

Marlborough Wine Estates

Food and beverages
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Key operating milestone to be missed

Marlborough Wine Estates Group (MWE), which was formed in March 2015 to acquire vineyard assets comprising the Otuwhero Estate from Min (James) Jia, is targeting the development of premium New Zealand white wine brands in China. MWE has notified the market that it expects to fall short of its key operating milestone (KOM) target for international bottled wine sales revenue by more than 10% for the year ended 30 June 2017.

Key customer to fall short of commitment

The company has been advised that a key customer, Great Esprit Limited (GEL), is unlikely to be able to meet its minimum annual commitment to purchase bottled wine for the year ended 30 June 2017 under its wine supply agreement with MWE's subsidiary Otuwhero Trustee Limited. Great Esprit is a distributor based in Hong Kong. The commitment was for NZ\$3m of bottled wine and MWE has been advised that the expected performance against this commitment is likely to be \$1.3m. MWE has not stated the reason for the shortfall.

KOM target for international wine sales to be missed

MWE advises that this development will adversely affect the company's KOM target for international bottled wine sales revenue by more than 10%. The target was NZ\$3.2m.

Implications of the miss

MWE is currently working through the implications of GEL not meeting its minimum annual order requirements. As part of this review process, the board is seeking further information and will announce the revised KOM target for international bottled wine sales revenue to the market in its business update, due for release by 3 May 2017. MWE has not stated that other KOMs will be affected.

We will write a further report once the KOMs have been restated.

Valuation: Above peers

MWE trades on an 11.5x FY16 EV/revenue multiple. We noted in March 2017 that this was considerably higher than its two listed peers in the NZ and Australian markets, which were trading at an average FY16 EV/revenue multiple of 2.3x.

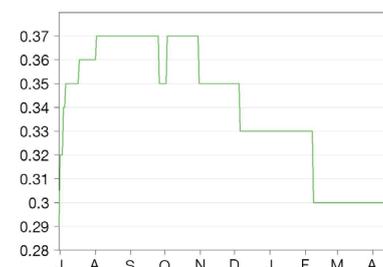
Historical performance

Year end	Revenue (NZ\$000)	NPAT*** (NZ\$000)	EPS (c)	DPS (c)	P/E (x)	Yield (%)
06/15 PF*	2,788	170	0.1	0.0	N/A	N/A
06/15**	1,840	590	0.2	0.0	N/A	N/A
06/16	7,424	(494)	(0.2)	0.0	N/A	N/A

Source: Marlborough Wine Estates. Note: *Pro forma for 12 months; revenue includes sales revenue and other revenue. **Actual from 18 March 2015 to 30 June 2015. *** FY15 NPAT includes positive fair value adjustment of NZ\$1.054m, according to management, and FY16 NPAT excludes one-off capital raising costs.

Price NZ\$0.30
Market cap NZ\$88m

Share price performance



Share details

Code MWE
 Listing NXT
 Shares in issue 293.3m

Business description

Marlborough Wine Estates Group (MWE) owns and operates six vineyard blocks located in the Awatere Valley in the Marlborough wine district of the South Island of New Zealand. It sells bottled wine to China, NZ and other markets, as well as bulk wine and grapes to wine producers in NZ.

Bull

- Marlborough white wines, particularly sauvignon blanc, have a global reputation for quality.
- Option to improve earnings by converting more of the grape harvest into bottled wine for local and export sales.
- Improvements in vineyard management, particularly in securing water supply, could improve grape yields.

Bear

- Maintenance of premium pricing is dependent on quality of the product.
- The majority of distribution in Asia is being made by related parties, albeit that the related party is purchasing bottled wine at a premium of 30% to the average NZ export price for white wine.
- Greater demand for MWE's products may depend on conversion of Asian markets from red wines to premium white wines.

Analysts

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Marlborough Wine Estates coverage is provided through the NXT Research Scheme

Expected miss on distributor's purchase commitment

When we reported on the interim results in March 2017, we noted that first-half sales of international bottled wine, at NZ\$0.8m, were low compared with the full year target of NZ\$3.2m. However, we also noted that the FY17 target, which was double FY16 actual sales, was underpinned by minimum purchase requirements that form part of the distribution arrangements with Great Esprit. Management expected that a large proportion of sales would fall into the second half of the financial year.

Management stated in its Q2 business update in January that it was unlikely that the KOM target would not be met, particularly considering the distributor had contractually agreed to order a minimum of NZ\$3m of wine in the current financial year.

The company has now learnt that it is unlikely Great Esprit will be able to meet its NZ\$3m minimum annual commitment to purchase bottled wine for FY17. The expected performance for the year is likely to be \$1.3m.

Against the KOM target of NZ\$3.2m for international bottled wine sales revenue, it therefore seems inevitable that the target will be missed by more than 10%.

About Great Esprit

As we wrote in our [initiation in June 2016](#), Great Esprit (GEL) is a Hong-Kong based entity owned by an associate of MWE's executive chairman, Min (James) Jia. It is therefore considered to be a related party. The non-exclusive distribution agreement covers Hong Kong, China and other yet to be exploited markets in Asia. Material changes to the terms of the distribution agreement may require shareholder approval under the NXT listing rules. MWE has not disclosed the reason why GEL now believes it is unable to meet its purchase commitment for FY17.

Implications of the change

MWE is currently working through the implications of GEL not meeting its minimum annual order requirements. As part of this review process the board is seeking further information and will announce the revised KOM target for international bottled wine sales revenue to the market in its business update due for release by 3 May 2017.

MWE has not stated that other KOMs will be affected. These are stated below.

Exhibit 1: Actual results and KOM targets			
	FY16 actual	HY17 actual	FY17 KOM
Gross harvest (tonnes)	1,653	0	1,544
Bulk grape sales (tonnes)	1,187	0	1,144
International bottled wine sales (NZ\$)	1,604,500	822,079	TBA
NZ bottled wine sales (NZ\$)	150,400	89,197	205,940
Source: MWE			

We will issue a further report once the KOMs have been updated.

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