

The Chinese wine wagon

Alan Kohler February 1, 2018 *CEO Interviews*



Today's Interview with
the CEO of ASX listed:



Piers Lewis is the CEO and Founder of Dawine. He lives in Perth and started the business a couple of years ago with the idea of selling wine into China. Not that he had much experience in the wine business, he was a corporate advisor, but he says he was passionate about wine and thought that it would be a good idea to sell to China.

The stock is selling at just under 1 cent and the market cap is just under \$4 million. About the most micro of micro caps you can get, but it's just begun, it's an absolute genuine start-up. What's it got? Well, that's how I started the interview, what have you actually got? What's your asset, Piers? And the answer in short is that he's got all the regulatory approvals for selling wine into China. That's the asset, really. He's got a warehouse in Shanghai and he's got a shop in what's called Tmall, which is a part of Alibaba.

He's now selling wine, not much yet, but it's a very cheap, interesting, early stage play into China's transformation, as it were, in the wine business. Obviously, the biggest Australian player in the Chinese wine market is Treasury Wine Estates, which is doing really well in China but if you're interested in the potential for real growth – I mean, obviously Treasury Wine Estates is a big company, one of the greatest wine companies in the world, really. That's not something you could accuse Piers and Dawine of being.

But look, it's pretty cheap and has potential, that's for sure. Interesting play, so I think it's well worth a listen to the interview and to consider the company.

Here's Piers Lewis, the CEO of Dawine.



Piers, tell us what Dawine's assets are, what have you got?

I guess what we've got that's probably unique to us is quite a bit of the licensing which takes some time in China. When we setup the company probably four years ago now, we spent the first two or three years really getting I guess all the red tape and regulations in order which is sometimes, I guess, the other way around to how some start-ups do it, but we thought we'd get all the boring stuff out of the way first. Getting the business licence, the liquor licence and the import licence and the food circulation permit, they call it, is quite a big procedure and you've got to setup, from an Australian point of view, a wholly owned foreign entity, a 100% entity in China that we own. Getting those items done took quite a bit of time and effort and that's quite a big asset that we've got.

Did it cost much?

It didn't cost a lot of money, maybe \$80-100,000 Australian dollars with the advisory fees, so it wasn't a massive capital outlay but the timing of it took a good 18 months from when we first went into it with earnest to completion.

And you haven't had to do a JV with somebody in China?

No, and that was a big thing for us, we really wanted to have 100% control of our subsidiaries and control of our own destiny. Actually, when we started it it was told to us that you would have to go into a JV with a China group, but under the new leadership it's become a fair bit easier for foreign entities to, I guess, get started in China. Now you can go with a wholly owned foreign entity.

Tell us a bit about your own background and what led you to start this process?

Yeah, sure. I'm a corporate advisor before I got into Dawine, but I've been a very passionate wine lover for many years and inherited that from my father who's a passionate wine lover. I've always sort of grown up and known wine. Being a corporate advisor, I was interested in the China market and obviously during the boom days, Chinese investment into resource projects was something that piqued

my interest. I guess it was more of combining a few of my passions and then a corporate advisory business in China and red wine.

Yes, some time ago I looked into the idea of being able to sell wine in China and I guess my background is to sort of dig into things quite deep and understand how it works. For quite a time we looked into, was it actually possible, could we actually do this? And the further we got into it and closer we got, the more exciting it became.

As well as the regulatory approvals, have you got any distribution deals now?

Yes. What we've setup, our other assets I guess, is we've got multiple online sales channels into China. Obviously, we're an online wine business. We don't have any physical stores.

You do have a warehouse, don't you?

Yeah, we do. We have a warehouse in the free trade zone in Waigaoqiao in Shanghai, so we do have a physical presence and an office but we don't have a store where you can walk in and buy a bottle of wine. It's an online only business. China's similar to the western world in many ways, in how they sell online, but it's also different. We'll setup what they call a Tmall store, which is actually quite a rigorous process to get that approved, especially when you want to put a new bottle of wine on, they're very much trying to prevent them selling fake wine on their service. Going through the process to get your wines on Tmall is just quite a big job. We also have a website obviously, an app, and they're our main sales channels at the moment.

What about your supply agreements, what have you done on the supply?

We've got some supply agreements with some wineries. We see ourselves as a curated wine approach, in that we go looking for wine ourselves rather than wineries coming to us. We have a tasting panel, we sit around and taste the different wines that we think will be right for the Chinese palate and then the ones we like, we then speak to the wineries and see if we can organise a supply deal. We've got one that we announced last year with Vasse Felix who's, as you may well know, a long term quality supplier out of the Margaret River and they've been very good to work with.

But as I said, a curated approach. China already buys a lot of the bigger names in the Penfolds, Wolf Blass's and Jacob's Creek, so we don't really want to supply those wines as much, it's more about finding hidden gems for our customers.

You seem to be on and off the list, you were in suspension and then you're back on. I'm losing track of whether you're suspended at the moment or not, what's the answer?

No, we're trading again. There was a large deal that we were working through that came about the end of November, early December with a partner in China. Due to some regulatory issues with that, the partner had to stop working on that deal and we've had to try and restructure that which we're working on at the moment. It was a bit of an unusual one in that we went into trading halt and then obviously you only get a few days for that and then into suspension. We kept working with the partner and they were saying, yes we're almost there, almost there, but we never got to that final signing stage.

We're still working with that partner and what's interesting in those events is that I guess you sort of push a little announcement out that you are looking at a deal so other people come knocking on your door. And as I put out in the announcement when we came back onto the boards, we are working through the partner and we have some other interests from other partners as well, so we're working through that at the moment.

What do you mean? What sort of partner are we talking about? Because your market update a couple of weeks ago described it as a strategic investor, and you're also looking at other strategic partners/investors. Is this about raising money?

It's partially about raising money, it's not all about raising money. We feel a good way to build sales and that distribution in China is to work with a Chinese partner. The wine industry up here is very hot topic at the moment and wine is becoming more and more popular. There's plenty of partners out there that I guess would like to get involved in the wine industry, especially an ASX listed wine company because there's only a few of us. So there's been a lot of interest in that regard but why we're looking at it is it's something that will open up distribution or business models that work with us in synergy.

There's a couple ideas that I can't talk about at the moment but we think would be very interesting and very exciting for the Chinese market and we could help if we work together with a strategic partner.

How much cash have you got now?

We've got a quarterly coming out probably in the next day or so, I can't say anything too much at the moment. I guess it depends when this comes out, Alan.

Okay, what did your last quarterly say?

Our last quarterly there was about \$2 million. I would expect it's around the \$1.5m mark.

What's your cash burn rate now?

It's between \$4-500,000 a quarter.

What's that money going on?

I guess it's marketing and the purchase of wine is our two biggest costs usually and I guess working capital, so staff costs, admin costs.

Have you got many staff? I noticed that you just hired someone in Beijing or in China to handle the marketing?

Yeah. Full time employees, there's not a huge number. We've got obviously warehouse staff in China. We've got a Chief Information Officer based out of Sydney who's looking after all of our technological requirements. We obviously have myself and someone in logistics. There's a reasonable staff base but it's under control and I guess we're trying to keep it at the right size for where we are.

Let's just kind of sum up where you're at then. Are you saying you've got all of the regulatory approvals that you need?

Yeah, we're selling wine in China at the moment.

Have you got a Tmall store?

Tmall store is operational and selling and that's our biggest seller at the moment.

And what about Alibaba?

Tmall's Alibaba.

That's Alibaba, is it?

Yeah, I guess it's the equivalent of Amazon in China. There's other sales channels such as JD.com, but we haven't gone down that route yet. We also have a WeChat store. I'm not sure if you're familiar with WeChat but you can now open stores on WeChat, so we've also got a WeChat store.

I'm not familiar with any of it, let's face it.

[Laughs] WeChat's China's Facebook I would say, the closest comparison. But it probably does a lot more than Facebook does. As I said, you can actually run an online store through your WeChat account in China.

You're saying you're selling wine now through Tmall, are you?

Yep, through Tmall, through WeChat, through our website and through our apps.

And how are you doing delivery and fulfilment?

It's a third party provider. Two major courier companies that we use just to dispatch and that goes nationally throughout China.

Can you give us a sense of how you're going? Are you sort of on plan? How many cases are you selling?

Our revenue figures are increasing quarter on quarter, which is what you want to see obviously with a business like this. We're tracking to where we want it to be at

this stage. I think in the last quarter we had revenue of just under \$90,000 Australian dollars, but keep in mind that's probably the first real quarter we had the stores operational. That was tracking, I guess, where we wanted to. This quarter we hope will be an increase on the last quarter, which would obviously point that we're starting to get the marketing right. That's what's key for our business at the moment, is getting the marketing right in China. It's a challenge.

When you're an Australian company doing business in China you try not to pretend that you're working in Australia still, because things that work in Australia do not work here. We haven't spent a great deal on marketing in China yet because we were really keen to make sure our marketing strategies were working. As with a lot of marketing strategies out there, you try quite a few different ideas. The ones that don't work, you don't pursue and the ones that do work, you throw more money at. We're now obviously going through that evolution of that marketing strategy again and again and we're learning every day.

And I presume the strategic investor/partner that you're talking to is a part of that?

That's right, yeah, definitely. As I said, there's a couple of parties interested at the moment and there's some different business models available, some that are very complementary to what we're doing, some that are a little bit different but I believe have merit for us to become, for example, an exclusive supplier to their new business model, which would be a good result for us if we were to do that.

But with these discussions you've got going on, are you going to also raise some cash?

Yeah, that's obviously for them to get involved with us they'd like to be part of the story and have some skin in the game, as such, as well from our point of view would be a good thing. Capital is definitely part of the process and given the scale that some of these parties are talking about, then significant capital will be required to just market what they're trying to do. Yeah, I think if negotiations are successful there'll be a capital raising that comes with it.

Well I imagine, apart from everything else, you'll need it because otherwise you'll run out of money?

[Laughs] The cash balance is pretty strong still but as with companies that are in the starting growth stage, capital raising is a part of life. No doubt, we'll need to raise money at some stage.

And how much of the business do you own Piers?

I've got a reasonable percentage, I think it's just over 6% of the company. I'm one of the major shareholders. We don't have anyone who has a big chunk of shares. I guess myself and the co-founder, Norman Lip, have a similar amount of shares.

It's pretty widely held then, is it?

Yeah, that's right, number one shareholder is a fund out of Perth. I think they have 8 or 9% from memory and then there's Norman and myself and two and three. Then the top 20 does hold a reasonable percentage but there's no one shareholder that has a controlling stake or anything like that.

You're obviously not paying yourself very much, I presume there's a fair bit of performance shares to be earned, is that right?

That's right. Yeah, I've put myself on what I think is quite a low wage for the job that's being done, but yes, it's more about the equity from my side. I'm not here for the salary, that's for sure.

And tell us about the wine that you're selling, is it all Australian or are you getting it from elsewhere as well?

No, it's foreign wine, we call it, into China. Predominantly it's Australian and French. We're close to getting some Chilean wine into the country as well. The top three selling wines in China are France by quite a stretch, then Australia, then Chile. We are seeing growth in the Australian market share and the free trade agreement getting more and more in place is making it more competitive as well.

What sort of margin are you getting and how will that go in the future?

I guess it depends on the product we're selling. Typically, I guess the margin ranges from 40-60% as a general rule. That comes down to obviously what we can source the wine for and what we can sell it for, that's obviously basic but it does depend on which wine we're selling. The margin on the French wine is a bit tighter than some of the Australian wines. The French negotiators are slightly harder to deal with than the Australian producers.

[Laughs] I'm not that surprised.

As you'd expect.

As you'd expect. But I presume also if you start moving volume you'll get a better price?

Yeah, absolutely, and that's the case definitely when you buy economies of scale and the more you buy, obviously the cheaper the price will get. What a lot of other producers are telling me which is interesting is that it's not so much, come here and I want to buy two containers of your wine. It's more, if you come back every year and are consistent and I know that I can produce wine and you're going to buy it, then that for them is a much more attractive option than – because there's plenty of examples of Chinese people coming to Australia and buying a container and next year they don't buy anything, the year after they buy three. That inconsistency is a nightmare for production. If we can become a consistent purchaser of wine, year on year, then that's definitely going to help us on the cost side.

What about the name, where did that come from? Has it got to do with the Chinese translation of Dawine?

Yeah, Da in Mandarin is sort of grand, superior or great, and obviously wine's a western word. In Chinese, it's Da-jiu – jiu, being the wine. Yeah, it's really grand, great, superior wine is what it loosely translates to. Don't ask me how we came up with the name, it was Norman and I sitting in a room and neither of us can remember who actually came up with it. We were just looking at words that worked with wine and that one stuck out.

The key to it is to replace the stuff they already drink which is – what's it called? It sounds like Da-jiu?

Baijiu?

Baijiu, yeah. Gradually, we're weaning Chinese people off that stuff and onto wine, is that what's going on?

Yeah, that's a strong push over here at the moment. The baijiu is not very good for your health and it's reasonably alcoholic. Maybe it's an acquired taste but it's not for me at the moment. I think obviously the Chinese public are getting used to red wine, for them it's new and a different taste to them, but obviously the health properties of wine compared to what they're drinking is a big selling point at the moment. The taste is obviously – once they're acclimatised to it, it will be much better for them as well and they'll see the wine journey you can go on with different flavours and varieties.

Some of the baijiu is very cheap, so sometimes it's very hard to compete with that, but I think given the health properties and the taste, we're seeing obviously a lot of growth and that's reported everywhere. That's the key, if people are going off baijiu and onto wine, there probably won't be enough wine in the world.

Well, I suppose that's the holy grail, isn't it? That's the pot of gold at the end of that particular rainbow.

Yeah, flying into Beijing last night, you look out the window of the plane and you do get constantly reminded how big China is and how many people there are here. It's inspiring to see what is out there and what's possible. When you go out to dinner or you're walking around especially the tier 1 cities here now, there's wine bars popping up everywhere, there's wines on almost every menu you go to, it's definitely becoming a part of their culture and gaining traction every month. We're very excited to be here and we see the future as being very bright.

Do you think you'll be selling it direct to homes mostly or to restaurants and bars?

Yeah, that's an interesting question. We'll position ourselves at the moment as retail to homes, and that's where a lot of our customers are from. Obviously, and it's a badge of being an ASX listed company is what we've seen is a lot of people

approaching us for wholesale wine opportunities which would include restaurants, bars, hotels, even just large corporations are getting interested in what we're doing. That's an angle we see as being a bit different than we're chasing. We did do the Elixir Festival in October and that's quite a big group that runs that and they have a big database.

It was quite an interesting exercise and it sort of opened the opportunity to work with corporations as well with their large databases. We are working again in the background on a couple of potential deals there which will be really, really exciting and interesting for us and our shareholders.

Your shareholders are having to be patient, aren't they? I mean, you're definitely flying under the radar. This morning your market cap slipped under \$4 million again, so are you disappointed with all that or you think that the shares should have performed better?

Obviously, I believe the price is not a true reflection of where we're at, so yeah, definitely want that to be higher for everyone. I don't think that will be the case for a long time and my view on share price is there's a lot of people trying to do whatever's hot in the market at that time but I believe a true business will come through and when our revenue figures continue to grow I think people will start sitting up and taking notice.

That was Piers Lewis, the CEO of Dawine.

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