



Andrew Peller Ltd. Takes the Big Gulp

Description

Any time you take out your cheque book and write the number 95 with six zeros following it, you're talking about a big deal.

Andrew Peller Ltd. ([TSX:ADW.A](#)) did exactly that in September, agreeing to buy three B.C. wineries for \$95 million: Black Hills Estate Winery, Gray Monk Estate Winery, and Tinhorn Creek Vineyards, all located in the Okanagan Valley. The trio of acquisitions are being paid for with \$17 million in company stock and the rest in debt. All should have closed by now.

Lately, Peller has garnered some positive press from analysts.

On October 10, the *Globe and Mail* reported that Acumen Capital Partners analyst Brian Pow, the first investment professional to actually cover the small-cap winery based in Grimsby, Ontario, has a buy rating on the stock and a 12-month price target of \$14 — 15% higher than where it's currently trading. The paper also suggested that at least one more analyst's coverage is imminent.

Industry consolidation continues

Pow believes industry consolidation in Canada will continue for the next few years, and Andrew Peller is primed to be at the front of the line when it comes to future acquisitions. Well capitalized and sporting a dual-class structure, which gives the Peller family voting control, the pedal is to the proverbial metal.

Not only will acquisitions help Andrew Peller grow, but it's also increasing revenue per litre of wine by reducing the number of lower-quality wines it sells and increasing the number of higher-quality wines and price points it offers its customers.

"Our company and my family feels good about the 20- to 30-year horizon for the industry and we're prepared to make significant long-term investments to make this happen," CEO John Peller told the *Globe and Mail*.

Another industry professional who's high on Andrew Peller is Peter Hodson, the founder of Kitchener-based 5i Research and owner of Canadian *Moneysaver* magazine. He views Andrew Peller as a diamond in the TSX rough that does nothing but generate positive cash flow while flying under the

radar.

Last November, I [suggested](#) investors buy Andrew Peller stock to hold until the Ontario Teachers' Pension Plan (OTPP) acquired the winemaker to pair with Alterra Wines, the Canadian wine assets it bought from **Constellation Brands** in December 2016. OTPP paid \$1.03 billion for Jackson-Triggs, Inniskillin, and the Wine Rack retail stores.

Could the roles get reversed?

I believe they could. Here's why.

Although it's early days in OTPP's ownership of its Canadian wine assets — private equity often has a three- to five-year holding period — it's not unheard of for deals to turn around in less than a year when the right strategic buyer comes along. It doesn't happen that often, so the more likely scenario is that both parties continue to operate business as usual for the next 12-18 months.

Let's assume at month 24 of its ownership, OTPP puts a \$2 billion valuation on its trio of assets. That's a big return for a two-year hold, but it's probably not too far off what it expects from any private equity investment it makes.

Andrew Peller has approximately \$123 million in debt, including the \$77 million used to buy the wineries out in B.C. To buy Arterra, it could use 20% in stock and borrow the rest, leaving it with around \$1.8 billion in debt. That's seems impossible until you consider that OTPP paid 12 times EBITDA to buy the assets.

So, that's \$86 million in 2016 EBITDA. Two years down the road, we might expect that to grow 15% annually to \$114 million. Andrew Peller's is currently around \$42 million. Put them together, and you've got \$156 million to cover approximately \$100 million in interest payments.

It would be a tight squeeze, but it's a definite game changer for both Andrew Peller and the Canadian wine industry.

It probably won't happen but they said the same thing about Constellation buying Corona in the U.S., and look how that's turned out.

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