



Growing Smarter

Wine industry benchmarking and insights 2018

New Zealand

February 2019

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Peter Felstead
Partner, Deloitte

It is with great pleasure to present the 2018 results of our annual benchmarking survey in conjunction with ANZ and New Zealand Winegrowers. The New Zealand wine industry continues to perform well on the back of profitability for wineries of all sizes, strengthening balance sheets and a healthy propensity for innovation. We would like to express our sincere thanks to those who provided data for the survey and wish you all the best for the year ahead.



Philip Gregan
CEO, New Zealand Winegrowers

New Zealand Winegrowers seeks to provide high quality data to assist informed discussion and decision making about the industry by our members and stakeholders. We are pleased to partner with Deloitte and ANZ in this winery benchmarking which continues to provide a wealth of industry data and insights. Best wishes for a successful and prosperous 2019.



John Bennett
General Manager
Central Region,
ANZ Commercial &
Agri

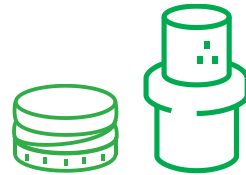
With strong profitability and balance sheets this report makes for positive reading. But with plenty of challenges on the horizon, notably around environment changes and staffing pressure, growing smarter through innovation is particularly relevant. We look forward to further discussion on these themes with businesses in the year ahead.

Key findings

Innovation impact

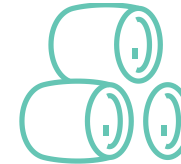
(pages 3 and 4)

Survey results indicate a positive correlation between innovation and financial performance of wineries. Respondents report digital tools are proving most beneficial in terms of improving business decision making and customer experiences.



94%

Investing in developing equipment technologies is important to 94% of survey respondents.



#3

For only the third time in the history of the survey all tiers achieved profitable results.

Profitability stable

(pages 5 and 15)

Positive profitability was achieved across all tiers but as with previous years we saw smaller wineries generally achieving lower returns with far greater variability amongst respondents.

Supply and demand

(page 9)

2018 saw a 1.8% lift in average prices received by Kiwi wineries after sales outstripped supply in the previous year. Prices per litre ranged from \$3.96/l for bulk export wine, \$8.47/l for packaged exports and \$10.34/l for supply into the domestic market.



\$7.33/l

The average sale price per litre received by wineries in 2018.

In 2018 the combined turnover of wineries in New Zealand was estimated at \$2.3 billion, with \$1.7 billion of this coming from export earnings.

2018 survey respondents account for approximately 44% of the New Zealand wine industry by litres of wine produced and 35% by export sales revenue generated for the 2018 year.



56%

Total equity as a percentage of total assets from survey dataset.

Stronger balance sheets

(pages 6 and 16)

Equity levels (as a percentage of total assets) for the wider survey group have been steadily increasing over the last 10 years. These equity levels ranged from 54% (\$20m+ turnover) to 72% (\$5-\$10m turnover).

Return on assets

(pages 8 and 17)

Return on assets (EBIT/Assets) varied across the different tiers in the survey from 2.4% (\$1.5-\$5m turnover) to 8.4% (\$20m+ turnover).



8.1%

The combined total Return on assets (EBIT/Assets) from survey dataset.



86%

Direct to consumer sales via cellar door or online are undertaken by 86% of survey respondents.

Connecting to customers

(pages 11 and 18)

Connecting directly with customers is increasingly important to build trust, brand reputation and profitable sales.

**Vintage
-2018-**

Featured insight #1 – Innovation impact

Kiwi wineries are increasing investment in new plant and equipment technologies

Larger wineries are more likely to prioritise innovation spending

Emerging technologies in the winery are receiving investment priority from larger wineries. These same companies also tended to generate stronger profits and return on assets than other wineries.

Improving quality in the winery drives most investment

This is followed by productivity driven improvements in the vineyard. For larger wineries, winery productivity investments take precedent which is unsurprising given the successful focus on cost of production amongst larger wineries.

Stronger returns are being achieved by wineries that prioritise innovation spending

Survey data indicates a positive link between innovation spending and returns, as illustrated in the following chart. Are financially strong wineries able to prioritise investment because they have more cash to invest, or do they have more to invest as the result of the innovations already applied?

The answer is likely a combination of both factors along with other factors unique to every business.

Smaller wineries have the strongest intentions to increase innovation spending

There are many reasons why smaller wineries may not have invested as much into innovative technologies. The most likely rationale is the relatively weaker cash flows and retained earnings experienced by these companies, which can render costs as prohibitive. Furthermore, some types of plant and equipment become comparatively more cost effective as scale increases. This can make some investment decisions difficult to justify for smaller wineries.

Problem solving

Strong investment intentions suggest potentially cost effective and innovative solutions are on the horizon for the myriad of challenges wineries are facing. Such challenges include staff availability and cost, Health & Safety, and optimising or overcoming biophysical (including water) factors in the winery and vineyard.

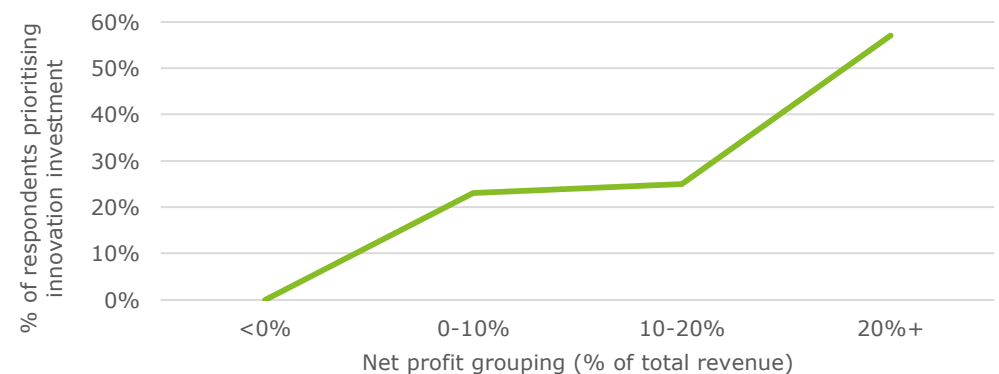
Survey findings supported by other research

A 2018 ANZ report, focussed on innovation in the New Zealand manufacturing sector, found a correlation between investment in innovation and the achievement of productivity gains. The data showed those who invested in innovation had a stronger return on invested capital than those who didn't, and sales revenue grew faster.

Innovative technologies in plant and equipment – 2018 Survey questions

Respondents were asked to describe their investment approach and opportunities in terms of different parts of the business. They were also asked about their investment intentions and how they prioritise spending in regards to technological advancements in plant and equipment. 94% of respondents reported that investing in developing technologies is important.

Linking innovation investment priorities with net profit performance



In the chart above we have grouped responses by net profit (as a percentage of total revenue). We then mapped the percentage of respondents in each group that identified innovation investment as a priority. The positive correlation aligns with the earlier finding that larger wineries, who tend to achieve stronger profitability, are more likely to prioritise innovation investment.

Growing smarter with digital tools

"By using the latest technology we're able to make good decisions more quickly, to reduce our environmental footprint and produce the finest quality wines for our customers."

Emma Marris, Marisco Vineyards

Survey results indicate that wineries are adopting digital tools for a range of reasons , the top three being:

1. Improving customer experience & engagement
2. Improving business decision making
3. Improving staff experience and engagement

Larger wineries are leading with a broader range of digital tools

The Internet of Things (IoT) uptake is a great example of larger wineries leading the adoption as they use IoT technology far more than smaller companies. Furthermore, across all tiers of digital tools, larger wineries have the strongest intentions to increase adoption and engagement with digital tools.

Cloud based applications, mobile and social media are most used technologies

Use of most digital tools appears to increase with scale, with the exception of social media which appears to be well used by wineries of all sizes.

Smaller wineries are also leveraging technology

Many smaller wineries are maintaining competitiveness in a tight market by leveraging technology to connect and engage with customers. All for a relatively low cost investment.

Survey findings supported by other research

Studies by Deloitte internationally have supported our findings that a benefit of digital tools is an improved customer experience.

Digital tools change the way customers engage with businesses and provide an opportunity to strengthen customer relationships. They help businesses target more customers in new markets.



In with the new but don't throw out the old just yet!

Digital tools are becoming easier to use, and the value of them is becoming better understood. But it appears these tools are not yet seen as transformative to business. In other words they are primarily seen as complementary, rather than replacements for processes and tools already in place.

Digital tools – 2018 Survey questions

Respondents were asked about the range of digital tools used in their business and the benefits associated with increased adoption of those tools. Finally they were asked about their intentions in relation to adoption and engagement of digital tools.

Recommendation

For wine businesses, use this report as a prompt to think about where you are at in terms of investing in innovative technologies. Remember also that innovation isn't necessarily about financial investment. It's very much about a way of thinking, of doing things differently and better. What can you do to foster a culture which drives innovation?

You don't have to reinvent the wheel, think about what you can learn from other businesses who are innovating and using digital tools.

Further reading:

[Deloitte - Tech Trends 2018: The symphonic enterprise](#)

[Deloitte - The digital transformation of customer services](#)

[ANZ - Innovation & Productivity Report 2018](#)

Survey insights – Profitability

Positive profit across all tiers of surveyed wineries suggest 2018 was a good year

All tiers reported positive profit for only the third time in the history of the survey

On averaging the results for each turnover category we found they all recorded a positive profit before tax result for only the third time in the twelve year history of the survey (2014, 2016 and 2018).

Consistent performance amongst larger wineries

The \$20m+ category once again achieved the largest average profit after tax at 18.7%. Total expenses at 19.3% of sales were lowest amongst this group. This reinforces the results of previous surveys showing that generally profitability increases with size due to economies of scale.

Cost challenges amongst smaller wineries

At the other end of the scale the two smallest tiers of wineries had the highest levels of expenses and the lowest profitability as a percentage of sales.

Income diversification and variability are features of small to mid-size wineries

The variability of profit margins amongst smaller wineries is evident in the bottom two charts. The black line indicates the median (or 'middle') profit margin with the shaded bars capturing the profit margins of the 'middle' 50% of participants.

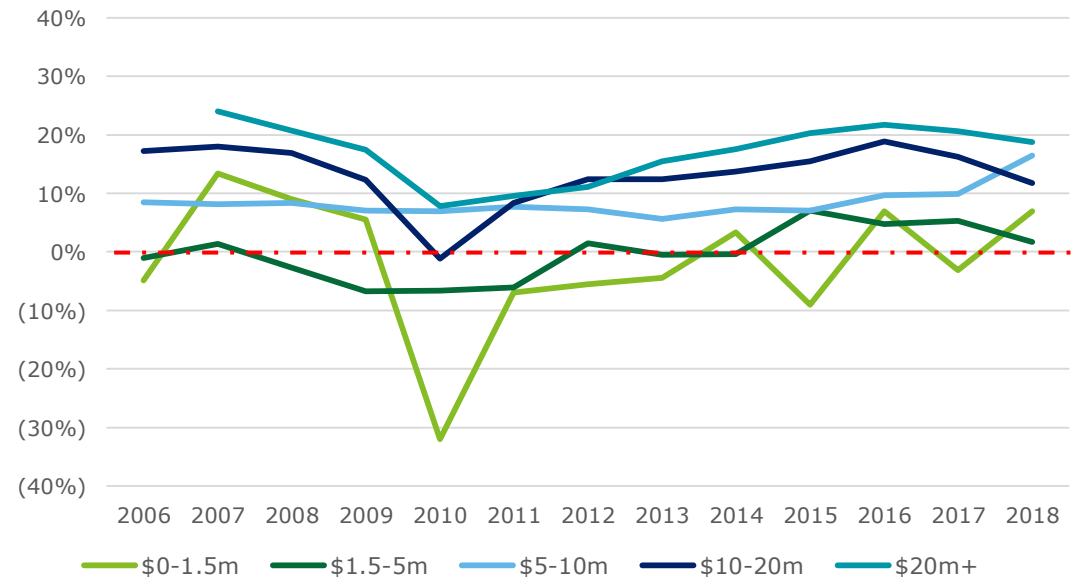
Furthermore, smaller wineries typically generate 10-15% of revenue through means other than wine sales. Grape and hospitality sales feature amongst other sources of revenue.

Impact on balance sheet

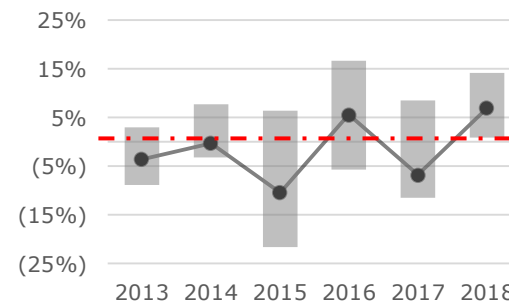
One consequence of volatile and weak profitability generally experienced by smaller wineries is the inability to accumulate retained earnings. This is in contrast to larger wineries which are generally able to build up strong reserves. Retained earnings offer businesses flexibility and options.

The full survey results and further profit and loss analysis can be found on page 15 of the report.

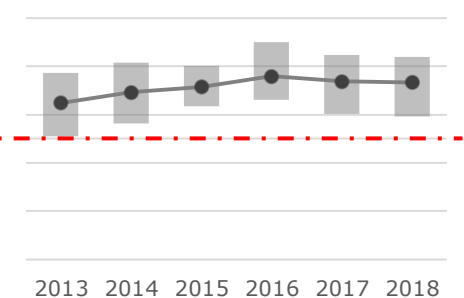
Profit before tax – All wineries
(as a % of sales; average by turnover band)



Profit before tax - \$0- 1.5m turnover
(as a % of sales; quartile range)



Profit before tax - \$1.5m- 20m+
(as a % of sales; quartile range)



Survey insights – Balance sheet

Balance sheets strong as equity levels rise in 2018

Equity ratios have strengthened across the survey group

It is also pleasing to see all tiers reporting average levels of equity above 50% in proportion to total assets. The chart above right uses linear trend lines to illustrate equity ratio improvements over the last ten years.

Smaller wineries most reliant on shareholder funding

For the purposes of benchmarking, shareholder loans have been treated as 'quasi equity' as they reflect shareholder capital. This has propped up equity levels for this tier.

Another feature of smaller winery balance sheets is reflected in the chart to the bottom right of the page. Here we see working capital (being current assets less current liabilities) peaking at the \$1.5-5m tier at 50% of assets.

This is mostly driven by higher levels of inventory than the other tiers. Of course varietal mix could well play a

role here, with some varietals being retained on the balance sheet significantly longer than the dominant Sauvignon Blanc varietal.

Larger wineries achieve largest equity lift and apply tight working capital processes

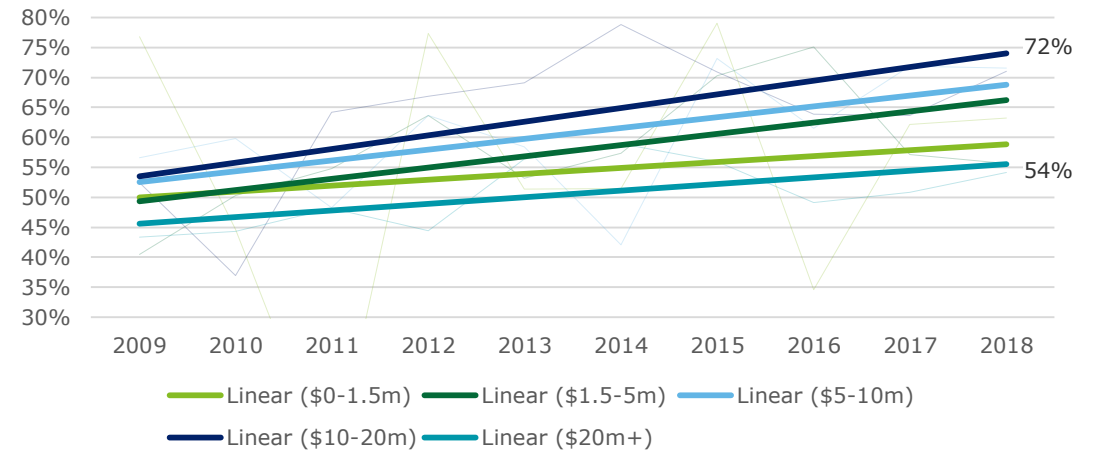
From 2017 to 2018 equity levels lifted most dramatically in the \$10m+ tiers, off the back of reductions in debt levels.

On the working capital front we can see that relative levels (including inventory) tend to reduce as winery scale increases.

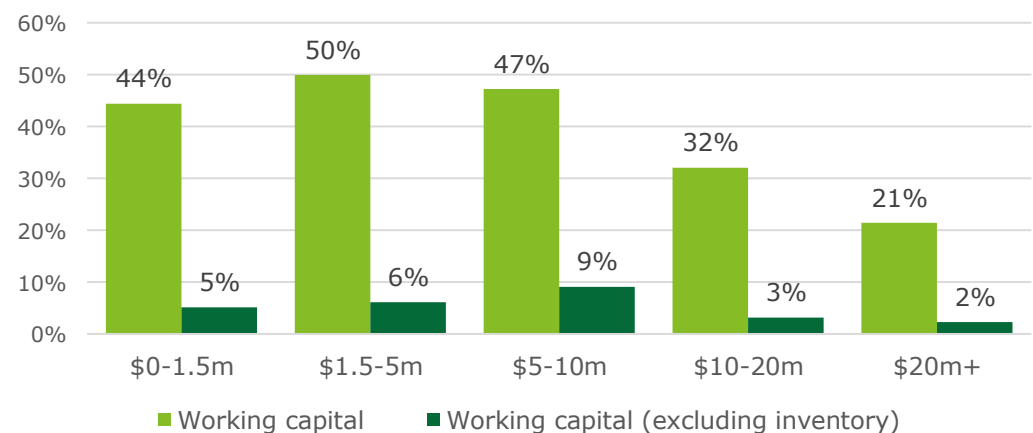
Aside from the influence of varietal mix (as noted above), this is likely a result of the larger operators maintaining more sophisticated and efficient processes, and procedures to manage lower levels of working capital than their smaller counterparts.

The full survey results and further profit and loss analysis can be found on page 16 of the report.

Total equity
(as a % of total assets)



Median working capital
(as a % of total assets)



Survey insights – Key ratios

Taking a closer look at revenue per employee and domestic vs export sales

The domestic vs export story

As evidenced by the bottom chart the \$0-1.5m category strongly favours domestic sales. For the smaller producers, sales into the domestic market often appear more attractive at smaller scales with generally lower marketing and distribution costs, shorter cash cycles and no currency risk.

Similarly with NZ wine export values growing past \$1.7 billion, it is not surprising that larger wineries are targeting and capitalising on export markets at scalable volumes when compared to that of the domestic market.

The domestic/export split is almost directly converse when examining the largest and smallest tiers of respondents. With the smallest wineries selling 69% of their wine into the domestic market. The largest wineries are selling 66% of their wine into export markets.

The revenue per FTE story

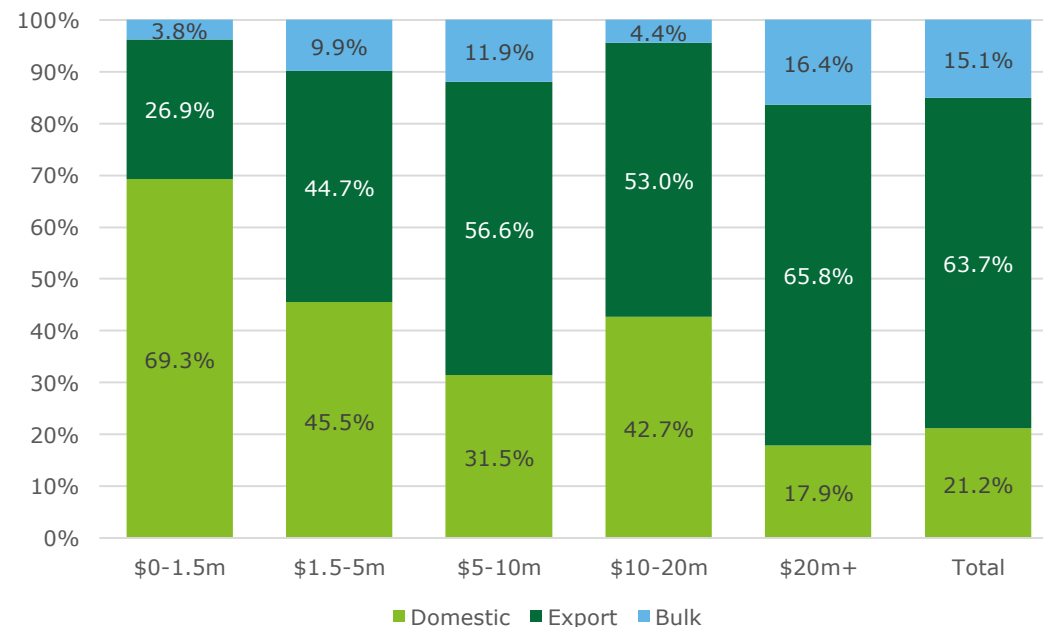
This is the first year the survey has asked participants for data on employee numbers so that we can see the relative revenue per full time equivalent (FTE). As expected the smaller tiers had a lower revenue per FTE reflective of the owner operator nature of many of these businesses.

For purposes of this survey, we grouped all \$20m+ turnover wineries into one tier. Despite a clear distinction between the number of employees for the \$20-\$100m and \$100m+ tiers, there is a strong similarity for the revenue per employee. This suggests limited efficiencies (in terms of revenue per employee) are gained when wineries expand beyond \$20m turnover.

The full survey results and further profit and loss analysis can be found on page 17 of the report.

| | \$0-1.5m | \$1.5-5m | \$5-10m | \$10-20m | \$20m+ |
|-------------------------|----------|----------|---------|----------|---------|
| Per FTE employee | | | | | |
| Average FTE | 3 | 13 | 24 | 29 | 123 |
| Revenue | 276,368 | 317,481 | 450,796 | 611,001 | 786,134 |
| Gross Profit | 126,413 | 139,534 | 162,141 | 256,240 | 326,325 |
| EBITDA | 42,509 | 31,836 | 46,470 | 113,999 | 181,822 |
| Profit before tax | 13,902 | 10,609 | 38,079 | 74,470 | 127,965 |

Wine sale dollars by type



Survey insights – Return on assets

Results reveal significant variation, with larger wineries generally achieving greater returns

An important and useful comparative measure

Return on assets (RoA) is an important measure of the performance of any business' assets, especially capital-intensive businesses such as integrated wineries.

Whilst there are a number of ways to measure this return, we have opted for earnings before interest and tax (EBIT) divided by total assets.

The 2018 Survey shows an average return range from 5.7% for our \$0-1.5m participants to 8.4% for those with revenue in excess of \$20m.

Revenue per litre and RoA

A negative correlation exists between levels of revenue per litre and returns on assets as evidenced by the chart (below right). As winery size increases, the revenue per litre tends to decrease due to the sales mix in terms of varietal, and export mix of bulk and packaged formats. We note larger wineries selling a higher proportion of bulk wine which is at the lowest price point.

Conversely we see return on assets generally increasing with winery scale. As noted earlier, larger wineries are generally more profitable. Again many factors play a role here, most notably economies of scale where resource capacity is maximised comparative to smaller wineries.

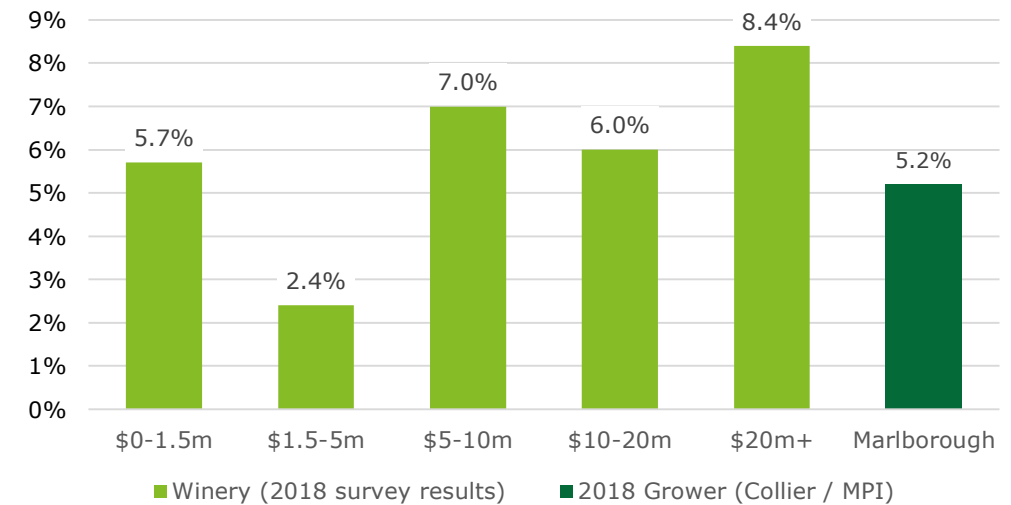
Surveyed winery returns compared to Marlborough grower only model

As a comparison, we have included in the chart (above right) the RoA from the 2018 Marlborough Vineyard Benchmarking Report produced by New Zealand Winegrowers and Ministry for Primary Industries. The 5.2% RoA figure is based on EBIT/total assets for the Marlborough Vineyard Model. This is indicative of returns achieved in 2018 by Marlborough based winegrowers that sell grapes to wineries.

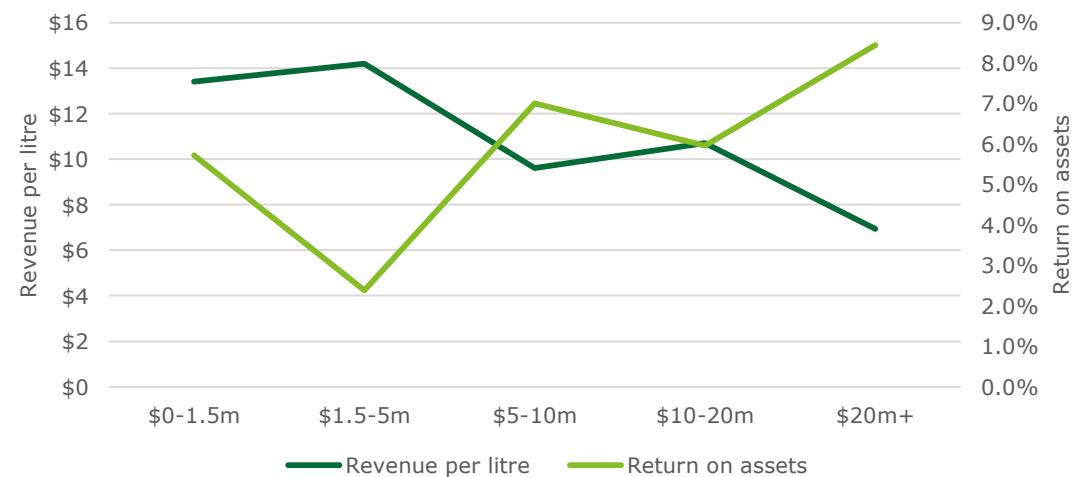
Winegrowers can access further information on viticulture benchmarking by visiting [NZ Wine](#) or [MPI](#).

Comparison of returns on assets

Source: Deloitte, NZ Wine, MPI, Colliers International



Revenue per litre vs return on assets



Industry insights – Supply & demand

Another strong export performance from Kiwi wineries saw total wine sales lift again in 2018 with a small uplift in prices to support total earnings

Wine exports grew for the 23rd consecutive year

In the year ended 30 June 2018 the value of New Zealand wine exports grew, for the 23rd year in a row, by 2.5% to reach \$1.7 billion.

Export volume growth slowing

Export volumes continued to increase in 2018 but the rate of increase slowed with just 0.8% more wine exported than 2017.

Domestic market supplemented by imports

Wine sales within New Zealand accounted for 17% of total wine sold with the remainder exported. The lower volume from the 2017 vintage, combined with the lift in wine exports, resulted in a 2.4% increase in wine imported into New Zealand in 2018.

Supply shortfalls drive increase in 2018 export price to \$6.70/l

Every year we analyse the scale of the vintage (in litres) and deduct export and domestic sales volumes from the following year to provide an indicator of the size of surplus or deficit carried over. Generally we observe a lift in export prices in the years following a volume deficit.

The adjacent chart (top right) illustrates how this played out in 2018, with export prices averaged across packaged and bulk lifting 1.6% to \$6.70 per litre. Further analysis shows that packaged export prices lifted 3.3%, whilst bulk prices lifted 0.5%.

Domestic price lifts to \$10.34/l

We are able to derive an average domestic market price by analysing industry, Statistics NZ and survey data. For 2018 this came in at \$10.34/l, up 3.4% on 2017.

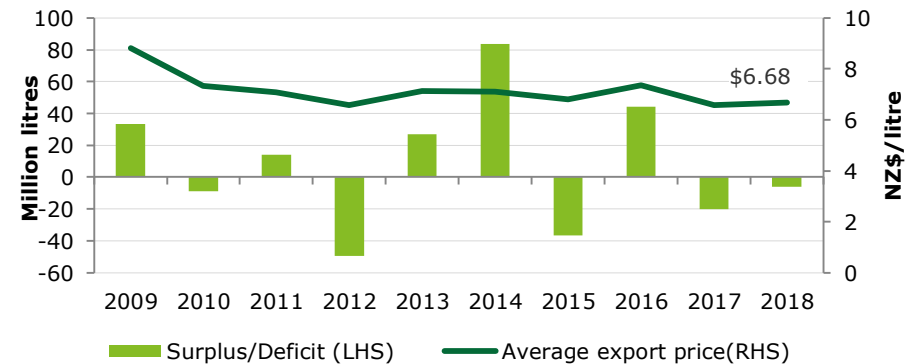
All markets average wine price of \$7.33/l

Combined analysis reveals a lift of 1.8% on average prices received by wineries for all sales across all markets to \$7.33/l, as reflected in the bottom chart.

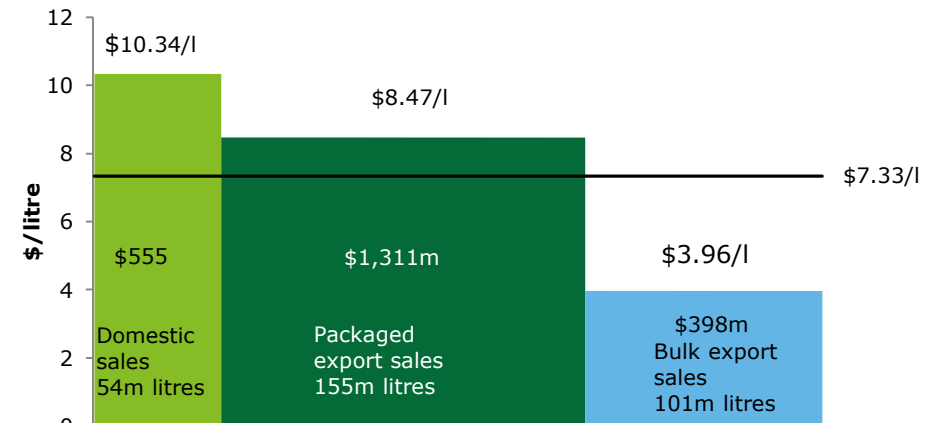
Medium term outlook remains positive

We expect supply growth to slow in coming years as available vineyard development land dwindles due to historical planting rates in Marlborough and competition from alternate land use in other regions. Coupled with continuing market demand from existing and emerging markets this points towards a positive medium term outlook for New Zealand wine.

NZ wines surplus/deficit and average export price



New Zealand wine sales for 2018



Source: ANZ, Deloitte, Statistics NZ, NZ Wine Growers

Industry insights – Key markets

With export sales already looking healthy we ask if the value of New Zealand’s wine exports could improve by further market diversification?

US remains most valuable market

Eighty percent of the wine exported from NZ is bought by just three markets: United States, UK, and Australia. The US is second only to the UK in terms of volume but with strong bottled and bulk pricing it is the number one market by value for New Zealand wine. A review of the export market for bottled wine exports (refer to p.19, Appendix) reveals the impressive growth story of the US market. Undoubtedly further growth opportunities exist in the US but there are some question marks over whether price points can be maintained.

Asian markets deliver higher returns

The price obtained for New Zealand wine exported to the Asian markets of China, Hong Kong, Singapore, and Japan is twice the average export price. These Asian markets account for just 2.5% of NZ’s wine exports indicating significant growth potential. Other markets where returns are at least 25% higher than average include Canada, Norway and Finland.

Trade agreements bring opportunity

With reduced tariffs brought about by the CPTPP Canada (already our 4th largest export market) and Japan (10th) are shaping as top candidates for growth opportunities.

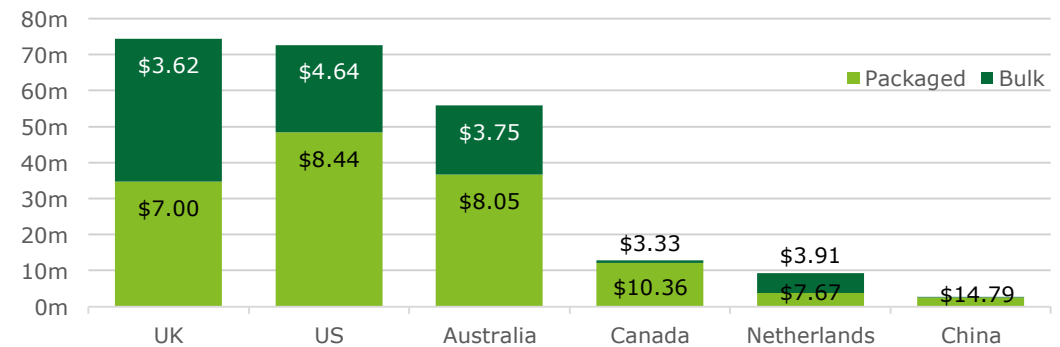
Sauvignon dominates but other varietals offer opportunities

Sauvignon Blanc remains the mainstay amongst export markets (86% by volume) which is unlikely to change any time soon. That said, strong growth in export volumes has been recorded over the last five years with two styles standing out - particularly Pinot Gris and Rose.

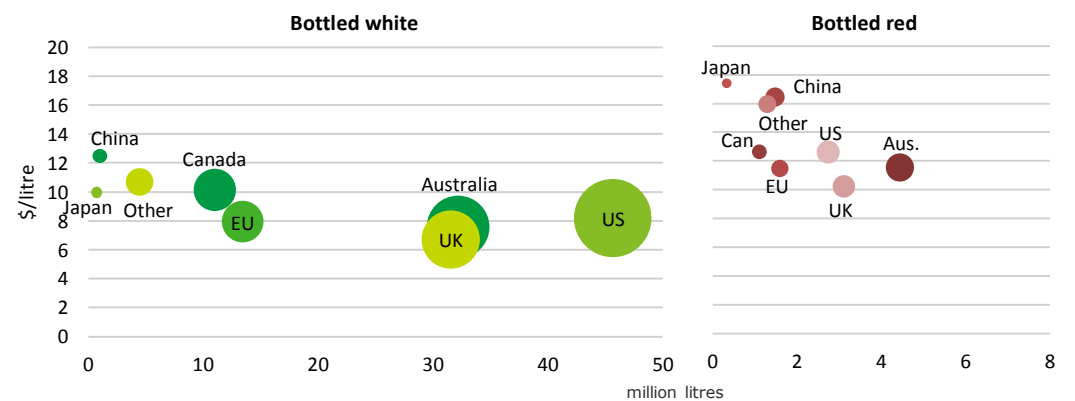
"Spreading our international sales across multiple markets and carefully managing key relationships allows us to grow sales profitably in a competitive environment. We are now planning for 3 – 5 years ahead on how to manage industry and operational pricing increases while lifting sales volumes."

Daniel Nelson, Hāhā Wines

Exports to main markets & average export prices in 2018



Bottled wine export prices, volumes and values 2018



● Bubble size denotes total market value, where a bubble of this size indicates \$100m value

Source: ANZ, StatisticsNZ

Featured insight #2 – Customer connections

Connecting directly with customers is increasingly important to build trust, brand reputation and profitable sales

Standing out in a crowded marketplace

All wineries have a need to connect directly with existing and potential customers. Markets are crowded with competition coming from other wine growing regions as well as other luxury beverages and consumables.

The majority of New Zealand's wineries produce less than 25,000 cases annually with quite limited resources to support a broad range of sales channels. Many of these wineries are finding different and relatively inexpensive ways to connect with customers to drive patronage and direct sales.

Direct sales generate more value

In this year's survey we looked into the relationship between gross margin and direct to consumer sales. We analysed all survey responses and combined online and cellar door sales revenues (as a percentage of total revenue), then we plotted this data against Gross Margin (as a percentage of total revenue).

As per the chart shown across the page, there is a positive correlation between gross margin and percentage of direct to consumer sales as shown by the trend line. This is unsurprising as direct sales mean less intermediate parties clipping the margin along the way. What is less well understood is whether wineries are able to achieve premium margins across all sales tiers by forming stronger direct connections with customers.

Trust and brand reputation

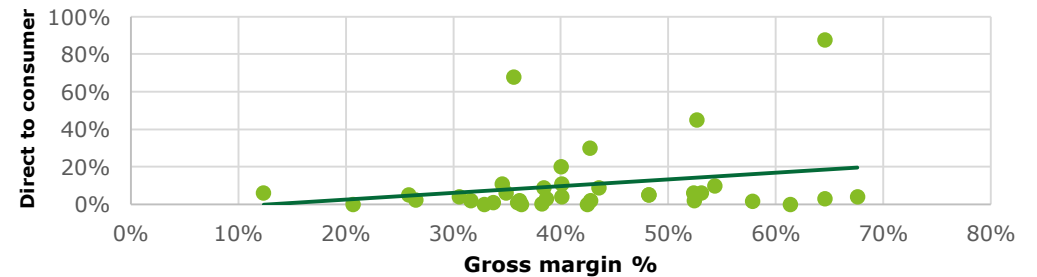
Regardless of scale or sales channel, most wineries understand the ongoing need to identify and engage directly with customers to ultimately support sales.

Know your customer first

A clear understanding of target customers is a pre-requisite to any successful engagement strategy. That said, effective customer engagement strategies can serve a key role in refining that understanding via real-time feedback.

With technology evolving rapidly, new and exciting methods of engagement continue to surface both here and abroad.

Gross margin vs direct to consumer



Sustainability credentials

98% of New Zealand's vineyard producing area is certified under the award winning Sustainable Winegrowing New Zealand (SWNZ) programme. Furthermore over 10% of New Zealand wineries hold organic certification. These are impressive credentials reflective of a winegrowing and winemaking culture that embraces responsible production systems.

Traceability & authentication

Transparency and traceability are becoming increasingly important as consumers seek assurances of environmental and social responsibility. By employing credible and auditable systems wineries can work to meet this consumer need. One cutting edge example being developed comes from the recently launched HUI Māori Collective. This group is using blockchain technology to authenticate food and wine products sold into the Chinese market.

Connecting through experiences

Hosting customers, either onsite or using virtual or augmented reality experiences, is an effective way of demonstrating credentials. How wineries gain customers' attention in order to earn the right to host customers is a whole other matter and that is where retail placement, media coverage (mainstream or social), awards and influencer endorsements play a key role.

"Focusing on real and personalized interactions with our customers through on-site accommodation and wine tours has enabled us to build lasting relationships, generating repeat sales and future champions of our brand - wherever they reside in the world."

Nick Gill, Greystone Wines

About and further information

Deloitte has conducted this annual financial benchmarking Survey in conjunction with ANZ Bank New Zealand Limited (ANZ) and New Zealand Winegrowers . The Survey was conducted between September 2018 and December 2018 and is based upon the 2018 financial statements. The Survey is designed to assist wine businesses by providing an insight into the relative efficiency and financial performance of their business – information to aid decision-making, to support and sustain growth, or assist capital raising initiatives.

Survey questionnaires were sent to all members of New Zealand Winegrowers. Comments made in this report are based on the responses of 36 Survey participants, which account for approximately 44% of the New Zealand wine industry by litres of wine produced and 35% by export sales revenue generated for the 2018 year. Respondents either own or lease 39% of the 37,969 producing hectares currently under vine in New Zealand. To assist the comparison of different sized wineries, respondents have been categorised into five tiers based on total annual revenue as follows:

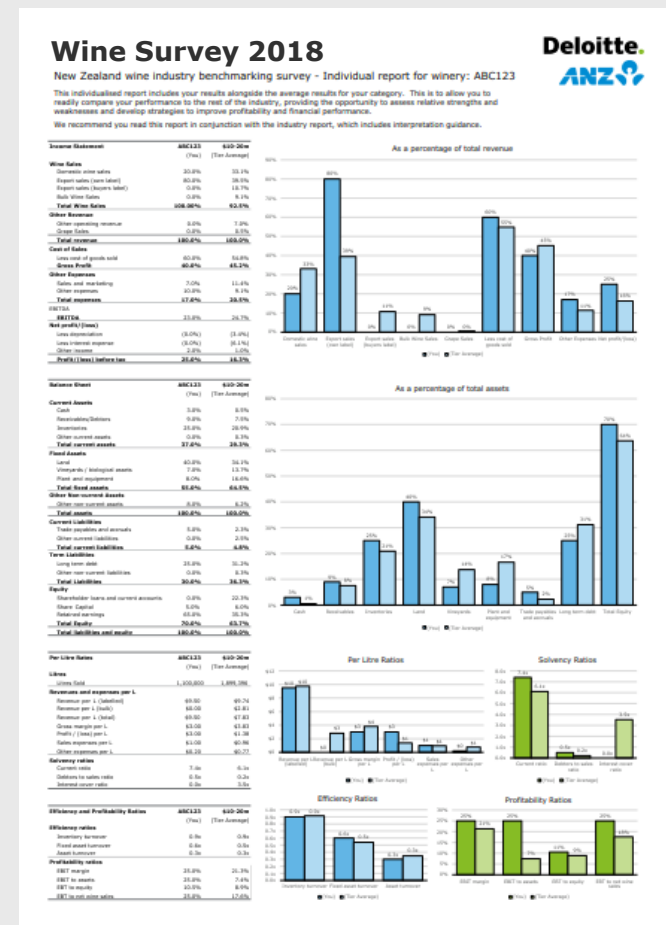
- \$0-\$1.5m
- \$1.5m-\$5m
- \$5m-\$10m
- \$10m-\$20m
- \$20m+

Participant information is treated with high confidentiality. The results are reported in aggregate form with no disclosure of the names of the individual participants, nor how many participants existed in each category. Where appropriate we have also commented on the results. Though the Survey response level is reasonable this Survey cannot be considered completely representative of the whole of the New Zealand wine industry. Care must therefore be taken when analysing the state of the industry based on the information set out in this Survey, although we believe it does provide an indication of industry performance and trends. Figures presented have not been adjusted to eliminate rounding variances. The survey is not advice. You should seek professional advice relevant to your individual circumstances.

New Zealand Wine Benchmarking Industry Report 2018 co-authors and contributors:

- Josh Hawkey, Rob Simcic, Susan Kilsby, Anteni Schalken, Murphy Turner, Philip Gregan, Peter Felstead, Andrew Gibbs, John Bennett, Kyle Uerata, Briar McCormack.

All participants receive a customised benchmarking report, comparing their own results to others of similar revenue size.



The leading teams in the business of wine

Deloitte.

Deloitte New Zealand brings together more than 1300 specialist professionals providing audit, tax, technology and systems, strategy and performance improvement, risk management, corporate finance, business recovery, forensic and accounting services.

Our dedicated professionals are passionate about the sector and enjoy providing a range of services to wineries. We are proud to have been producing our annual wine industry financial benchmarking survey since 2005.

For more information about Deloitte in New Zealand, go to our website www.deloitte.co.nz.



I provide tax planning and compliance advice to a wide range of corporate clients. In particular I advise large exporters, including in the agri sector on international tax and supply chain matters and have assisted non-residents with structuring their investments into New Zealand.

Peter Felstead
Managing Partner
Tax & Private



I co-lead our Primary Industry team which is predominant focussed on working with the sector to address their growth and regulatory challenges. I have wide experience in investigation, project management and advisory work performed in connection with feasibility studies, business change and planning in the public and private sectors.

Andrew Gibbs
Head of Primary Industries & Partner
Corporate Finance



ANZ is proudly New Zealand's largest financial services provider, with almost half of all New Zealanders having a banking relationship with us.

We have dedicated Wine Sector Specialist Relationship Managers located across the country. Our team aspires to make business easier for our winery customers by providing access to knowledge, insights and connections.

For more information about ANZ, visit our website www.anz.co.nz and to learn more about our insights visit [ANZ Business Insights](#)



I am responsible for the Central region of Commercial & Agri. I have over 20 years' banking experience in the UK and New Zealand across markets, trade and asset finance, Institutional, Commercial and Agri banking. I am proud to have supported numerous wineries over the years with structured lending solutions and value add connections.

John Bennett
General Manager – Central Region
Commercial & Agri



I lead our Food & Beverage sector support strategy. I provide insights and connect businesses through our regional, national and global network. I have over 15 years' banking experience supporting the agri-food sector and live on a small Sauvignon Blanc vineyard in Marlborough.

Rob Simcic
Head of Food & Beverage,
Commercial & Agri

Appendix

Profitability

Income statement 2018

| | \$0-1.5m | \$1.5-5m | \$5-10m | \$10-20m | \$20m+ | Total |
|-----------------------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Wine sales | | | | | | |
| Domestic wine sales | 58.1% | 43.2% | 27.4% | 39.2% | 17.4% | 20.4% |
| Export sales (own label) | 12.2% | 40.4% | 48.9% | 45.2% | 61.6% | 58.9% |
| Export sales (buyers label) | 10.4% | 1.4% | 0.3% | 3.6% | 2.5% | 2.4% |
| Bulk wine sales | 3.2% | 4.2% | 10.4% | 4.0% | 16.0% | 14.4% |
| Total wine sales | 83.9% | 89.2% | 86.9% | 92.0% | 97.4% | 96.1% |
| Other revenue | | | | | | |
| Other operating revenue | 7.1% | 5.0% | 5.2% | 3.0% | 1.8% | 2.2% |
| Grape sales | 9.0% | 5.6% | 4.9% | 0.7% | 0.6% | 1.0% |
| Hospitality revenue | 0.0% | 0.2% | 3.0% | 4.3% | 0.2% | 0.7% |
| Total revenue | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |
| Cost of sales | | | | | | |
| Less cost of goods sold | 51.7% | 55.8% | 61.0% | 60.1% | 54.2% | 55.1% |
| Gross profit | 48.3% | 44.2% | 39.0% | 39.9% | 45.8% | 44.9% |
| Other expenses | | | | | | |
| Sales and marketing | 13.7% | 19.0% | 10.3% | 10.7% | 12.2% | 12.1% |
| Other expenses | 18.5% | 15.6% | 10.3% | 12.1% | 7.1% | 7.9% |
| Total expenses | 32.3% | 34.6% | 20.6% | 22.8% | 19.3% | 20.0% |
| EBITDA | 16.1% | 9.6% | 18.4% | 17.1% | 26.5% | 24.9% |
| Net profit/(loss) | | | | | | |
| Less depreciation | (4.5%) | (5.6%) | (1.4%) | (2.7%) | (4.6%) | (4.2%) |
| Less interest expense | (5.3%) | (2.7%) | (2.7%) | (4.8%) | (5.1%) | (4.9%) |
| Other income | 0.7% | 0.4% | 2.1% | 2.3% | 1.9% | 1.9% |
| Profit before tax | 7.0% | 1.7% | 16.4% | 11.8% | 18.7% | 17.7% |

Consistent with last year we see domestic sales featuring highest and export sales featuring lowest for the \$0-1.5m tier at 58.1% and 12.2% respectively. This is expected as the domestic market is a safer game for the smaller operators due to the lower distribution costs, shorter cash cycles and no currency risks.

Similarly, we see export and bulk sales featuring highly in the larger tiers. With the domestic market in New Zealand ranging between \$500-600 million and wine exports exceeding \$1.7 billion there is no surprise the larger operators are tapping into this larger international market.

Other revenue includes grape sales, hospitality and 'other'. Combined, these occupy a greater portion of smaller winery tiers revenue than larger winery tiers. This diversification of revenue is unsurprising as smaller wineries may look to

diversify with shorter cash cycle revenue flows and supplement their overall wine sales. While the larger wineries generally run a model focussed almost solely on wine sales.

We normally expect to see cost of goods sold (as a proportion of sales) decrease with larger operators in reflection of economies of scale. This year we note the \$0-1.5m had the lowest cost of goods sold percentage which is a first for this survey however we note that 'other expenses' were significantly higher for this tier which might suggest variance in accounting treatment of expenses.

Interest expense as a percentage of sales has reduced across all tiers against last year reflective of the decreased levels of long term debt reported and the continued low interest rates currently on offer.

Balance sheet

Balance sheet 2018

The biggest movement we note in the 2018 survey is the increase of inventories for the first two tiers reflective of the particularly good 2018 harvest in Hawkes Bay and Central Otago.

We usually expect to see land investment of 30-40% in proportion to total assets for the \$0-1.5m and \$1.5-5m tiers. However we see a big drop in 2018 which is likely due to the larger amount of inventories held due to the good 2018 harvest in parts of the country.

Vineyard, biological assets, plant and equipment investment as a portion of assets, is generally shown to increase with size. Typically smaller scale wineries use more contract winemaking services than larger wineries. Similarly larger wineries have a greater exposure to contract growers. These two factors will have a material influence on fixed asset ratios across the tiers.

Other current assets and other non-current assets are unusually high in the \$5-10m category which may reflect non-core or non-wine related assets used for generating hospitality revenue or other revenue reported on the previous page.

Long-term debt levels appear to vary between tiers with the largest reporting an average of 34.3% of assets. The lowest average was reported by the \$5-10m tier at 19.8% and also had the joint lowest interest expense in relation to sales at 2.7%.

Equity levels have increased as a whole with all tiers reporting levels of equity above 50% in proportion to total assets.

Further analysis on debt as well as shareholder loans are included within the ratios section of this report.

| | \$0-1.5m | \$1.5-5m | \$5-10m | \$10-20m | \$20m+ | Total |
|-------------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Current assets | | | | | | |
| Cash | (1.4%) | 3.3% | 2.0% | (0.7%) | 1.5% | 1.3% |
| Receivables/Debtors | 10.1% | 9.1% | 11.5% | 8.5% | 8.0% | 8.2% |
| Inventories | 39.1% | 43.6% | 25.2% | 28.5% | 18.8% | 20.3% |
| Other current assets | 1.8% | 0.6% | 3.3% | 0.4% | 1.8% | 1.8% |
| Total current assets | 49.6% | 56.6% | 41.9% | 36.6% | 30.1% | 31.6% |
| Fixed assets | | | | | | |
| Land | 23.1% | 9.8% | 20.8% | 24.9% | 19.5% | 19.9% |
| Vineyards / biological assets | 10.8% | 14.7% | 21.0% | 11.6% | 16.0% | 16.0% |
| Plant and equipment | 13.2% | 18.0% | 4.5% | 22.0% | 33.0% | 30.2% |
| Total fixed assets | 47.1% | 42.5% | 46.2% | 58.6% | 68.5% | 66.0% |
| Other non-current assets | | | | | | |
| Other non-current assets | 3.3% | 0.8% | 11.8% | 4.8% | 1.4% | 2.3% |
| Total assets | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |
| Current liabilities | | | | | | |
| Other current liabilities | 6.1% | 6.8% | 4.8% | 4.1% | 4.6% | 4.6% |
| Trade payables and accruals | 1.9% | 4.9% | 2.5% | 0.9% | 2.7% | 2.6% |
| Total current liabilities | 8.0% | 11.8% | 7.3% | 5.1% | 7.3% | 7.2% |
| Term liabilities | | | | | | |
| Long term debt | 28.4% | 31.0% | 19.8% | 23.5% | 34.3% | 32.6% |
| Other non-current liabilities | 0.3% | 1.6% | 1.0% | 0.4% | 4.3% | 3.8% |
| Total liabilities | 36.7% | 44.3% | 28.1% | 28.9% | 45.9% | 43.5% |
| Equity | | | | | | |
| Shareholder loans | 87.0% | 34.7% | 3.7% | 21.8% | 1.7% | 4.0% |
| Share Capital | 20.8% | 51.4% | 7.6% | 15.2% | 22.6% | 21.4% |
| Retained earnings | (44.6%) | (30.5%) | 60.6% | 34.1% | 29.8% | 31.0% |
| Total equity | 63.3% | 55.7% | 71.9% | 71.1% | 54.1% | 56.5% |
| Total liabilities and equity | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

Ratios and returns

Ratios and returns

| | \$0-1.5m | \$1.5-5m | \$5-10m | \$10-20m | \$20m+ | Total |
|------------------------------------|----------|----------|---------|-----------|------------|-----------|
| Litres | | | | | | |
| Litres sold | 63,137 | 183,315 | 655,751 | 1,097,114 | 13,085,911 | 3,657,604 |
| Revenues and expenses per L | | | | | | |
| Revenue per L (labelled) | \$15.27 | \$15.93 | \$12.17 | \$11.73 | \$7.68 | \$8.19 |
| Revenue per L (bulk) | \$3.26 | \$4.42 | \$3.76 | \$3.72 | \$4.68 | \$4.60 |
| Revenue per L (total) | \$13.41 | \$14.20 | \$9.61 | \$10.72 | \$6.95 | \$7.33 |
| Gross margin per L | \$7.73 | \$7.05 | \$4.31 | \$4.65 | \$3.27 | \$3.43 |
| Profit / (loss) per L | \$1.11 | \$0.27 | \$1.81 | \$1.38 | \$1.33 | \$1.35 |
| Sales expenses per L | \$2.20 | \$3.03 | \$1.14 | \$1.25 | \$0.87 | \$0.92 |
| Other expenses per L | \$2.96 | \$2.49 | \$1.14 | \$1.41 | \$0.51 | \$0.60 |
| Solvency ratios | | | | | | |
| Current ratio | 6.2x | 4.8x | 5.7x | 7.2x | 4.1x | 4.4x |
| Debtors to sales ratio | 0.2x | 0.2x | 0.3x | 0.2x | 0.2x | 0.2x |
| Interest cover ratio | 2.2x | 1.5x | 6.3x | 3.0x | 4.3x | 4.2x |
| Efficiency ratios | | | | | | |
| Inventory turnover | 0.7x | 0.8x | 1.0x | 0.9x | 1.1x | 1.1x |
| Fixed asset turnover | 1.1x | 1.4x | 0.9x | 0.7x | 0.6x | 0.6x |
| Asset turnover | 0.5x | 0.6x | 0.4x | 0.4x | 0.4x | 0.4x |
| Profitability ratios | | | | | | |
| EBIT margin | 11.5% | 4.1% | 17.0% | 14.3% | 22.0% | 20.7% |
| EBIT to assets | 5.7% | 2.4% | 7.0% | 6.0% | 8.4% | 8.1% |
| EBT to equity | 5.5% | 1.8% | 9.4% | 6.9% | 13.3% | 12.3% |
| EBT to net wine sales | 8.3% | 1.9% | 18.9% | 12.8% | 19.2% | 18.4% |

Consistent with previous surveys, average litres sold are exponentially higher for the larger tiers. We notice this year that the litres sold for the \$10-20m category has almost halved however this appears just due to a mix of participants given that gross margin per litre is mostly in line with previous years' results for this category.

Revenue per litre for labelled wine continues to indicate that larger participants experience lower selling prices than smaller-sized participants. This will be due to a range of factors including how sales are made up in terms of varietal, sales channel, and export volumes in terms of bulk and packaged format.

The current ratios for all tiers have improved against last year reflective of the strong balance sheet positions this year. This

indicates a strong ability to pay debts as they fall due. A current ratio of 6.2x means that the \$0-1.5m category has \$6.20 of current assets to repay every \$1 of current liabilities. This does assume that inventory is 100% saleable and we did note the balance sheets showing the \$0-1.5m category with increased levels of inventory for 2018.

Inventory turnover is calculated as the cost of goods sold divided by the closing inventory figure on the balance sheet. An inventory turnover level of less than one shows increasing inventory levels. Wineries would be expected to have a turnover of less than one during periods of increased production or supply as wine stock is held over to drive sales growth for the future.

Distribution channels

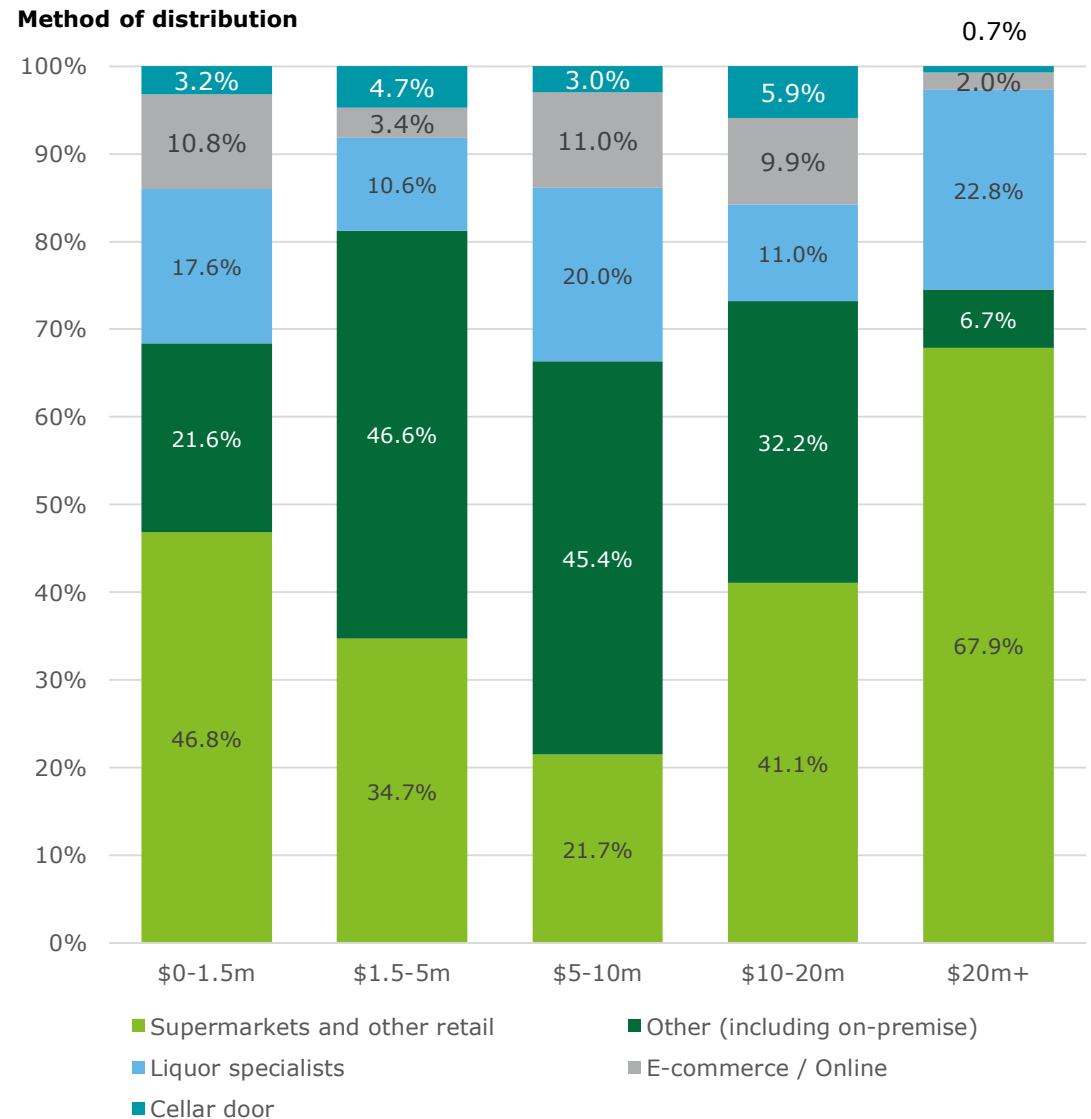
Online sales overtake cellar door sales for the first time

Conversations with wine businesses are often focused on the topic of distribution channels. It is the means by which product is sold as well as a key determinant of both profit margins and trade terms (with varying distributor margins, trade terms and customer markets).

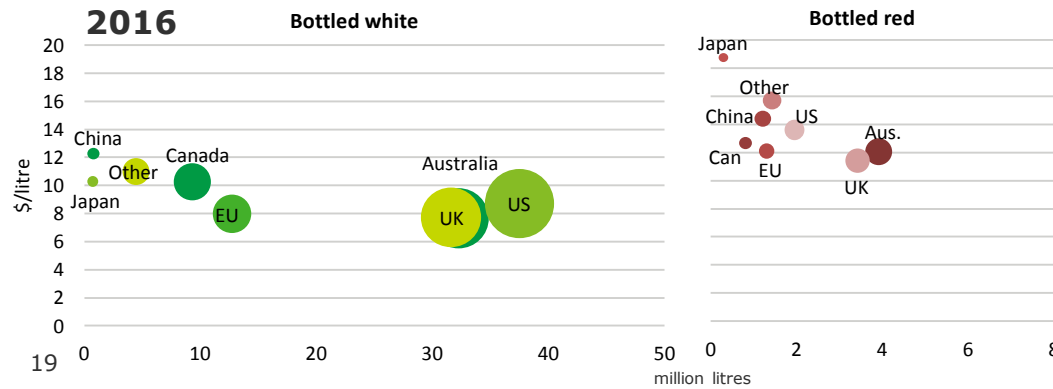
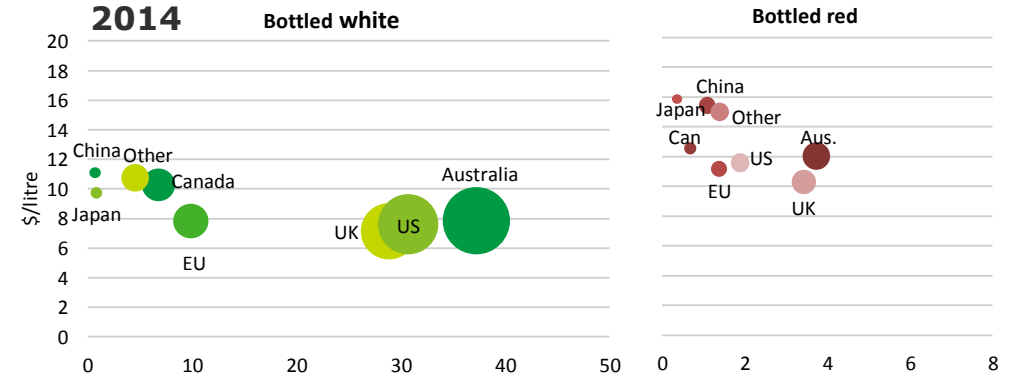
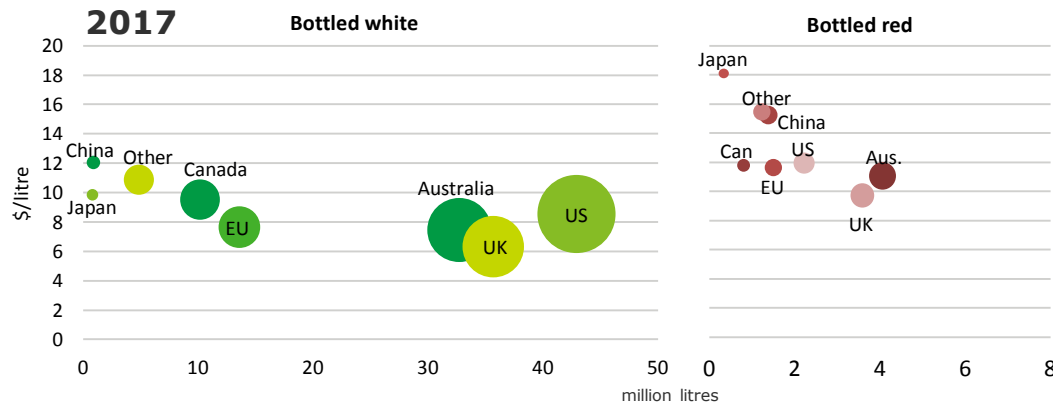
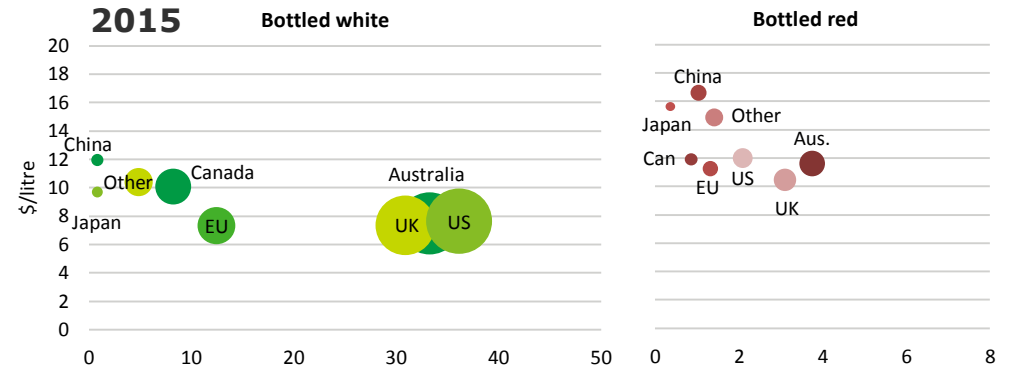
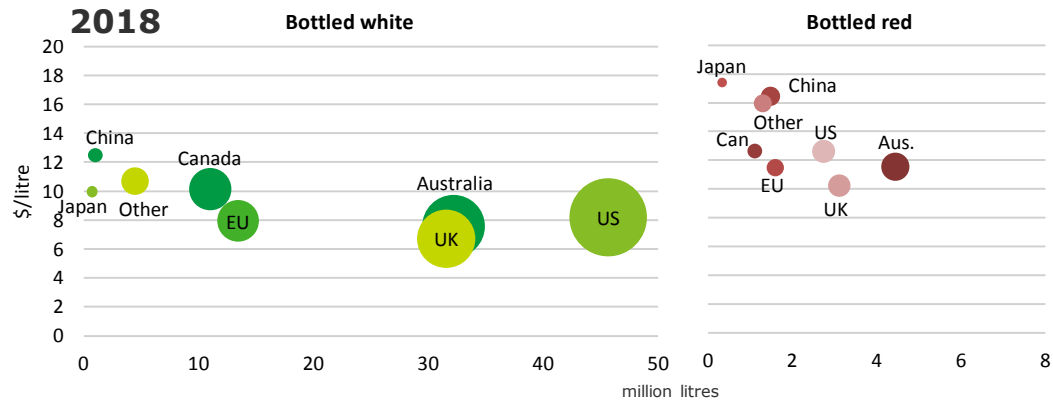
As expected supermarkets and other retail represent the majority of the \$20m+ category as this is the biggest market but it is interesting to see the largest proportion for the \$1.5-5m and \$5-10m to come through the 'other / on premise' channel reflective of the higher revenue per litre in these tiers.

We note for the first time that online sales have overtaken cellar door sales with the exception of the \$1.5-5m category reflecting the growth of digital as a legitimate sales channel.

It is also interesting to note that 100% of respondents in the \$0-\$1.5m and \$1.5-5m categories had at least some direct to consumer sales, either by cellar door or online. Overall across the survey, 86% of respondents made direct to consumer sales showing the importance of connecting directly with customers to build their brand.



New Zealand bottled wine export charts 2014-2018



Source: ANZ, Statistics NZ

Bubble size denotes total value of market where a bubble of this size indicates \$100m value

2018 Regional round-up

Key

-  Wineries
-  Numbers employed
-  Cellar Doors

Tasman/Nelson: 9,120 tonnes

 38  323  20


Marlborough: 313,038 tonnes

 141  2550  36

Canterbury/Waipara: 11,157 tonnes

 67  430  16

Otago: 11,358 tonnes

 136  820  34

Northland: 113 tonnes

 17  105  17

Auckland: 787 tonnes

 102  1520  48

Waikato/BOP:

 10  142  5




Gisborne: 13,000 tonnes

 17  260  8

Hawkes Bay: 41,061 tonnes

 91  940  33

Wairarapa: 4,592 tonnes

 69  280  30

Source: Deloitte, New Zealand Wine, Statistics NZ







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