | 0.81 | 0.86 | 0.93 | 0.77 | 0.82 | 0.85 |
| P/NTA (x) | 0.56 | 0.52 | 0.48 | 0.59 | 0.55 | 0.53 |
| Adjusted NTA ($ps) | 0.91 | 0.96 | 1.04 | 0.80 | 0.86 | 0.88 |
| Book Value ($ps) | 1.08 | 1.11 | 1.19 | 1.22 | 1.23 | 1.27 |
| Price/Book (x) | 0.42 | 0.40 | 0.38 | 0.37 | 0.36 | 0.36 |
| DPS (¢) | 2.7 | 2.7 | 3.4 | - | 1.5 | 2.0 |
| Payout on reported (%) | 69.2% | 38.7% | 49.6% | 0.0% | 48.6% | 38.4% |
| Yield (%) | 6.0% | 6.0% | 7.6% | 0.0% | 3.3% | 4.4% |
| Franking (%) | 63.0% | 60.0% | 60.0% | #DIV/0! | 60.0% | 60.0% |
| **Equity Linked Targets & Covenants** | | | | | | |
| 3-yr EPS CAGR (Target >10.6%) | 26.0% | 36.7% | 34.8% | -24.1% | -23.9% | -8.8% |
| ROCE (Target >6.4%) | 4.2% | 7.5% | 6.5% | 2.1% | 3.3% | 4.9% |
| Net debt/equity (%) | 22.2% | 13.7% | 24.8% | 16.7% | 16.7% | 15.3% |
| Net debt/EBITDA (x) | 2.1 | 0.9 | 1.8 | 1.9 | 1.6 | 1.2 |
| Net debt/EBITDASL (x) | 2.4 | 1.1 | 2.0 | 2.9 | 2.4 | 1.6 |
| EBIT bank interest cover | 5.9 | 14.7 | 12.5 | 3.0 | 5.1 | 7.3 |

SOURCE: BELL POTTER SECURITIES ESTIMATES

**Recommendation structure**

**Buy:** Expect >15% total return on a 12 month view. For stocks regarded as 'Speculative' a return of >30% is expected.

**Hold:** Expect total return between -5% and 15% on a 12 month view

**Sell:** Expect <-5% total return on a 12 month view

*Speculative Investments are either start-up enterprises with nil or only prospective operations or recently commenced operations with only forecast cash flows, or companies that have commenced operations or have been in operation for some time but have only forecast cash flows and/or a stressed balance sheet.*

*Such investments may carry an exceptionally high level of capital risk and volatility of returns.*

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