Australian Whisky Holdings

Positional paper

Advancing Tasmania's whisky industry

Australian Whisky Holdings (AWY) is an early stage company which is focused on creating, both organically and by acquisition, a commercial Tasmanian artisan, single malt whisky production and marketing company. The company is seeking to capitalise on the growing worldwide demand for premium singly malt whisky, particularly in China and has over the past four years brought together three of Tasmania's award-winning brands under its control and has an equity interest in a fourth distillery. The company also has, through the Lark Distillery acquisition, a premium gin label, Forty Spotted, which will provide early cashflows while the company grows and expands its whisky inventory. The company raised $10m in a share placement at $0.041/share to repay debt, fund capital investment and working capital. We have established a net present value (NPV) of estimated cashflows from whisky and gin sales of $0.09 a share, with whisky inventory at June 2028 contributing $0.05 a share. We have dimensioned an upside and downside case including capital expansion which delivers an NPV range of $0.06 to $0.19/share.

Business model

Australian Whisky Holdings controls three single malt whisky distilleries, Lark, Overeem and Nant, and a gin distillery, Forty Spotted, in Tasmania and has a 12% shareholding in a fourth Tasmanian whisky distillery, Old Kempton, which is distinguished as being one of only two paddock-to-bottle distilleries in the world. AWY aims to produce, mature and sell artisan, single malt whisky for both the Australian and export markets, in particular China. Its products are aimed at the premium end of the market, with its whisky retailing at ~$150-$200 per 500ml and its gin selling at ~$70 for 700 ml.

Capital Raising, FY19 Earnings Estimates and Valuation

AWY has recently completed a $10m (before expenses) share placement to institutional and sophisticated investors, priced at $0.041/share, which was a 7.6% discount to the 5-day VWAP prior to the raising. The proceeds will be used to repay debt, fund the Nant barrel buyback, pay for the second stage expansion of Nant distillery and working capital.

We are forecasting that Australian Whisky Holdings decants and bottles 20% of its estimated 366 mature barrels in FY19 and that Lark's gin still produces one run a week of 1,400 bottles. We also assume that AWY produces 1,296 barrels of premium whisky this financial year which will take at least four years to mature. This results in our forecast for $8.6m in revenue and a net loss of $2.3m.

We have used the discounted cashflow methodology to value Australian Whisky Holdings, arriving at a base case valuation of $0.09 per share including $0.05 per share for the whisky inventory we estimate AWY will hold at June 2028. Our valuation is generated from a WACC of 9.8%, terminal value 2.2% and a CAGR of free positive cashflows from 2021 of 44.3%, with most of this generated from FY21-23. We have also considered an upside case and a downside case based on an 20% increase/decrease in whisky and gin production giving a downside valuation of $0.06/share and upside of $0.14/share. Additionally, we have dimensioned a doubling of production capacity at each of the distilleries using debt and this potentially could add another $0.03-$0.05/share to the valuation range.

Historical earnings and RaaS Advisory estimates

Year end	Revenue (A$m)	EBITDA reported (A$m)	NPAT reported (A$m)	EPS (c)	P/E (x)	EV/Sales (x)
06/18a	0.4	(2.2)	(3.5)	(0.69)	na	128.45
06/19e	8.6	(1.0)	(2.3)	(0.15)	na	6.7
06/20e	12.3	0.9	(1.0)	(0.06)	na	4.7
06/21e	16.9	3.0	0.6	0.04	113.0	3.3

Source: Company data, RaaS Advisory Estimates for FY19e, FY20e and FY21e

Food and beverage

4th December 2018

Share details

ASX Code	AWY
Share price	$0.041
Market Capitalisation	$66.6M
Enterprise Value	$57.8M
Shares on issue	1.58B

Share performance (12 months)

Upside Case

- Opportunity to further consolidate Tasmanian whisky industry
- Premium, award-winning brands
- Board and management experienced in building businesses particularly beverage opportunities

Downside Case

- Very small player in an industry dominated by global players
- Talent is difficult to retain and will often leave to start up rival distilleries
- Working capital tied up in inventory

Board of Directors

Terry Cuthbertson	Non-Executive Chairman
Gary Mares	Non-Executive Director
Peter Herd	Non-Executive Director

Company contact

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Investment Case

AWY has the opportunity to achieve success, in our view, due to the following reasons:

- The company had acquired some of Tasmania's leading premium whisky brands and is well placed to capitalise on the growing demand for premium whisky in Asia, in particular China;
- It has a management team and advisers well experienced in building premium brands;
- Having secured near-full control of Lark Distillery, which owns both premium whisky and gin distilling interests, AWY has the opportunity to scale the group's operations through additional capital investment;
- Now it controls several premium and award-winning brands, AWY has the opportunity to consistently produce and market the brands in a manner not previously available to the individual businesses.

However, its plans are not without risks. AWY is a very small player in the liquor industry which is dominated by global players such as Diageo (DGE.L) and Remy Cointreau (REMYF) and Tasmania's whisky industry is tiny relative to the UK, the home of premium single malt whisky. While AWY has recently doubled production capacity at Nant Estate, its current combined production capacity across the three whisky distilleries is 28 barrels a week or 1,344 barrels a year. This translates into 288,960 bottles equivalent a year. To put that into context, Scotch whisky exports in 2017 were more than one billion bottles equivalent with single malt, the category that AWY's brands target, accounting for 122m bottles equivalent exported. The market for scotch whisky, however, is growing, with Scotland's single malt scotch whisky achieving double digit growth (14%) in value and volume terms in FY17. Demand for premium scotch whisky is growing rapidly in China, in particular, and we see an opportunity for AWY to capitalise on Tasmania's "clean and green" reputation in that market. The recent investment by Seppeltsfield Wines' in AWY potentially offers a bridge for the company into the Chinese market with this new investor already exporting into the region.

Company Background

Australian Whisky Holdings was previously called Montec International which was listed in November 2003 to market and sell its patented monounsaturated dairy formula in China. At the time, the company raised $10m at $0.50 a share, giving it a market capitalisation of $27m at float. By the end of FY14, the dairy export business was on care and maintenance. In Q1 FY15, Montec acquired a shareholding in Lark Distillery Pty Ltd, having already partnered with the whisky distiller earlier in calendar 2014 to export and market its whisky and gin in China. In late 2014, Montec asked shareholders to vote on changing its name to Australian Whisky Holdings so that it could pursue expansion of its interests in the Tasmanian whisky industry. Over the following three years, the company built its stake in Lark to 48.1% and then made a cash and scrip bid for the remaining shares it did not own. By June 2018, AWY owned 99.96% of Lark, having paid 307m shares and $0.83m in cash for the additional shares. This delivered AWY control of the Lark and Overeem whisky brands and the Forty Spotted gin brand.

In the meantime, AWY also reached agreement to acquire Nant Estate and its assets (October 2016). However, this initially hit a snag when the company subsequently discovered, in the process of its due diligence, that a barrel investor scheme had resulted in a short fall of whisky-filled barrels. The company announced that it intended to protect those who had invested in the barrel scheme and set about arranging a $1m finance facility to acquire the barrels from those who had invested. The company will now commit an additional $3.2m form the proceeds of its November 2018 capital raise to fund the remaining barrel buyback. In August 2017, AWY acquired the distillery assets including all IP for Nant from the receivers of NAW Distillery Pty Ltd, giving it outright control of the Nant estate and its distillery assets. AWY also owns a 12% share of Old Kempton Distillery, formerly known as Redlands Estate, which it acquired in 2016 for $300,000.

FY18 performance

AWY reported a net loss of $3.39m in FY18 on revenues of $0.43m. Gross profit for the period was $0.28m and demonstrated the first full year for AWY as a whisky producer. The company recognised a $23,181 profit from Lark Distillery for the period, of which its share was $11,155, having increased its holding from 48% to 99.96% by June 28. The company reported negative operating cashflows of $5m and ended FY18 with net debt of $0.13m, including cash of $6.86m.

Capital raised

In March 2018, AWY raised $7.85m (before expenses) at $0.03 per share, in a private placement to institutions and private investors. The transaction was at a 14.3% discount to the previous close and 7.3% discount to the 10-day VWAP. The proceeds of the issue were to be used as follows:

- Continuation of the barrel buyback program at Nant
- Capex on the stage one expansion at Nant to increase production from 416 barrels a year to 700 barrels a year;
- Planning on stage two expansion to more than double expansion to 1,500 barrels a year;
- Investment in marketing and distribution initiatives.

On November 2, 2018, AWY raised $10.0m (before expenses) at $0.041 per share, which was at a 6.8% discount to the last close and a 7.6% discount to the 5-day VWAP before the raise. The proceeds of this raise will be used to fund the following:

- $3.2m towards the Nant barrel buyback program;
- $2.5m towards repayment of debt
- Investment of $0.75m in second stage infrastructure at Nant distillery
- $3.55m to fund inventory and general working capital requirements.

Global whisky industry

Whisky/whiskey is produced in several countries but most relevant comparable market for AWY is Scotland. Scotch whisky exported just over one billion bottles equivalent in 2017 at a value of £4.3bn, according to the Scotch Whisky Association (data released in April 2018). Single malt scotch whisky accounted for 12.2% of scotch whisky exports. The US was the largest market for exports in dollar terms, followed by France which is the largest market in volume terms. It should be noted that Singapore and Latvia are hubs for surrounding countries export sales. China was one of the fastest growing markets for scotch whisky sales, increasing bottle volume sales by 30.6% and $ volume sales by 47.4%, reflecting an increasing shift to premium labels. We have set out the top 20 export markets for scotch whisky in the following exhibit.

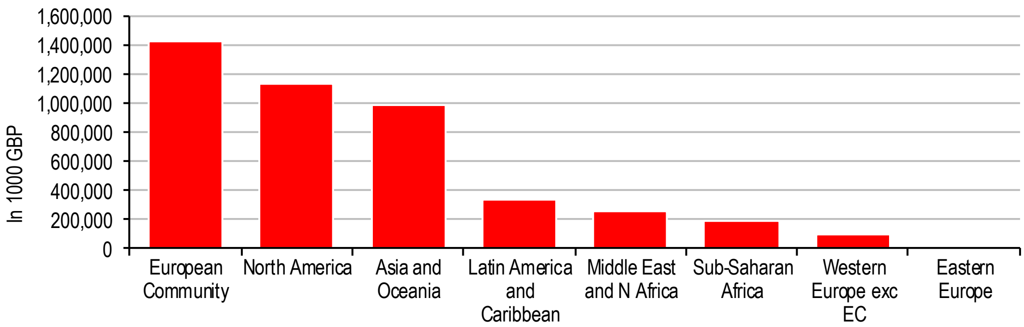
Exhibit 1: Top 20 Export Markets for all Scotch Whisky by value and volume in 2017 (ranked first by value)

Rank	Country	Value (£m)	% chg on pcp	Volume (m bottles)	% chg on pcp
1	USA	921.7	7.7%	127.5	7.4%
2	France	435	2.2%	178.8	-5.9%
3	Singapore	290.7	29.4%	46.6	14.1%
4	Germany	186.6	13.7%	56.3	6.1%
5	Spain	175.3	5.2%	60.9	-4.6%
6	Taiwan	160	-8.3%	18.7	-4.6%
7	United Arab Emirates	129.8	-1.2%	25.6	-7.6%
8	Latvia	120.5	104.7%	36.7	74.9%
9	South Africa	114.2	20.7%	52	17.0%
10	Mexico	111.1	-0.4%	53.4	-7.5%
11	India	103.5	7.2%	89.5	-4.8%
12	Australia	103.1	2.8%	30	4.4%
13	Japan	97.7	18.8%	33.8	13.9%
14	The Netherlands	85.1	11.7%	23.4	0.1%
15	Canada	83.3	13.2%	12.4	3.2%
16	South Korea	71.5	-18.2%	11.4	-27.2%
17	Poland	67.9	8.6%	27.5	-2.8%
18	China	61.0	47.4%	14.7	30.6%
19	Brazil	55.7	1.1%	36.2	-15.4%
20	Turkey	52.6	-0.4%	14.2	14.2%

Source: Scotch Whisky Association (www.scotch-whisky.org.uk)

Our following exhibit graphically demonstrates where UK exports of scotch whisky ended on a regional basis in 2017.

Exhibit 2: UK Whisky Exports in GBP by Region, 2017



Source: Statista, Scotch Whisky Association

Stepping back whisky for a second, it is worth considering the alcohol consumption levels by country forecasted for 2018. Perhaps not surprisingly, China is forecast to be the biggest consumer of alcohol in volume terms followed by the US. Statista has estimated that Chinese consumption of alcohol will increase to 65.2b litres of alcohol by 2020.

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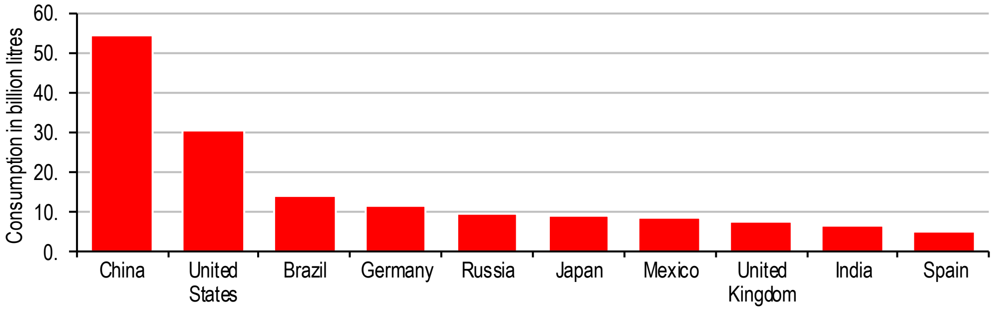
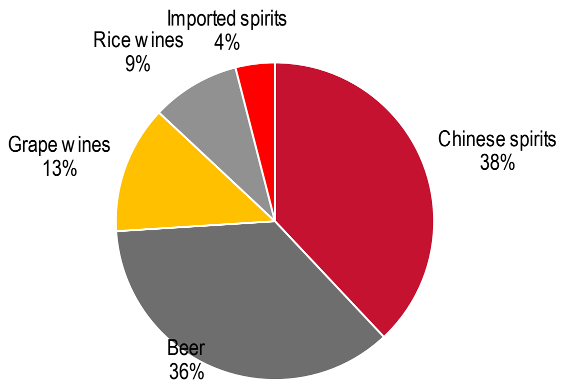
Exhibit 3: Alcoholic beverage consumption: leading countries worldwide 2018



Source: Banco do Nordeste; Euromonitor, Statista

However imported spirits are still a very small proportion of the Chinese alcoholic beverage market with Statista estimating at January 2017 that this category accounted for just 4% of sales. This demonstrates upside opportunity, particularly amongst China's growing middle class.

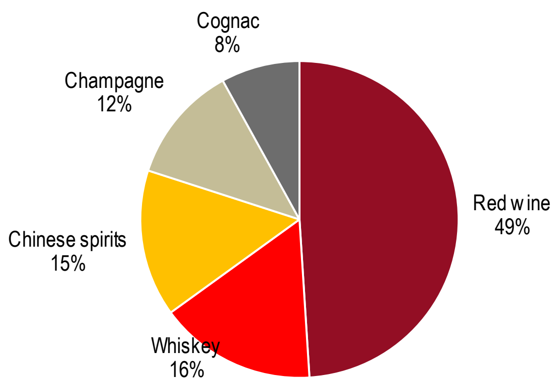
Exhibit 4: Alcoholic beverage market in China as of January 2017, by sub-sector



Source: Statista

While Chinese spirits is currently the most popular alcoholic beverage, there is potential for other beverages to erode its share, particularly as China becomes wealthier. Whisky consumption is more popular amongst wealthy Chinese although red wine is the preferred beverage, with 49% of Chinese millionaires in 2013 making red wine their drink of choice. Whisky was the second most popular beverage amongst Chinese millionaires at 16% and ahead of Chinese spirits, according to the 2013 survey by the Hurun Research Institute and GroupM. Note that whiskey outranks Chinese spirits with this group.

Exhibit 5: Most popular alcoholic beverages among Chinese millionaires in 2013



Source: GroupM; Hurun Research Institute

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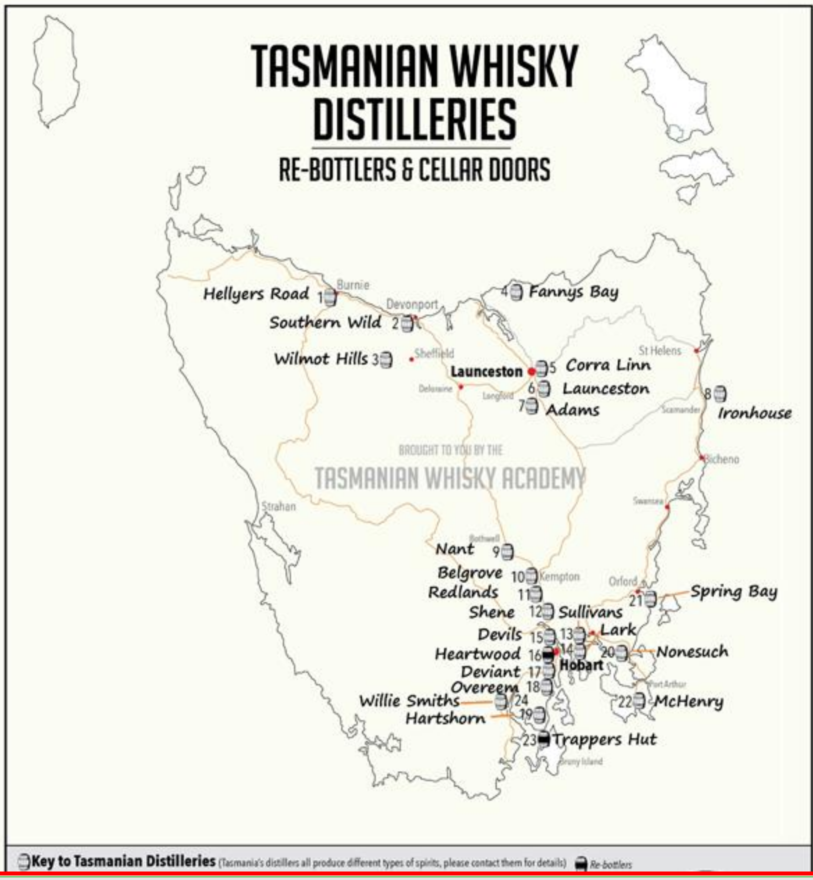
Australia’s whisky industry

Australia has around 60 distilleries with half of these located in Tasmania. Tasmania’s renewed whisky industry is now over 25 years old with around 30 distilleries operating and producing spirits on the island. The first modern day distillery, Lark, was founded in 1992 by Bill Lark, with barley borrowed from Cascade Brewery. Around 14 distilleries have produced and released aged whisky to the market and more are expected to do so over time. AWY owns three award winning brands, Lark, Overeem and Nant and has a 12% stake in Old Kempton (formerly Redlands) which is one of only two paddock-to-bottle distilleries in the world (the other is Kilchoman in Scotland). Other award-winning distilleries in Tasmania include:

- Sullivan’s Cove which won the World's Best Single Malt Whisky at the World Whisky Awards in 2014. This award was a first for Australia, and for any distillery outside of Scotland or Japan;
- Sullivan’s Cove American Oak Single Cask HH0351 collected the World’s Best Single Malt Whisky award at the 2018 World Whisky Awards. The HH0351 cask was distilled in 2000 and decanted in January 2017, making it 16 years and 5 months old. It was matured in a 200L American Oak ex-bourbon barrel and produced only 136 bottles.
- Hellyers Road which won two gold and one silver medal at the 2018 World Whisky Awards in London. The Hellyers Road Distillery Slightly Peated whisky won gold in the Australian no age division while the Master Series Port Cask Matured whisky won silver in the single cask Australian division. The distillery was also named Tasmania’s Exporter of the Year for 2017.

The industry however is still a cottage industry with availability of supply one of the biggest issues for the sector. Local retailers such as Dan Murphy’s and Vintage Cellars have been long supporters and stockists of Tasmanian whiskies and conversations with various outlets point to supply as the industry’s major hurdle.

Exhibit 6: Tasmanian Whisky Distilleries by location



Source: Tasmanian Whisky Academy

RaaS Forecasts

We have modelled each distillery both in terms of production and COGs. Following is a breakdown of the assumptions we have made:

- Starting price per barrel is $28,415 (this is derived from the company's Business Update presentation from March 2018;
- Nant's production and aged inventory profile has been built along the lines of the Stage 1 expansion maturation profile outlined in the March 2018 presentation. We have assumed that Nant produces on average 12 barrels a week in H119 (Q1 at 8 barrels per week and Q2 at 14 barrels per week) and H219 production and thereafter increases to 14 barrels a week;
- We have assumed that Nant commenced FY19 with 166 mature barrels and that through the barrel buyback scheme it will add another 1,000 barrels to its mature barrels for sale over the next two years. Lark and Overeem produce 7 barrels a week (starting with 200 mature barrels) and Forty Spotted does one still turn a week (1,400 bottles) rising to 1.7 turns (still capacity is 5 turns a week).
- Our forecasts assume that on average AWY decants and sells 25% of its inventory from FY19 (20% in FY19). This will rely on the distilleries producing whisky at the rate we have described above and, due to the low inventory levels to begin with, this will potentially result in a fall in sales in FY21 while inventory matures.

Exhibit 7: Forecasts on a per bottle, per distillery basis by half year

	1H19	2H19	1H20	2H20	1H21	2H21	1H22	2H22	1H23	2H23	1H24	2H24	1H25	2H25
Nant														
Revenue $ per bottle	132.16	134.15	136.16	138.20	140.27	142.38	144.51	146.68	148.88	151.11	153.38	155.68	158.02	160.39
COGS $ per bottle	56.35	57.19	58.05	58.92	59.81	60.70	61.61	62.54	63.48	64.43	65.39	66.37	67.37	68.38
Gross Profit $ per Nant bottle	75.82	76.95	78.11	79.28	80.47	81.67	82.90	84.14	85.41	86.69	87.99	89.31	90.65	92.01
Lark														
Revenue $ per bottle	132.16	134.15	136.16	138.20	140.27	142.38	144.51	146.68	148.88	151.11	153.38	155.68	158.02	160.39
COGS $ per bottle	59.35	60.24	61.14	62.06	62.99	63.93	64.89	65.87	66.85	67.86	68.88	69.91	70.96	72.02
Gross Profit per Lark bottle	72.82	73.91	75.02	76.14	77.28	78.44	79.62	80.81	82.03	83.26	84.50	85.77	87.06	88.36
Overeem														
Revenue $ per bottle	183.32	186.07	188.86	191.70	194.57	197.49	200.45	203.46	206.51	209.61	212.75	215.94	219.18	222.47
COGS $ per bottle	76.75	77.90	79.07	80.25	81.46	82.68	83.92	85.18	86.46	87.75	89.07	90.40	91.76	93.14
Gross Profit per Overeem bottle	106.57	108.17	109.80	111.44	113.11	114.81	116.53	118.28	120.06	121.86	123.68	125.54	127.42	129.33
Forty Spotted														
Revenue $ per bottle	50.0	50.8	51.5	52.3	53.1	53.9	54.7	55.5	56.3	57.2	58.0	58.9	59.8	60.7
COGS $ per bottle	39.8	40.4	41.0	41.6	42.2	42.8	43.5	44.1	44.8	45.5	46.2	46.8	47.5	48.3
Gross Profit per Forty Spotted bottle	10.2	10.4	10.5	10.7	10.9	11.0	11.2	11.4	11.5	11.7	11.9	12.1	12.2	12.4
Gross profit generated $M														
Nant	0.54	0.44	1.85	1.41	2.52	2.51	4.00	3.91	3.86	4.28	4.85	5.30	5.67	5.98
Lark	0.39	0.32	0.32	0.24	0.19	0.71	1.11	1.58	1.94	2.23	2.46	2.65	2.80	2.93
Overeem	0.25	0.20	0.20	0.16	0.12	0.09	0.07	0.67	1.13	1.65	2.06	2.39	2.65	2.86
Forty Spotted	0.49	0.50	0.51	0.51	0.63	0.63	0.64	0.65	0.80	0.81	0.82	0.83	1.01	1.03
Total Gross Profit	**1.67**	**1.46**	**2.88**	**2.32**	**3.45**	**3.94**	**5.82**	**6.81**	**7.73**	**8.97**	**10.19**	**11.17**	**12.14**	**12.80**
Shared costs $M	2.03	2.09	2.12	2.15	2.19	2.22	2.26	2.30	2.33	2.37	2.41	2.45	2.49	2.53
EBITDA ($M)	**(0.36)**	**(0.63)**	**0.76**	**0.17**	**1.26**	**1.72**	**3.56**	**4.51**	**5.39**	**6.60**	**7.78**	**8.72**	**9.65**	**10.27**

Source: RaaS forecasts

Note that we do not include the cost of producing new barrels in our earnings forecasts. We anticipate that the company will capitalise these costs and bring them to account when the barrels are matured and ready for sale. We also assume the following:

- Cost of production in the barrel is $2,100 per barrel (a combination of barley, cooperage, water, electricity and labour);
- Excise costs for 500ml bottles of 43% proof whisky of $18.10, 700ml of $25.30 and 700ml of 40% proof gin $23.50;
- Bottling, labelling and packaging costs of $12 per bottle for Nant, $15 each for Lark and Overeem and $10 for production and bottling for Forty Spotted gin.
- We anticipate that 50% of sales will be on mainland Australia where AWY has commissioned Spirits Platform, a company 37% owned by Remy Cointreau and the main distributor for premium single malt whisky labels McCallan and Highland Park to sell Nant and Proof & Co, another distributor recently established in Australia to sell Lark, Overeem and Forty Spotted. We assume 25% of the wholesale price goes to these two distributors.

Our per bottle estimates are set out on the previous page in Exhibit 7. We set out FY19 to FY25 revenue, EBITDA, NPAT and EPS in the following exhibit. We are anticipating that AWY generates positive EBITDA in FY21 as sales volumes pick up enough to offset the largely fixed cost nature of shared costs.

Exhibit 8: Earnings forecasts FY19-FY25 (in $m unless otherwise stated)

Year ending June 30	2019	2020	2021	2022	2023	2024	2025
Revenue	8.6	12.3	16.9	26.3	34.4	42.7	50.2
EBITDA	(1.0)	0.9	3.0	8.1	12.0	16.5	19.9
NPAT	(2.3)	(1.0)	0.6	4.2	6.8	10.1	12.7
EPS	(0.15)	(0.06)	0.04	0.26	0.43	0.64	0.80

Source: RaaS estimates

SWOT analysis

A SWOT analysis of AWY is set out in the following exhibit. We see more strength and opportunities for the company than weaknesses and threats.

Exhibit 9: Strengths, Weaknesses, Opportunities, Threats

Strengths	Opportunities
Highly regarded and award-winning product	China is a growth market for spirits, in particular whisky and has the fastest growing online alcohol market with more than US$6.1m in sales in 2017 (three times the US online alcohol sales market)
Board and senior executive team experienced in building businesses and brands	Further consolidation of Tasmanian industry
Have the founder of Tasmanian whisky, Bill Lark, in the fold as a shareholder and adviser	Gin Still can be expanded to deliver more near term cashflows
Scale is delivering economies and greater consistency of production	Additional capex of circa $28-29m over the next three years would double production capacity
Has attracted Seppeltsfield Wines as a strategic shareholder, giving AWY potential access to both its export contacts in China and high-quality aged sherry and port barrels	Opportunity to improve GP margins through streamlined practices
	Chinese backlash against US has resulted in a 25% cut in US whiskey imports to China; this represents an opportunity for whisky from other jurisdictions
Weaknesses	**Threats**
Small player in a competitive market dominated by global players	Global players are aggressively chasing market share
Stock liquidity	Dependent on access to water and to barley prices
Whisky inventory is tied up for at least five years before maturity	Tendency for trained staff to be poached or establish their own labels
Giving up 25% of its wholesale price for distribution in mainland Australia	Declining sherry and port consumption will put pressure on barrel availability

Source: RaaS analysis

Sensitivities

- Aged whisky takes several years to mature and, as a consequence, working capital will be tied up in inventory. We have assumed that AWY decants and sells 25% of its matured whisky. However, it is going to take time to build inventory for scale. We estimate that AWY commenced FY19 with 366 mature barrels in its inventory and that it will take until the end of calendar 2021 to build that to 1,000 mature barrels. In addition, Overeem's maturation profile takes at least 5-6 years versus the 4-5 year maturation profile of Lark and Nant;
- The provenance of inputs into AWY's whiskies is important to the brands and access to Tasmanian grown barley is an ongoing issue. According to ABARES, Tasmania's barley production in FY18 was expected to be 17,290 tonnes, 0.2% of the national crop and it has been static for the past three years. The growth in craft beers and distillers in the state has increased competition for the crop. CEO, Chris Malcolm notes that he bought up all the barley he could for Nant in 2017 to ensure Nant could claim provenance;
- Our forecasts assume the average cost of whisky production is $2,100. This comprises $600 for the barrel, $330 for barley. $65 for yeast, $404 for distiller wages (5 distillers), electricity $210, insurance $250, other costs $250. Production costs will be sensitive to increases in electricity and insurance inputs as well as barley as we highlighted above.
- Access to water is a potential risk for the Lark and Overeem distilleries which rely on access to town water; Nant has a dedicated pipeline from Lake Sorell ensuring it has sufficient water for future expansion;
- Access to talent is an ongoing issue for AWY and the industry at large; there is no tertiary course for distillers and often-times, senior distillers will leave to set up their own distilleries;
- Aged sherry and port barrels are becoming harder to access as worldwide consumption, and production, declines. AWY is fortunate in that its CEO Chris Malcolm owns separate interests which specialise in both sourcing aged barrels and cooperage and its strategic shareholder Seppeltsfield Wines also is a supplier of high-quality aged sherry and port barrels to the whisky industry.

Board and management

Directors

Terry Cuthbertson, Non-Executive Chairman, has been chairman of the entity since July 2004, following the death of Jim Grant, the founding chairman of Montec International, the predecessor of AWY. Mr Cuthbertson is also non-executive chairman of Austpac Resources NL (APG), MNF Group Ltd (MNF), Malachite Resources Ltd (MAR) and South American Iron and Steel Corporation Ltd (SAY) and is non-executive director of Mint Wireless Ltd (MNW) and iSentric Ltd (ICU). He has previously been a partner of KPMG and director of KPMG Corporate Finance and the NSW partner in charge of mergers and acquisitions and was group finance director of Tech Pacific Holdings

Gary Mares, Non-Executive Director, has extensive public accounting, corporate governance and corporate services experience, having held senior positions at KPMG, Lend Lease and Tech Pacific Holdings. He is the principal of Sydney based accounting firm Gary D. Mares and Associates. He has been a director of AWY since September 2014.

Peter Herd, Non-Executive Director, has been a non-executive director since July 2004. He was previously general manager of Dairy Farmers' Milk and Beverage division, nd held several regional senior executive and country head positions with Coca-Cola in the Asia-Pacific region.

Management

Chris Malcolm, Chief Executive Officer, was appointed to the position in March 2017 after initially assisting the company in an advisory capacity in the Nant Estate acquisition. Mr Malcolm is also the chairman of Lark Distillery and Clark Rubber Franchising, a business he built from scratch to 79 stores and ~$110m in sales. He also is a co-owner and a director of Whisky Negociants Pty Ltd, and a director of Mastercask Pty Ltd, a barrel and cooperage business.

Demetrius Giouzelis, Head of Brand and Commercial, was appointed to his position on 1 August 2018. He brings more than 17years' experience to the role having been responsible for the marketing of mid-range Scotch whisky brands Laphroaig and Bowmore, the house of Suntory whisky range, American oak whisky Auchentoshan, Roku Gin and the mass market Jim Beam, Makers Mark, Canadian Club and Cointreau brands.

Brendan Waights, Chief Financial Officer, was appointed on 18th October 2018. He brings more than 27 years' experience in finance, mergers & acquisitions, risk management, corporate restructuring and capital raisings across a diverse range of sectors.

Peer Comparison

We have examined a range of peers both in Australia, New Zealand and internationally to consider what sort of profit margins and trading multiples AWY should trade on in future years. It should be noted that with the exception of Foley Family Wines in NZ and Berentzen-Gruppe AG in Germany, the peer group is dominated by large and multi-national companies. The peer group is also populated by mature companies at a much later stage in their lifecycles to AWY.

Exhibit 10: Profitable local and global compcos

Company	Code	Share price	Market Cap (M)	Enterprise value (M)	EV/EBITDA	EV/Sales	P/E	EBITDA margin %
Australian/NZ Distillers and Vintners								
Australian Vintage	AVG	0.51	143	230	9.9	0.9	18.9	9%
Delegat	DGL.NZE	9.70	981	1,250	13.2	4.6	21.0	35%
Foley Family Wines	FFW.NZE	1.36	72	89	12.5	2.3	45.3	17%
Treasury Wines	TWE	14.29	10,270	11,050	29.0	4.4	18.2	15%
Median Australia/NZ					**12.9**	**3.4**	**19.9**	**16%**
International Small Cap Distillers and Vintners								
Castle Brands	ROX.US	0.91	153.5	202.4	36.3	2.33	56.8	7%
Marie Brizard Wine & Spirits	MBWS.PA	4.47	124.97	128.11	8.45	0.29	5.5	3%
Berentzen-Gruppe AG	BEZ.F	6.27	59	57	4.0	0.3	14.5	8%
International Large Cap Distillers & Vintners								
Brown-Forman Corporation	BF-B	46.40	22,350	25,640	22.9	7.8	30.5	34%
Constellation Brands	STZ-B	195.60	36,980	47,520	16.5	6.0	11.8	36%
Diageo Plc	DGE.L	2823.50	68,740	79,870	19.4	6.6	23.3	34%
Davide Campari-Milano	CPR.MI	7.42	8,530	9,810	19.6	5.5	21.6	28%
Remy Cointreau	REMYF	117.42	6,060	6,230	20.7	4.7	35.6	23%
Median All			**3,521**		**17.9**	**4.6**	**21.3**	**21%**

Source: Thomson Reuters, Bloomberg, Capital IQ, RaaS Analysis *Prices at 22 November 2018 and shown in the currency of each company's domicile

If we were to apply the median EV/sales multiple of 4.6x to our FY20 revenue forecasts of $12.3m (giving AWY 12 months' leeway to get its production and distribution systems operational) we would arrive at a compco valuation of $0.035 per share. However, this does not acknowledge the early stage nature of AWY's business.

The compco group has generated a median CAGR of revenues from 2014 to 2018 of 3.7% (set out in Exhibit 11 on the following page), reflecting the mature nature of the group. AWY is much earlier stage and therefore is forecast to have a much higher growth rate in revenues and NPAT in its early years. We don't anticipate the company to be profitable until FY21 and discuss an additional valuation methodology in the following section.

Research as a Service

Exhibit 11: CAGRs in revenues generated by Australian/New Zealand tech compcos

Company	CAGR in revenues 2014-2018
Australian Vintage	3.5%
Delegat	4.2%
Foley Family Wines	2.8%
Treasury Wines	6.1%
Castle Brands	12.6%
Marie Brizard Wine & Spirits	-5.4%
Berentzen-Gruppe AG	3.0%
Brown-Forman Corporation	0.9%
Constellation Brands	5.9%
Diageo Plc	3.0%
Davide Campari-Milano	3.9%
Remy Cointreau	4.2%
Median All	**3.7%**

Source: Company reports, Consensus from Stockopedia, RaaS Analysis

Valuation – 'the Golden Rule'

The sense of pre-earnings and pre-cash flow valuations can be cross checked using a simple relationship that focuses attention on the most significant risks and opportunities. This premise was examined by Dr Kingsley Jones[1] and suggested as a golden rule used by venture capitalists and early stage investors to sense check their valuations. The golden rule is based on the following:

- Early-stage companies have revenue as the most visible performance metric
- Later-stage companies have earnings and margin as visible metrics
- Valuations at both stages are subject to sentiment and changing multiples

This simple valuation rule takes into account profit margins and earnings multiples and is defined as:

Current price to sales = Stable NPAT margin X Price Earnings Ratio X Sales uplift/Price uplift.

The price that the market will pay at a given time is dependent on the cyclicality of markets. When the market favours growth then the emphasis is on revenue multiples with seemingly little regard for profitability. However, as this enthusiasm cools the market will turn its attention to profitability and return on funds employed. If we apply the simple valuation rule explained above and make the following assumptions:

- Sales uplift (defined as the expected growth in sales over the investor's investment horizon) divided by price (to the investor) uplift (defined as the investor's expectations of return over the investor's investment horizon).
- A long run EBITDA profit margin for the industry of ~21% which converts to 15% NPAT margin using a tax rate 30%.

The third component to this calculation is Price Earnings Ratio. The long-term PE ratio of the ASX is 15x. The median PE for profitable companies in our comparative company group is 21.3x. The market capitalization of this group of companies averages US$3.6b. Most of these companies are profitable leaders in their respective markets and this, together with relative size and growth prospects, sees the market paying around 1.4x the market PE.

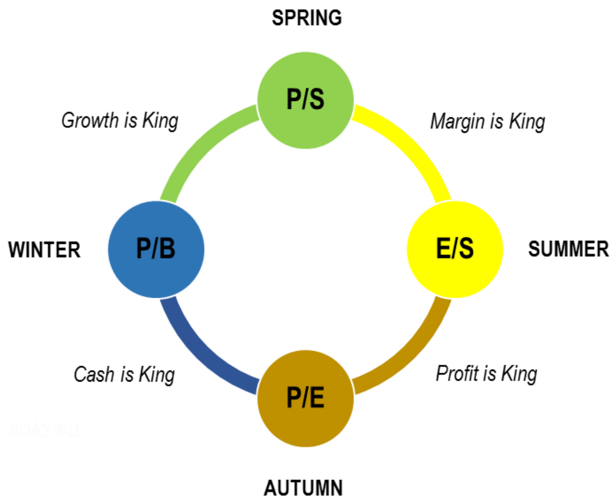
Our simple valuation approach (the Golden Rule) described above is a way of taking into account the ultimate profitability of each company. In a buoyant financial market where growth is king, investors will tend to focus on revenue (the spring season). The next stage will be a focus on margins followed by an autumn period where the focus turns to profit before entering the depressed winter stage where cash is

1 Jevons Global – Valuation for Early-Stage Technology Companies

RaaS
Research as a Service

king. In our view the market seems to have turned its attention more to profitability or at least the path to profitability rather than revenue growth. Investor mood changes are illustrated in the exhibit below:

Exhibit 12: The seasons of valuation



Source: Jevons Global – Valuation for Early-Stage Technology Companies (P/S – Price/Sales; E/S – Earnings/Sales; P/E – Price/Earnings; P/B – Price/Book)

Application of Golden Rule

Input selection

We have selected as a long-term steady state PE 21.3x which is at a 42% premium to the long-term average market PE of 15x. Our analysis of the comparative company group suggests that companies with scale and reach trade at a greater premium. We have laid out the following exhibit to demonstrate the uplift factor required to achieve various revenue multiples, based on using the peer group NPAT margin of 15% and the group's PE. We have shaded in the second row of this table to highlight the revenue multiple that most closely matches the peer group in terms of uplift factor, NPAT margin and long-term PE and the implied enterprise value of AWY using this method. Based on a compco revenue multiple of 4.6x, the implied uplift factor is 1.44. If we apply the revenue multiple of 4.6x to our FY20 revenue forecast of $12.3m (we use FY20 as it is the first full year in which AWY will have the benefit of its current expansion program), we arrive at an implied enterprise value of $56m, or $0.035/share. We have also highlighted on the following exhibit the uplift factor and revenue multiple implied in the current share price of $0.041/share, using the peer NPAT margins and PE multiple and the revenue multiple and uplift factor required to achieve our DCF valuation of $0.09 per share. This serves to highlight the early stage nature of AWY and the growth required to achieve the current share price and our base case valuation.

Exhibit 13: Uplift factors required to achieve current share price and DCF

NPAT margin	P/E	Uplift factor	Revenue multiple (x)	Implied AWY EV ($m)	Implied AWY Share Price
15%	21.3	1.00	3.20	39.3	$0.025
15%	21.3	1.44	4.60	56.6	$0.035
15%	21.3	1.65	5.27	64.8	$0.041
15%	21.3	2.00	6.39	78.6	$0.049
15%	21.3	3.00	9.59	117.9	$0.074
15%	21.3	3.65	11.66	143.4	$0.090
15%	21.3	4.00	12.78	157.2	$0.098

Source: RaaS analysis

DCF valuation

We are of the view that the discounted cashflow methodology is the most appropriate methodology for valuing early stage companies. Our base case DCF valuation of AWY's cashflows from FY19 to FY28 is $0.09/share and uses a WACC of 9.8% (beta of 1.2, terminal value of 2.2%). We ordinarily would lean towards a higher WACC but an examination of the 3-year beta of the company's peer group suggests that our beta of 1.2 is conservative as we demonstrate below.

Exhibit 14: Peer company 3-year beta

Company	Beta
Australian Vintage	0.38
Delegat	0.35
Foley Family Wines	0.27
Treasury Wines	0.85
Castle Brands	0.62
Marie Brizard Wine & Spirits	0.66
Berentzen-Gruppe AG	0.04
Brown-Forman Corporation	0.64
Constellation Brands	-0.13
Diageo Plc	1.21
Davide Campari-Milano	0.22
Remy Cointreau	0.49
Median All	**0.44**

Source: Reuters

We set out our base case DCF valuation in the following exhibit. It should be noted that we have also applied a net present value to the inventory at June 2028 to demonstrate the value of the inventory captured in the total DCF valuation. This accounts for $0.05 of our $0.10 a share valuation.

Exhibit 15: Base Case DCF valuation and NPV of Whisky Inventory at 2028

Parameters	Outcome
Discount Rate / WACC	9.8%
Beta	1.2
Terminal growth rate assumption	2.2%
Sum of PV ($m)	37.2
Terminal value ($m)	251.8
PV of terminal Value ($m)*	90.4
PV of Enterprise ($m)	127.6
Debt (Cash) ($m) (inc cash from recent capital raise)	(9.3)
Net Value – Shareholder ($m)	136.9
No of shares on issue (inc in the money options) (m)	1599
NPV per share	**$0.09**
Number of barrels at 2028	6,190
Price per barrel	$37,705
Cost per barrel	$2,787
Total value of Whisky inventory ($m)	**216**
NPV of Whisky inventory (in $m)	85
NPV per share of whisky inventory*	**$0.05**

Source: RaaS estimates *NPV of whisky inventory included in the terminal value

Reverse DCF

We have applied a reverse DCF to determine the growth rate expectations for implied in the current share price of $0.041/share. Using our forecast for FY21 EBIT of $1.5m (first forecasted year for profitable EBIT), we need to apply a compound annual growth rate (CAGR) of 26.9% from FY21 to FY28 in free cashflows to arrive at a valuation of $.041/share. This compares with the 44.3% CAGR in free cashflows from FY21-FY28 in our base case DCF valuation.

Scenario analysis

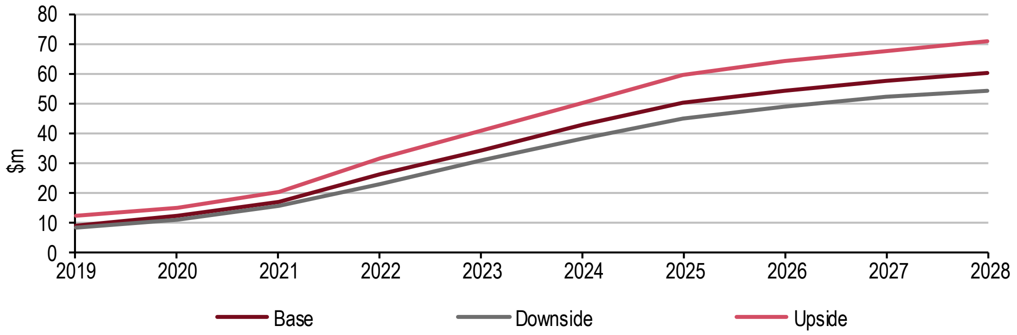
We have set out the different scenarios in our model for base case, an upside case and a downside case in the following four exhibits.

We set out some of the parameters we have used to reach these forecasts:

- Base case revenue and costs are as we have already set out on page 6 and 7;
- An Upside case assumes that 30% of mature barrels are decanted and sold and that gin production is 1.3 turns a week, rising to 2.2 turns;
- A downside case assumes 20% of mature barrels are decanted, bottled and sold and that gin production is 0.8 turns a week rising to 1.3 turns.

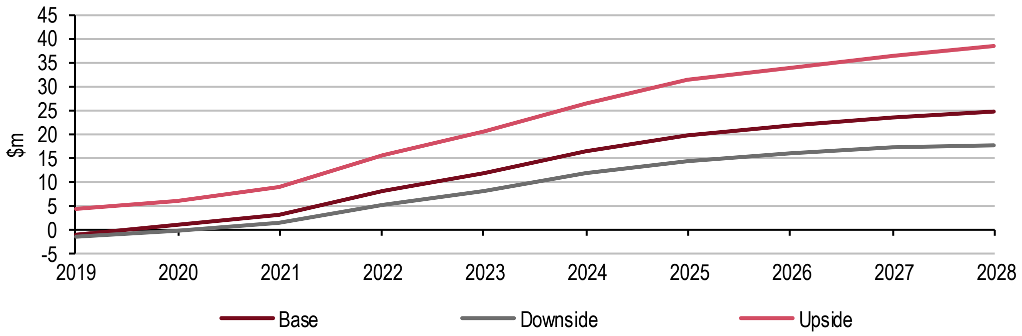
The revenue ad EBITDA forecasts by year are set out in the following two exhibits.

Exhibit 16: Revenue estimates



Source: RaaS estimates

Exhibit 17: EBITDA estimates



Source: RaaS estimates

Impact of expanded capacity

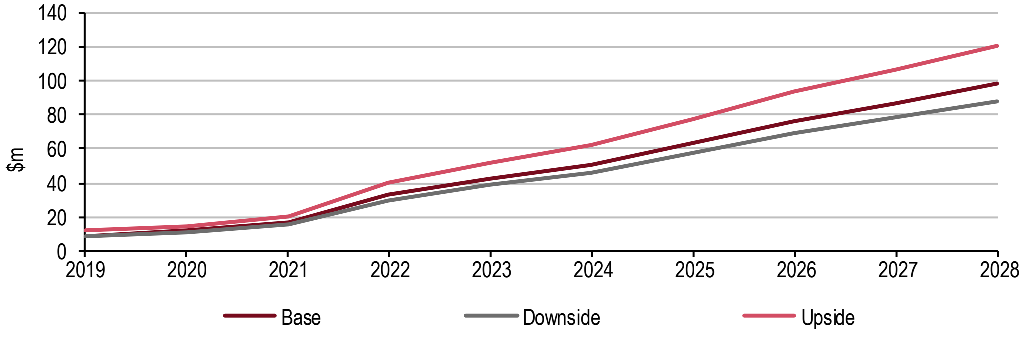
We have also dimensioned additional capacity in our model as AWY has stated ambitions to expand production. We have assumed that, using debt, the company doubles capacity at Nant in 1H21 at a capital cost of $7.5m. This would take production to 1,344 barrels a year at the site. We have also assumed the following:

- Gin production doubles at 1H22 with capex of $4.5m. This would lift turns to 3.5 a week.
- Lark's distillery would double capacity to 672 barrels a year at a capital cost of $8m. We have assumed this is funded by debt and introduced in 1H23;

- Overeem doubles capacity to 672 barrels a year at a capital cost of $8m with this coming into play at 1H24.

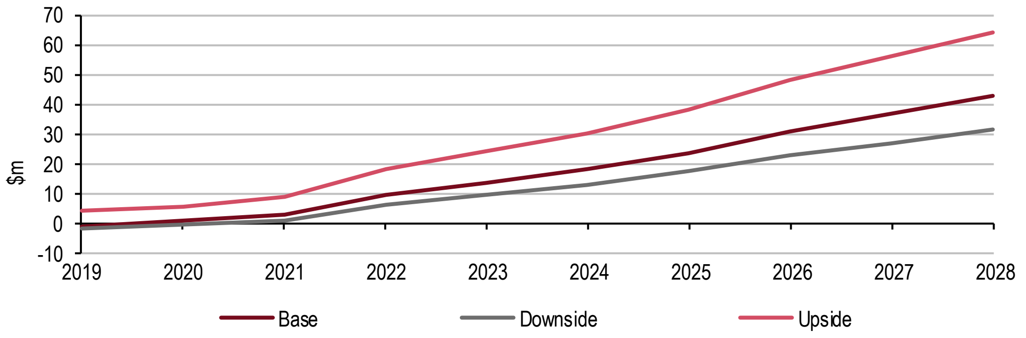
The impact on revenue and EBITDA estimates on a case selection basis is set out in the following two exhibits on the next page.

Exhibit 18: Revenue estimates including capex expansion of the four distilleries



Source: RaaS estimates

Exhibit 19: EBITDA estimates including capex expansion of the distilleries



Source: RaaS estimates

We have set out the valuation impact of the scenario analyses highlighted above in the following exhibit.

Exhibit 20: Impact of scenario analyses on DCF valuation

Base case valuation		**Base case with expanded capacity**	
NPV ex whisky inventory at 2028	$0.03	NPV ex whisky inventory at 2028	$0.02
NPV of whisky inventory at 2028	$0.05	NPV of whisky inventory at 2028	$0.10
Total NPV per share	**$0.09**	**Total NPV per share**	**$0.12**
A downside case valuation		**A downside case with expanded capacity**	
NPV ex whisky inventory at 2028	$0.01	NPV ex whisky inventory at 2028	-$0.01
NPV of whisky inventory at 2028	$0.05	NPV of whisky inventory at 2028	$0.10
Total NPV per share	**$0.06**	**Total NPV per share**	**$0.09**
An upside case valuation		**An upside case with expanded capacity**	
NPV ex whisky inventory at 2028	$0.08	NPV ex whisky inventory at 2028	$0.09
NPV of whisky inventory at 2028	$0.05	NPV of whisky inventory at 2028	$0.10
Total NPV per share	**$0.14**	**Total NPV per share**	**$0.19**

Source: RaaS estimates

Exhibit 21: Financial Summary

Australian Whisky Holdings Ltd (AWY.AX)					
Profit and Loss (A$m)					
Y/E 30 June	**FY17A**	**FY18A**	**FY19F**	**FY20F**	**FY21F**
Revenue	0.1	0.4	8.6	12.3	16.9
Gross profit	(0.1)	0.3	3.1	5.2	7.4
GP margin %	nm	64.4%	36.3%	42.3%	43.7%
EBITDA	(2.1)	(2.2)	(1.0)	0.9	3.0
Depn	(0.0)	(0.1)	(1.3)	(1.6)	(1.5)
Amort	(0.0)	0.0	(0.7)	(0.6)	(0.6)
EBIT	(2.1)	(2.4)	(3.0)	(1.3)	0.9
Interest	(0.6)	(1.0)	(0.3)	(0.1)	(0.1)
Tax	0.0	0.0	1.0	0.4	(0.2)
Minorities	0.0	0.0	0.0	0.0	0.0
Equity accounted assoc	0.1	0.0	0.0	0.0	0.0
NPAT pre significant items	(2.6)	(3.5)	(2.3)	(1.0)	0.6
Significant items	0.0	0.0	0.0	0.0	0.0
NPAT (reported)	**(2.6)**	**(3.5)**	**(2.3)**	**(1.0)**	**0.6**
Cash flow (A$m)					
Y/E 30 June	**FY17A**	**FY18A**	**FY19F**	**FY20F**	**FY21F**
EBITDA	(2.1)	(2.2)	(1.0)	0.9	3.0
Interest	(0.3)	(0.5)	(0.3)	(0.1)	(0.1)
Tax	0.0	0.0	0.0	0.0	(0.2)
Working capital changes	(0.4)	(2.3)	5.1	0.1	(0.7)
Operating cash flow	(2.8)	(5.0)	3.8	0.9	1.9
Mtce capex	0.0	0.0	(0.4)	(0.4)	(0.4)
Free cash flow	(2.8)	(5.0)	3.4	0.5	1.5
Growth capex	(6.4)	(3.3)	(4.0)	(0.4)	(0.4)
Acquisitions/Disposals	(3.7)	(1.8)	0.0	0.0	0.0
Other	0.0	(0.1)	0.0	0.0	0.0
Cash flow pre financing	(12.9)	(10.2)	(0.5)	0.1	1.1
Equity	6.9	14.9	9.4	0.0	0.0
Debt	6.5	1.3	(2.5)	(0.1)	0.7
Dividends paid	0.0	0.0	0.0	0.0	0.0
Net cash flow for year	0.5	6.0	6.4	(0.0)	1.8
Balance sheet (A$m)					
Y/E 30 June	**FY17A**	**FY18A**	**FY19F**	**FY20F**	**FY21F**
Cash	0.9	6.9	13.3	13.3	15.1
Accounts receivable	0.2	1.4	3.6	5.1	7.0
Inventory	1.4	9.6	7.0	9.1	12.1
Other current assets	0.0	0.3	0.3	0.3	0.3
Total current assets	*2.5*	*18.2*	*24.2*	*27.8*	*34.6*
PPE	6.4	12.9	16.0	15.3	14.6
Goodwill	0.0	0.0	0.0	0.0	0.0
Investments	6.7	0.6	0.6	0.6	0.6
Deferred tax asset	0.0	0.0	1.0	1.4	1.4
Other non current assets	0.0	7.4	6.7	6.1	5.5
Total non current assets	*13.2*	*20.9*	*24.2*	*23.3*	*22.0*
Total Assets	15.7	39.0	48.4	51.1	56.6
Accounts payable	1.0	0.7	2.7	3.5	4.7
Short term debt	2.2	0.3	0.3	0.3	0.3
Tax payable	0.0	0.0	0.0	0.0	0.0
Other current liabilities	0.1	0.1	2.8	5.8	8.8
Total current liabilities	*3.3*	*1.1*	*5.9*	*9.6*	*13.8*
Long term debt	6.2	6.7	4.2	4.0	4.8
Other non current liabs	0.0	0.3	0.3	0.3	0.3
Total long term liabilities	*6.2*	*7.0*	*4.5*	*4.3*	*5.1*
Total Liabilities	9.5	8.1	10.3	13.9	18.9
Net Assets	**6.2**	**31.0**	**38.1**	**37.1**	**37.7**
Share capital	30.9	38.0	47.4	47.4	47.4
Accumulated profits/losses	(24.9)	(7.0)	(9.3)	(10.3)	(9.7)
Reserves	0.1	0.0	0.0	0.0	0.0
Minorities	0.0	0.0	0.0	0.0	0.0
Total Shareholder funds	**6.2**	**31.0**	**38.1**	**37.1**	**37.7**

Share price (3 December 2018)					A$	0.041
Interim (A$m)	**H118A**	**H218A**	**H119F**	**H219F**	**H120F**	**H220F**
Revenue	0.2	0.3	4.5	4.1	6.6	5.7
EBITDA	(1.4)	(0.8)	(0.4)	(0.6)	0.8	0.2
EBIT	(1.6)	(0.8)	(1.4)	(1.6)	(0.4)	(0.9)
NPAT (normalised)	(2.0)	(1.5)	(1.1)	(1.2)	(0.3)	(0.7)
Minorities	0.0	0.0	0.0	0.0	0.0	0.0
NPAT (reported)	(2.0)	(1.5)	(1.1)	(1.2)	(0.3)	(0.7)
EPS (normalised)	(0.5)	(0.2)	(0.1)	(0.1)	(0.0)	(0.0)
EPS (reported)	(0.5)	(0.2)	(0.1)	(0.1)	(0.0)	(0.0)
Dividend (cps)	0.0	0.0	0.0	0.0	0.0	0.0
Imputation	30.0	30.0	30.0	30.0	30.0	30.0
Operating cash flow	(2.5)	(2.5)	6.3	(2.5)	0.5	0.4
Free Cash flow	(0.6)	(1.1)	6.9	1.3	1.0	0.8
Divisionals	**H118A**	**H218A**	**H119F**	**H219F**	**H120F**	**H220F**
Whisky sales	0.2	0.2	2.1	1.7	4.2	3.2
Gin sales			2.4	2.4	2.5	2.5
Total Revenue	**0.2**	**0.2**	**4.5**	**4.1**	**6.6**	**5.7**
Whisky gross profit	0.1	0.2	1.2	1.0	2.4	1.8
Gin gross profit			0.5	0.5	0.5	0.5
Total Gross Profit	**0.1**	**0.2**	**1.7**	**1.5**	**2.9**	**2.3**
Employment	0.2	0.0	0.6	0.6	0.6	0.6
Marketing			0.1	0.1	0.2	0.2
Other costs	1.3	1.0	1.3	1.4	1.4	1.4
Total costs	**1.5**	**1.0**	**2.0**	**2.1**	**2.1**	**2.2**
EBITDA	**(1.4)**	**(0.8)**	**(0.4)**	**(0.6)**	**0.8**	**0.2**
Margins, Leverage, Returns		**FY17A**	**FY18A**	**FY19F**	**FY20F**	**FY21F**
EBITDA		(2159.1%)	(516.7%)	(11.5%)	7.6%	17.6%
EBIT		(2171.2%)	(548.5%)	(34.6%)	(10.4%)	5.3%
NPAT pre significant items		(2701.7%)	(812.8%)	(26.7%)	(7.9%)	3.4%
Net Debt (Cash)		(752.4%)	(12.9%)	879.6%	890.4%	1000.8%
Net debt/EBITDA (x)	(x)	n/a	n/a	n/a	952.7%	335.8%
ND/ND+Equity (%)	(%)	54.9%	0.4%	(30.0%)	(31.5%)	(36.1%)
EBIT interest cover (x)	(x)	n/a	n/a	n/a	n/a	9.3%
ROA			(8.6%)	(6.8%)	(2.6%)	1.7%
ROE			(18.7%)	(6.6%)	(2.6%)	1.5%
ROIC			(12.0%)	(16.8%)	(9.9%)	9.6%
NTA (per share)		1.6%	2.3%	2.4%	2.3%	2.4%
Working capital		50.8%	1025.0%	787.3%	1066.7%	1441.6%
WC/Sales (%)		**525.8%**	**2392.3%**	**91.5%**	**86.6%**	**85.3%**
Revenue growth			343.7%	1907.1%	43.2%	37.3%
EBIT growth pa		n/a	n/a	n/a	n/a	(170.7%)
Pricing		**FY17A**	**FY18A**	**FY19F**	**FY20F**	**FY21F**
No of shares (y/e)	(m)	386	1,339	1,582	1,582	1,582
Weighted Av Dil Shares	(m)	271	493	1,625	1,625	1,625
EPS Reported	cps	(0.97)	(0.69)	(0.14)	(0.06)	0.04
EPS Normalised/Diluted	cps	(0.97)	(0.69)	(0.15)	(0.06)	0.04
EPS growth (norm/dil)		n/a	n/a	n/a	n/a	-159%
DPS	cps	-	-	-	-	-
DPS Growth		n/a	n/a	n/a	n/a	n/a
Dividend yield		0.0%	0.0%	0.0%	0.0%	0.0%
Dividend imputation		30	30	30	30	30
PE (x)		-	-	-	-	116.1
PE market			15.2	15.2	15.2	15.2
Premium/(discount)				-100%	-100%	664%
EV/EBITDA		- 11.2	- 24.9	- 58.6	61.8	-
FCF/Share	cps	-0.7	-0.4	0.3	0.1	0.1
Price/FCF share		- 6	- 11	15	46.6	27.8
Free Cash flow Yield		(17.5%)	(9.1%)	6.5%	2.1%	3.6%

Source: RaaS Advisory

FINANCIAL SERVICES GUIDE

RaaS Advisory Pty Ltd

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Corporate Authorised Representative, number 1248415

of

BR SECURITIES AUSTRALIA PTY LTD

ABN 92 168 734 530

AFSL 456663

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Research as a Service

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- our services
- how we transact with you
- how we are paid, and
- complaint processes

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