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Optimism paired with results

Winery Benchmarking 2016

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Contents

Welcome

It is with great pleasure to present the 2016 results of our annual benchmarking survey, in conjunction with New Zealand Winegrowers. After 10 years of producing this report, we undertook a comprehensive review of the survey process and report contents, with a specific focus on making it as easy as possible for wineries to participate and benefit in the value of benchmarking their businesses. It is with this in mind that we thank all of those who provided the valuable feedback that allowed us to ensure that the most important content and measures remained part of the survey.

It is very pleasing to see another year with all categories reporting positive average net profit results, and generally healthy financial ratios, which also aligned with the large 2016 harvest. Optimism in the export market opportunities has also featured strongly in the results.

Finally, we express our sincere thanks to those who provided data. We hope that you found this year's exercise immensely easier to participate in, with the changes we've made.

We hope that you enjoy this new simplified version of the report and we look forward to our continued work with the industry in the years to come.

Peter Felstead

Sponsoring Partner - Deloitte

Welcome to the 2016 Winery Annual Benchmarking Survey conducted in conjunction with Deloitte.

One of the core functions of New Zealand Winegrowers is the production of information that assists informed decision making in and about the industry.

This survey is part of a suite of reports, including the Viticulture Monitoring Reports, which New Zealand Winegrowers is proud to be associated with. Together these reports provide an overview of the financial performance of our industry. As such the reports are important tools in terms of individual and industry benchmarking, risk assessment and forward planning.

This 2016 survey would not be possible without the participation of the wineries who have supplied the data. Thank you to those wineries for the time and commitment they have invested in this project. We trust you have found your participation worthwhile.

New Zealand Winegrowers greatly values our partnership with Deloitte which enables this report to be produced. This partnership has endured for 10 years – we look forward to it continuing for many more.

Philip Gregan

CEO – New Zealand Winegrowers

Results
Executive Summary

- Pleasingly, all size categories reported an average positive net profit before tax result for 2016, ranging from 4.7% for the $1.5-5m category and 21.8% for the $20m+ category.
- The highest proportion of bulk wine revenue reported was 20% by the $5-10m category. A high proportion of other operating revenue (28.3%) was also reported by the $0-1.5m category which may likely include grape sales or other non-wine revenue such as restaurant or contract winemaking.
- Selling and marketing costs ranged between 9% and 14.5% for the $10-20m and $20+ categories respectively. Other overheads reflected the economies of scale of larger wineries at 4.6% of revenue and 16.3% for the smallest category.
- Average proportions of assets funded by equity, increased in variation this year with the $1.5-5m category reporting 75.1% and the $0-1.5m category reporting 34.6%. Those entities with the highest levels of long term debt also reported the lowest equity ratios. In terms of working capital, the average debtor positions appeared largely consistent with previous surveys, with the balances making up between 5.4% and 11.5% of assets.
- Creditor positions had a much lower variation between categories. A general trend that can be observed, shows that average inventory levels decrease as winery size increases – potentially indicative of larger players having more established and efficient distribution channels in place, or differing maturation periods on the primary varietals of each category.
- Grape yields per hectare that were reported by participants showed an almost linear correlation between yields and winery size, with the $0-1.5m category showing an average of approximately 4 tonnes per hectare and the $20m+ reporting over 16. These yield levels also provide an indication as to the primary regions and varietals of each of the categories.
- Per litre ratios including revenue and overheads decreased with winery size which is indicative of both the price points and economies of scale achieved at the various levels of scale across categories. Financial lending ratios such as current ratio and interest cover, both also appeared to exceed the usual minimum levels of 1 and 2–3 times respectively.
- Distribution channel rankings were also reported between 'cellar door', 'mail order', 'website' and 'other'. Results were relatively even except for the $1.5-5m category reporting the highest ranking of the 'cellar door' channel and the $20m+ reporting the highest 'other'.
- The top industry issues & challenges identified by participants included 'sales margin pressure' within the top three amongst all categories, with other export themed items featuring highly. Interestingly, 'increasing sales margins' also featured in the top three industry opportunities and advantages by all but the $5-10m category. Sales volume growth from existing markets and existing products also featured strongly.

Results
Profitability

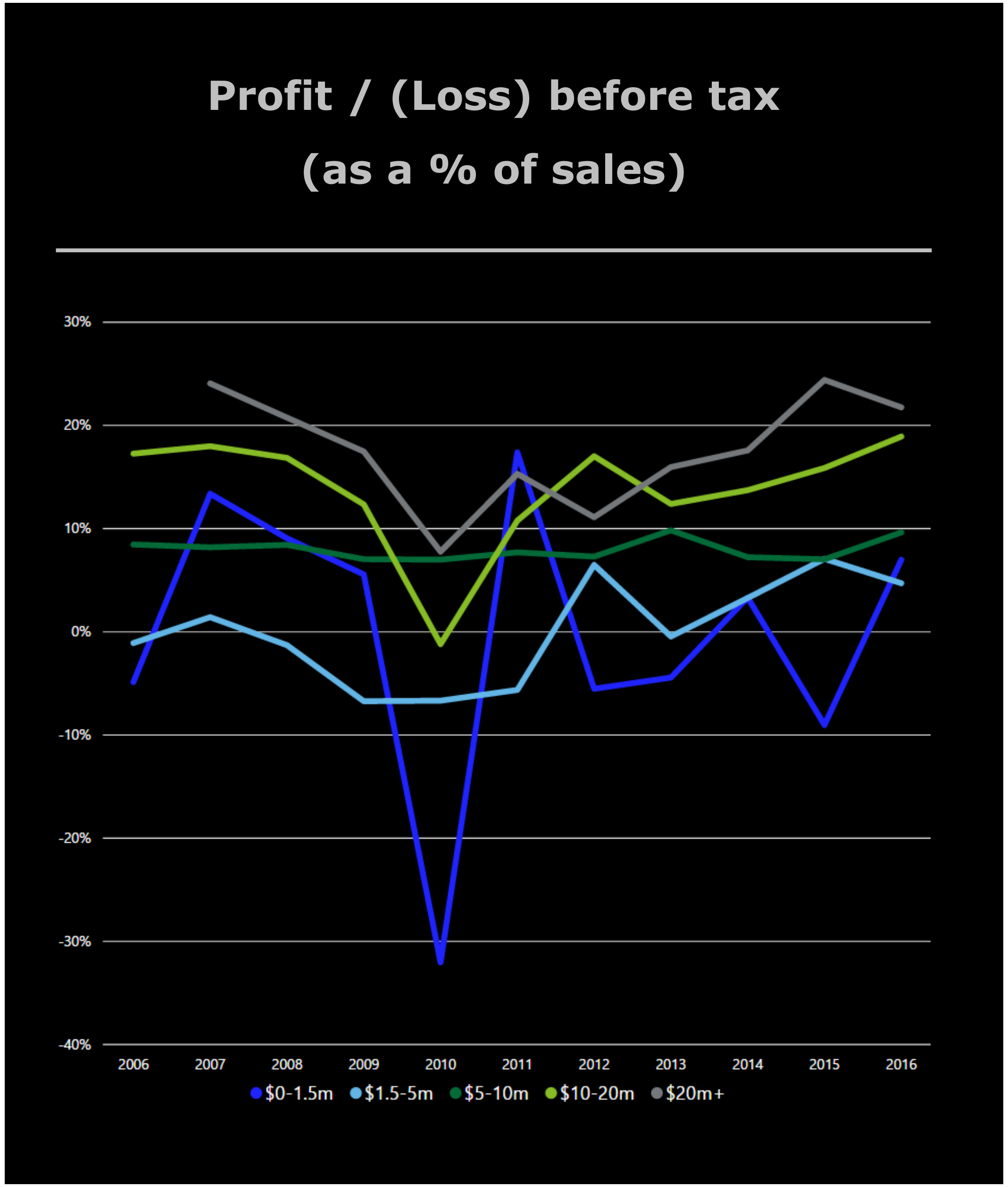
Income Statement 2016

	$0-1.5m	$1.5-5m	$5-10m	$10-20m	$20m+
Revenue and Gross Margin					
Domestic wine sales	44.9%	23.8%	21.8%	34.7%	17.5%
Export sales (own label)	18.8%	54.2%	44.0%	44.5%	64.0%
Export sales (buyers label)	6.6%	3.1%	0.4%	3.9%	3.6%
Bulk Wine Sales	1.4%	2.5%	20.0%	6.9%	13.8%
Total Wine Sales	**71.7%**	**83.6%**	**86.2%**	**90.0%**	**98.9%**
Other operating revenue	28.3%	16.4%	13.8%	10.0%	1.1%
Total revenue	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**
Less cost of goods sold	59.8%	69.6%	60.9%	57.8%	51.5%
Gross margin	**40.2%**	**30.4%**	**39.1%**	**42.2%**	**48.5%**
Expenses					
Sales and marketing	11.7%	10.1%	9.3%	9.0%	14.5%
Other expenses	16.3%	10.7%	15.5%	9.6%	4.6%
Total expenses	**28.0%**	**20.8%**	**24.8%**	**18.6%**	**19.1%**
Net profit/(loss)					
EBITDA	**12.2%**	**9.6%**	**14.3%**	**23.6%**	**29.4%**
Less depreciation	(4.2%)	(5.3%)	(3.8%)	(3.0%)	(4.9%)
Less interest expense	(2.8%)	(0.5%)	(2.6%)	(3.4%)	(5.4%)
Other income	1.8%	0.9%	1.8%	1.7%	2.7%
Profit/(loss) before tax	**7.0%**	**4.7%**	**9.7%**	**18.9%**	**21.8%**

- It is pleasing to report all categories of participants showed an average positive net profit result for 2016. This has only occurred twice since commencing the survey in 2006 (2014 and 2016), the occurrences of which also correspond with large national harvest volumes of 445,000 and 436,000 tonnes of grapes.
- The lowest average net profit/(loss) before tax reported was by the $1.5-5m category at 4.7% and the highest at 21.8% for the $20m+ category.
- The $1.5-5m category also had the highest cost of goods sold at 69.6% while the $20m+ category experienced the lowest at 51.5%, the effect of which has flowed through to their gross margins and bottom lines.
- The revenue mix between labelled and bulk wine only varied slightly across all categories. Also noted is the higher proportion of other operating revenue reported by the $0-1.5m category of 28.3% and the bulk wine sales of 20% reported by the $5-10m category. The $20m+ category also reported 13.8% of it's revenue as being bulk wine sales.
- The relatively high level of other operating revenue reported by the $0-1.5m category at 28.3% was particularly interesting. This would most likely consist of grape sales, however could also include other non-wine revenue items such as contract wine making and restaurant or accommodation revenue.

Results
Profitability

- Selling and marketing costs varied slightly between categories however largely in line with the results of previous surveys. The $20m+ category reported the highest ratio of these costs at 14.5% of revenue and the $10-20m category the lowest ratio at 9%.
- Other expenses (overheads) did vary as usual between all categories given the economies of scale achieved by larger wineries, with the largest category reporting these costs at 4.6% of revenue and the smallest category reporting quite a different level at 16.3%.
- Depreciation expense ratios were reported as the highest by the $1.5-5m and $20m+ categories at 5.3% and 4.9% respectively, which also aligns with their proportions of fixed assets in their balance sheet (discussed later).
- Interest expense also approximately aligned with each categories level of long term debt, except for the smallest category which may be due to either the reduction of debt closer to year end or non-interest bearing shareholder loans included in this line item.
- As with any survey the results reported do depend on the participants in any one year. However it is interesting to note the trend shown on the adjacent graph, which appears as a 'narrowing' of the bottom line results between larger and smaller wineries towards profit results of between 10-20% before tax.



Balance Sheet 2016

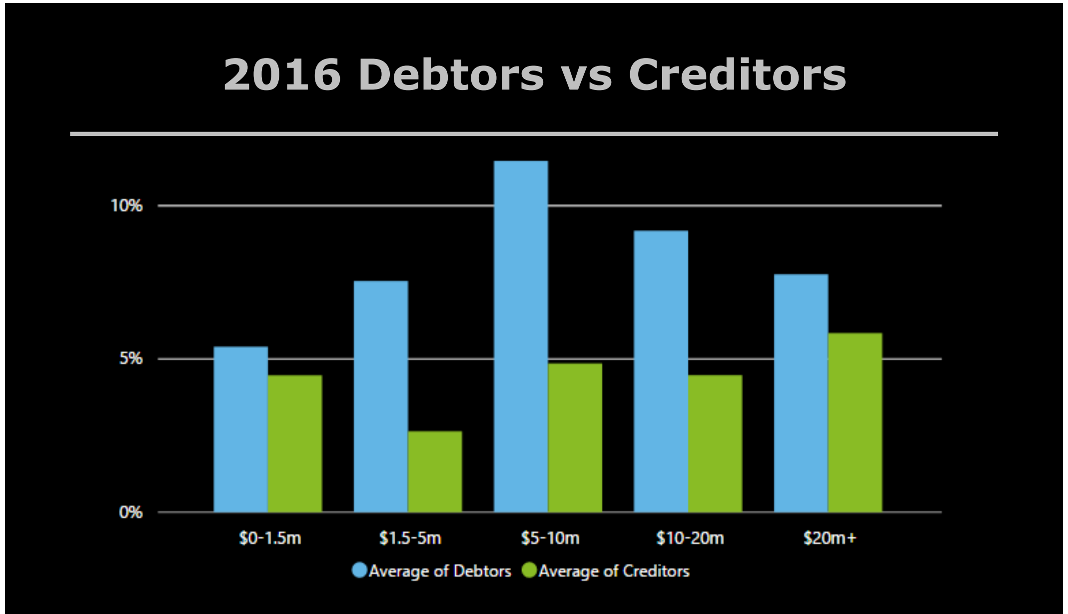
	$0-1.5m	$1.5-5m	$5-10m	$10-20m	$20m+
Assets					
Current assets					
Cash	5.2%	3.8%	2.8%	3.1%	0.8%
Receivables/Debtors	5.4%	7.5%	11.5%	9.2%	7.8%
Inventories	29.1%	23.6%	29.8%	20.9%	20.4%
Other current assets	1.2%	0.8%	4.7%	0.9%	2.1%
Total current assets	**40.9%**	**35.7%**	**48.8%**	**34.1%**	**31.1%**
Fixed assets					
Land and vineyards	41.8%	45.7%	19.4%	35.9%	33.9%
Plant and equipment	16.0%	18.5%	6.1%	19.9%	33.2%
Total fixed assets	**57.8%**	**64.2%**	**25.5%**	**55.8%**	**67.1%**
Other non-current assets	1.3%	0.1%	25.7%	10.1%	1.8%
Total assets	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**
Liabilities					
Current liabilities					
Trade payables and accruals	4.5%	2.6%	4.9%	4.5%	5.8%
Other current liabilities	2.8%	6.4%	17.5%	2.7%	2.0%
Total current liabilities	**7.3%**	**9.0%**	**22.4%**	**7.2%**	**7.8%**
Term Liabilities					
Long term debt	43.1%	0.9%	13.4%	25.0%	37.8%
Other non-current liabilities	15.0%	15.0%	2.7%	3.9%	5.2%
Total liabilities	**65.4%**	**24.9%**	**38.5%**	**36.1%**	**50.8%**
Equity					
Share capital	59.6%	38.8%	30.0%	8.4%	27.4%
Retained profits & reserves	(25.0%)	36.3%	31.5%	55.5%	21.8%
Total Equity	**34.6%**	**75.1%**	**61.5%**	**63.9%**	**49.2%**
Total liabilities and equity	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

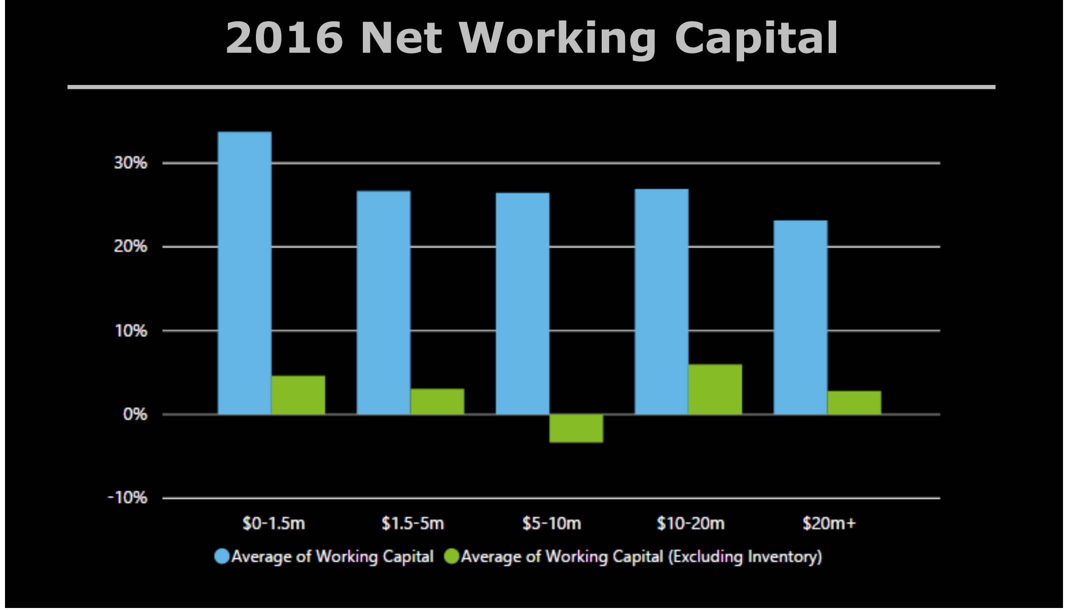
Results
Financial Position

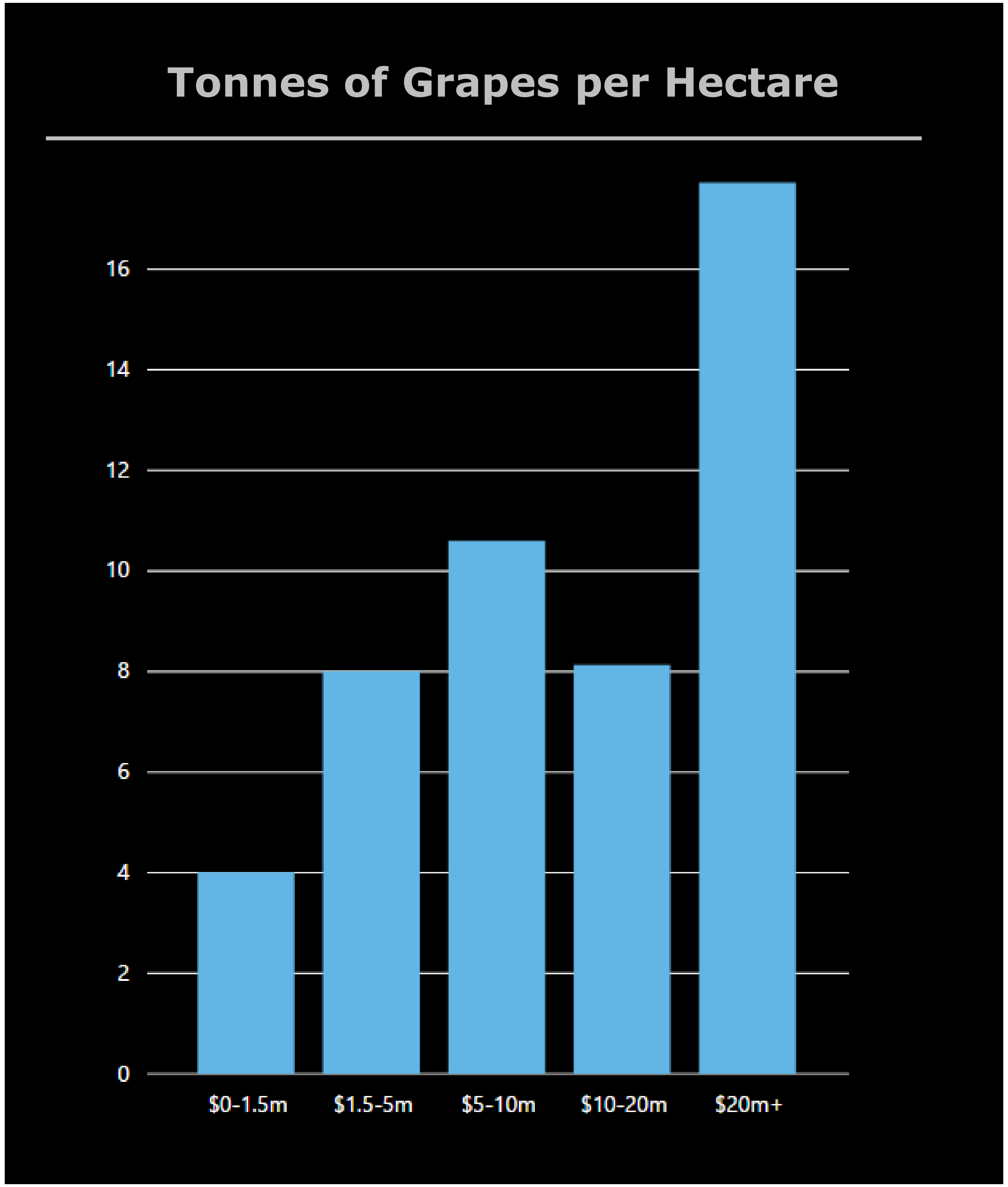
- While there are some variations, this year's balance sheet results show no dramatic differences from recent surveys of cash, trade debtors or creditor positions among the different categories.
- The average proportions of equity to total assets reported, have increased in variation between categories this year, with the $1.5-5m category reporting 75.1% of assets being funded by equity and the $0-1.5m category only showing 34.6% for the same ratio.
- The categories with the highest long term debt levels (and lowest equity ratios) include the $0-1.5m category, reporting 43.1% of assets funded by debt and the $20m+ category showed 37.8%. It should also be noted that long term debt for some smaller wineries may include shareholder loans, which could be regarded as similar to equity.
- As discussed in the profitability section, the proportions of fixed assets and debt between categories also correspond with the proportions of depreciation and interest expenses, with the exception of the smallest category.
- Interestingly, the $5-10m category also reported an unusually high level of other non-current assets, as well as other current liabilities which were concentrated to a few participants, who may also hold non-core or non-wine related assets and liabilities.

Results
Financial Position

- As shown in the adjacent graph and consistent with the results of previous surveys, debtors positions appear to range between that shown by the $5-10m category (11.5%) and the $0-1.5m category (5.4%).
- The range of average creditor balances appear relatively low when compared to prior years where the range extended from 4% to 12%. This year however, we see the range extend from 2.6% in the $1.5-5m category to 5.8% for the $20m+ category, which could indicate more efficient debtor collections.
- As usual and unsurprisingly, the net working capital graph adjacent shows a large proportion of the working capital of wineries consisting of inventory.
- There is a general trend that can be seen where the proportion of assets in inventory reduces as winery size increases, which may be a result of the more established and efficient market distribution channels of the larger wineries. Differing maturation periods may also influence these results depending on the primary varietals of each category.
- A negative net working capital excluding inventory was also noted in the $5-10m category due to higher current liabilities.







Results
Vineyards

- This is the first time we have reported on the average grape yields in our survey results and we believe they provide an important context to the results in other sections of this report.
- A result that is quite obvious in the adjacent graph is the yields experienced by the largest category wineries and how they compare to those of the smaller categories.
- As a comparison, below are the regional yields for New Zealand's main varietals from the 2016 Viticulture Gross Margin Benchmarking Report, published by the Ministry for Primary Industries and New Zealand Winegrowers:

Region	Sauv. Blanc	Pinot Noir	Chardonnay	Merlot
Marlborough	15.9	8.5	-	-
Hawkes Bay	14.2	-	8.7	9.4
Gisborne	-	-	12.7	
Wairarapa	-	5.4	-	-

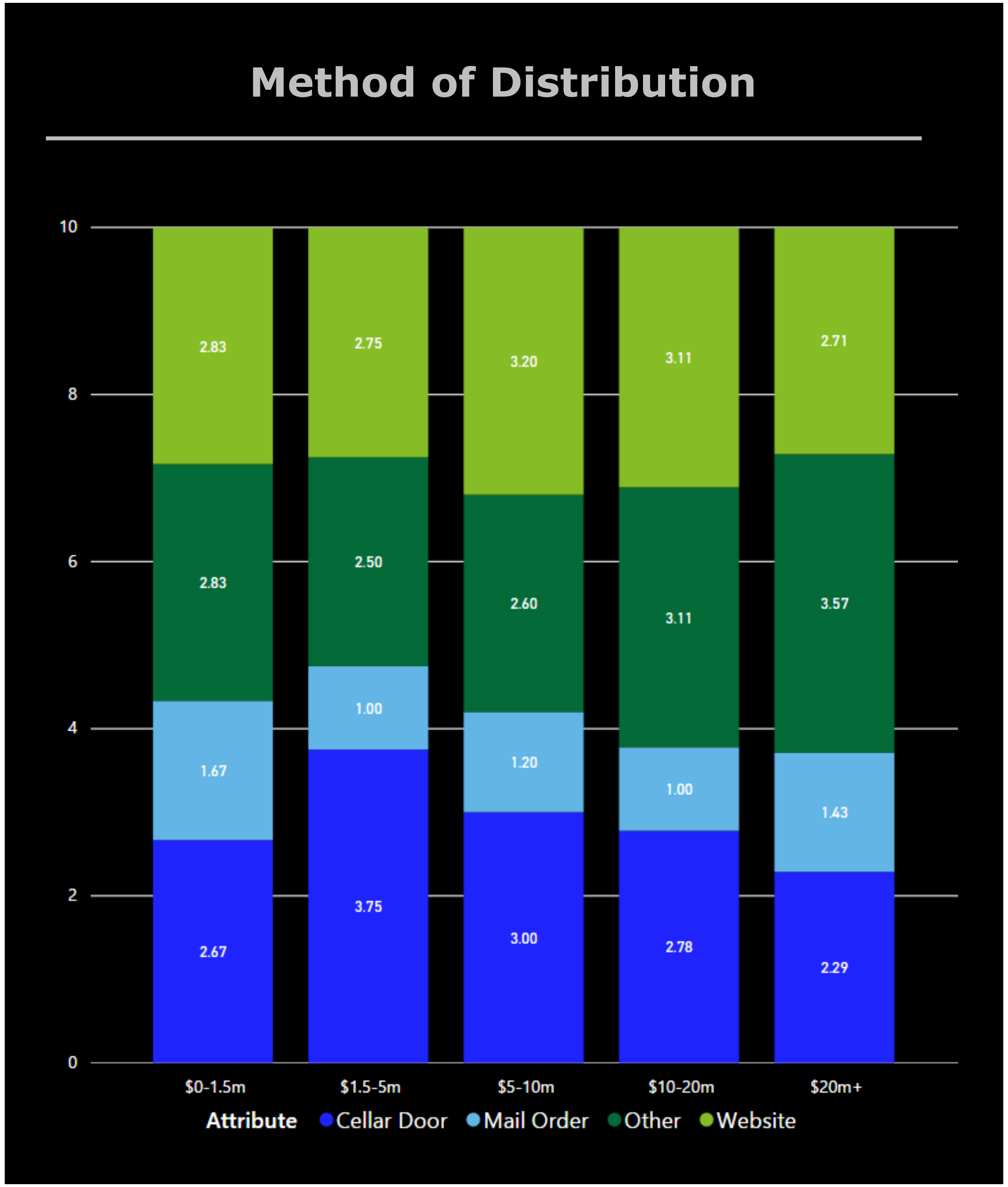
- Comparing the above yields with those reported by the survey participants, there is the obvious conclusion that the wineries in the $20m+ category are likely to typically operate in regions with larger yields and total production. Conversely, the smaller categories of wineries tend to either operate in regions or varietals with lower yields, or deliberately limit yields to support a more selective harvest volume.

Results
Ratios

- This is the first year the survey has focussed on litres instead of cases, which has allowed a more direct comparison of volumes across various winery revenue lines including labelled product and bulk wine.
- Somewhat unsurprisingly, almost all of the reported revenue, margin and overheads per litre, appear to decrease with the increased winery size, with the lower costs per litre depicting the economies of scale that can be achieved in the industry.
- The highest labelled wine revenue per litre was reported by the smallest category at $15.23 and the lowest by the largest at $6.44. Arbitrarily, at a 750ml bottle size, this would translate to approximate price point ranges of $8-$20 per bottle or $103-$244 per case (based on 12 bottles).
- It is pleasing to see the current ratios reported above 200% for all categories, indicating that all categories on average have at least $2 of current assets for every $1 of current liabilities. This does however assume 100% saleable inventory.
- Common lending requirements include businesses having more equity than debt as well as a 200–300% interest cover ratio, which pleasingly all categories met.

Financial Ratios

	$0-1.5m	$1.5-5m	$5-10m	$10-20m	$20m+
Litres Sold	42,188	252,355	812,491	1,412,698	16,809,728
Revenues and expenses per case					
Revenue per L (labelled)	$15.23	$11.46	$14.85	$10.05	$6.44
Revenue per L (bulk)	$5.57	$3.71	$3.34	$3.60	$5.12
Gross margin per L	$8.27	$3.92	$3.74	$4.15	$3.04
Profit / (loss) per L	$1.43	$0.61	$0.92	$1.86	$1.37
Sales expenses per L	$2.41	$1.30	$0.90	$0.88	$0.91
Other expenses per L	$3.35	$1.38	$1.48	$0.95	$0.29
Solvency ratios					
Current ratio	567.3%	395.0%	218.4%	473.8%	394.0%
Debtors to sales ratio	11.5%	25.0%	20.4%	21.9%	18.7%
Interest cover ratio	285.8%	849.0%	396.7%	602.8%	453.9%
Efficiency ratios					
Inventory turnover	96.4%	89.0%	114.8%	115.4%	105.3%
Fixed asset turnover	81.2%	47.1%	219.9%	75.0%	62.0%
Asset turnover	46.9%	30.2%	56.2%	41.9%	41.6%
Profitability ratios					
EBIT margin	8.0%	4.3%	10.4%	20.7%	24.4%
EBIT to assets	3.8%	1.3%	5.9%	8.6%	10.2%
EBT to equity	9.5%	1.9%	8.8%	12.4%	18.4%
EBT to net wine sales	9.7%	5.6%	11.2%	21.0%	22.0%



Results
Distribution

- For this year's survey, we included the method (or channel) of distribution as a ranking, with participants selecting between 1 and 4, with 1 for the method making up the highest amount of sales, and 4 the least.
- To arrive at the proportions displayed in the graph adjacent, the rankings were inverted to 'scores' with 1 converting to 4 and 4 converting to 1 and so on. The scores were then averaged with each method's score divided over the total to arrive at an average score for each category.
- Whilst the total scores (rankings) for 'cellar door', 'website' and 'other' are largely even in total, there are some key differences to note between each category.
- The $20m+ category ranked the highest in the 'other' category and also the lowest for 'cellar door'. The $1.5-5m category also ranked 'cellar door' quite highly.
- The smallest category also ranked the highest proportion of 'mail order' sales.

Results
Issues & Challenges

- With 2016 being our 11^{th} year conducting the survey and after receiving highly valued feedback on the exercise, we have made some amendments to the issues and challenges included in our survey, for ranking by participants.
- While some issues have only been slightly updated, additions include succession, terms of trade (cash cycle) and sales margin pressure.
- As can be seen from the adjacent table, sales margin pressure is clearly a highly ranked issue among all categories of wineries.
- This is followed by distribution (including marketing) and exchange rates which the $1.5-5m, $5-10m and $10-20m categories ranked most highly.
- Marketing product overseas (as it was previously included) has always ranked highly for participants in recent years, with the exception of the largest category who likely have more well established distribution channels offshore.
- Other highly ranked issues included government compliance costs, terms of trade, grape supply and affordability of land.

Top Issues and Challenges

$0-1.5m

1. Sales margin pressure
2. Labour supply/Cost
3. Government and other compliance costs

$1.5-5m

1. Exchange rates
2. Sales margin pressure
3. Distribution including marketing product overseas

$5-10m

1. Distribution including marketing product overseas
2. Sales margin pressure
3. Terms of trade (cash cycle)

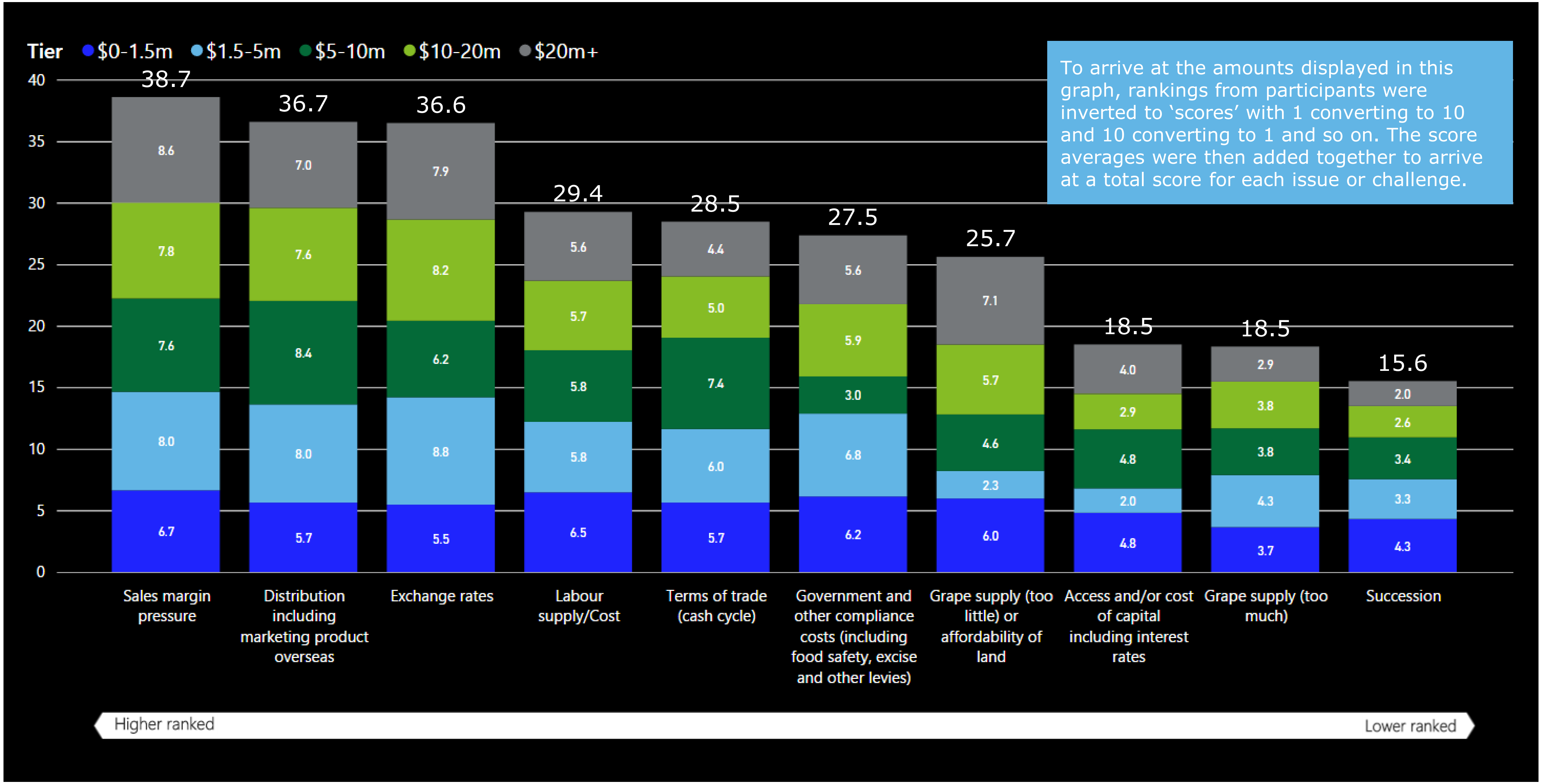
$10-20m

1. Exchange rates
2. Sales margin pressure
3. Distribution including marketing product overseas

$20m+

1. Sales margin pressure
2. Exchange rates
3. Grape supply (too little) or affordability of land

Issues & Challenges



Top Opportunities and Advantages

$0-1.5m

1. Increasing sales margins
2. Sales volume growth from existing markets & existing products
3. Sales volume growth from new markets & existing products

$1.5-5m

1. Increasing sales margins
2. Sales volume growth from existing markets & existing products
3. Production efficiencies

$5-10m

1. Sales volume growth from existing markets & existing products
2. Sales volume growth from new markets & existing products
3. Sales volume growth from existing markets & new products

$10-20m

1. Sales volume growth from new markets & existing products
2. Sales volume growth from existing markets & existing products
3. Increasing sales margins

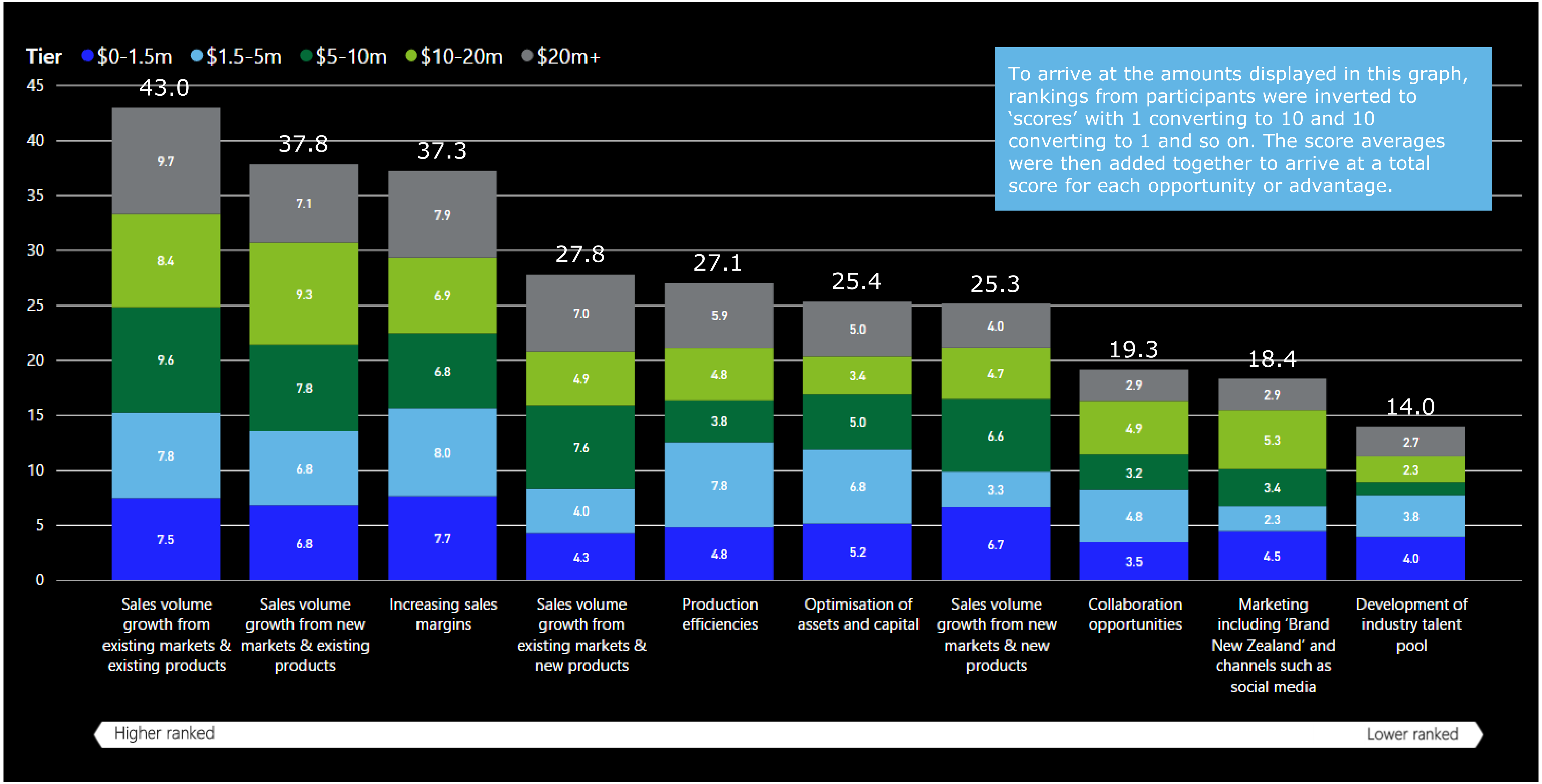
$20m+

1. Sales volume growth from existing markets & existing products
2. Increasing sales margins
3. Sales volume growth from new markets & existing products

Results
Opportunities & Advantages

- On a more positive note this year, we are pleased to have provided the means this year to also capture the opportunities and advantages participants see for the industry.
- Many of the items available for participants to rank focus on opportunities for sales volume growth, which have made up our top two. These are: sales volume growth from existing markets & existing products and sales volume growth from new markets & existing products.
- Growth from existing markets and products was the highest ranked opportunity for the $5-10m and $20m+ categories.
- Also ranking highly in third place were increasing sales margins which ranked highest on average for both the $0-1.5m and $1.5-5m categories.
- Interestingly, increasing sales margins ranked in the top three for all categories (except the $5-10m category) alongside the issue of sales margin pressure, which was also ranked a top three issue by all categories among their issues and challenges.
- Other items that ranked highly included sales volume from new markets as well as production efficiencies.

Opportunities & Advantages



About

2016 Benchmarking Results

Deloitte has conducted this annual financial benchmarking survey in conjunction with New Zealand Winegrowers. The survey was conducted between September 2016 and January 2017 and is based upon the 2016 financial statements. The survey is designed to assist wine growers to make more informed decisions about their relative strengths and weaknesses compared with others in the industry. The study also hopes to provide wineries with an insight into the relative efficiency and financial performance of their business – information that is vital for those looking to attract capital, expand and sustain growth. Survey questionnaires were sent to all members of New Zealand Winegrowers. Comments made in this report are based on the responses of 31 survey participants, which account for approximately 43% of the New Zealand wine industry by litres of wine produced and 37% by export sales revenue generated for the 2016 year. Respondents either own or lease 19% of the 36,192 producing hectares currently under vine in New Zealand. To assist the comparison of different sized wineries, respondents have been categorised 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.

About Deloitte

Deloitte provides audit, tax, consulting, and financial advisory services to public and private clients spanning multiple industries. With a globally connected network of member firms in more than 150 countries, Deloitte brings world-class capabilities and high-quality service to clients, delivering the insights they need to address their most complex business challenges. Deloitte has in the region of 200,000 professionals, all committed to becoming the standard of excellence.

Deloitte New Zealand brings together more than 1,000 specialists providing audit, tax, technology and systems, strategy and performance improvement, risk management, corporate finance, business recovery, forensic and accounting services. Our people are based in Auckland, Hamilton, Rotorua, Wellington, Christchurch and Dunedin, serving clients that range from New Zealand's largest companies and public sector organisations to smaller businesses with ambition to grow. For more information about Deloitte in New Zealand, look to our website **www.deloitte.co.nz** and our dedicated wine industry webpage **www.deloitte.com/nz/wine**.

About New Zealand Winegrowers

New Zealand Winegrowers is the national organisation for New Zealand’s grape and wine sector. The organisation currently has approximately 800 grower members and 700 winery members and aims to represent, promote and research the national and international interests of the New Zealand wine industry.

New Zealand Winegrowers conducts a wide range of tasks on behalf of the grape and wine sector including: advocacy at regional local and international levels; providing a global marketing platform for New Zealand wine; facilitating world-class research on industry priorities; giving the industry timely and strategic information; and organising sector wide events such as the Bragato Conference and Awards and the Air New Zealand Wine Awards.

New Zealand Winegrowers was established in March 2002 as a joint initiative of the New Zealand Grape Growers Council, representing the interests of New Zealand’s independent grapegrowers, and the Wine Institute of New Zealand, representing New Zealand wineries.

New Zealand Winegrowers is governed by a Board of Directors of 12, comprising 7 representatives from the Institute and 5 representatives from the Council. New Zealand Winegrowers is funded through levies collected by the Council and the Institute as well as from user pays activities and sponsorships. For more information on New Zealand Winegrowers visit **www.nzwine.com**.

Authors

Anteni Schalken
Associate Director, Tax & Private
Deloitte New Zealand
Tel: +64 9 306 4441
Email: aschalken@deloitte.co.nz

Data Analytics:

Josh Hawkey
Consultant, Tax & Private
Deloitte New Zealand
Tel: +64 9 975 8550
Email: johawkey@deloitte.co.nz

Key Contacts

Deloitte

Peter Felstead
Managing Partner, Tax & Private
Deloitte New Zealand
Tel: +64 9 306 4441
Email: pfelstead@deloitte.co.nz

Andrew Gibbs
Head of Primary Industries & Partner, Corporate Finance
Deloitte New Zealand
Tel: +64 4 470 3639
Email: agibbs@deloitte.co.nz

Tim Stables
Director, Corporate Finance
Deloitte New Zealand
Tel: +64 9 303 0851
Email: tistables@deloitte.co.nz

Rob McDonald
Director, Corporate Finance
Deloitte New Zealand
Tel: +64 3 363 3836
Email: robmcdonald@deloitte.co.nz

Mike Curtis
Partner, Tax & Private
Deloitte New Zealand
Tel: +64 4 495 3904
Email: mikecurtis@deloitte.co.nz

New Zealand Wine

Philip Gregan
Chief Executive Officer
New Zealand Winegrowers
Tel: +64 9 306 4441
Email: philip@nzwine.com

Sarah Szegota
Communication Manager
New Zealand Winegrowers
Tel: +64 9 306 5553
Email: sarah@nzwine.com

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