Endeavour Group Limited, FY 2022, Earnings Call 2022-08-23

Presentation

Steve Donohue

Thanks, and good morning, everybody. I appreciate you all joining us for Endeavour Group's Financial Year 2022 Results Announcement. As mentioned, I'm Steve Donohue, and I'm the Group CEO and Managing Director for Endeavour Group. And I'm joined today by Shane Gannon, our Chief Financial Officer.

I'd like to begin by acknowledging the Gadigal people of the Eora nation as the traditional custodians of the land on which we gathered today and pay my respects to their elders past and present. I also extend that acknowledgment and respect to any Aboriginal and Torres Strait Islander people listening in today.

Before I step through some of the details of our results, I wanted to just take a moment to acknowledge that it was a really tough year, not just for us at Endeavour Group but actually for everybody throughout Australia.

We had a continuation of the COVID-19 pandemic, which brought the challenges of further lockdowns and restrictions. And on top of that, we had devastating floods. And for many Australians, this was also a time when they became unfortunately disconnected from family, friends and their communities. That's part of the reason why we take our purpose of creating a more sociable future together so seriously, and it's also why we're really excited to play our part in creating products and places and experiences that bring people back together. Something I'm happy to report, we're seeing more and more of in our hotels right now.

I'll step through to our group highlights for the 2022 financial year, which Shane will expand a bit on – a bit later in the presentation. Overall, the team delivered a strong financial result that reflected the resilience of our business and the natural hedge between our retail and hotel segments as well as the tenacity of our team.

Total sales were $11.6 billion, which was broadly in line with the previous corresponding period. EBIT was $924 million, up 2.8% despite the inclusion of new corporate costs, which were not incurred in F'21. And profit after tax rose 11.2% to $495 million. And importantly, the business continues to generate strong operating cash flow, which was $949 million for the period, allowing us to continue to invest while also delivering a full year dividend to our shareholders of $0.202 per share.

The dividend payment equates to a full year payout ratio of 73.1%, which is in line with our payout guidance of 70% to 75%, which we provided at the F '21 Annual General Meeting. If you jump forward to the slide reflecting our first year as a listed business, and you'll see that as it was our first year as an independently listed company, we did achieve a lot. Now the team certainly achieved a lot throughout the course of the year. I won't go through all the detail on that slide, but the key point is that despite the distractions of demerging and listing and everything else that happened throughout the course of the year, the team were able to maintain really positive momentum across the business.

A couple of things I'll call out, though, is that we've continued to enhance and expand our network, adding 32 net new retail stores and 5 new hotels. And at the same time, we've renewed 81 retail stores and 40 hotels. We also maintained our trend leadership and met customers evolving preferences through a commitment to innovation supported by strong partnerships with our suppliers and the expansion of our Pinnacle Drinks portfolio.

And perhaps most importantly, our team actually improved their customer engagement and satisfaction scores across all of our businesses despite the challenges of lockdowns, rapidly changing restrictions, trading restrictions, team shortages and supply chain challenges.

So we jump forward to the retail segment performance. The retail business achieved sales of $10.1 billion and EBIT of $666 million both broadly consistent with the strong COVID-effected performance experienced in the prior year. In the first half, our sales performance was assisted by the switch to at-home consumption, reflecting the various COVID restrictions that prevailed at the time.

In the second half, we saw the normal seasonal sales shift accentuated by the reopening of on-premise venues. And we also experienced an increase in supply chain costs through the second half. Looking beyond the impacts of COVID, some things were consistent throughout the year, such as customers continuing to embrace discovery and drinking better, driving the increasing popularity of craft and local ranges and the trend towards premiumization.

We also continue to build for the future, enhancing our digital customer engagement platforms and introducing new retail formats such as the seller by Dan Murphy's and Dan Murphy's new neighborhood stores. As a final note on our retail segment, I'd add that throughout the year, our stores and online – in our stores and online, I should say. We retained our focus on areas of profitable growth despite an increase in competitive promotional activity, particularly in the second half.

If you move forward to Slide 9 in the presentation pack and the drivers of our hotel performance, we delivered sales of $1.5 billion and EBIT of $315 million up 20.7% on the prior pandemic affected year. Of course, the most significant influence on the performance of the hotel segment, as was the case for our retail segment was the impact of COVID-19.

Over the course of the first half, there were only about 30% of days where all of our hotels were open. And beyond impacting our financial performance in the half, this also placed extraordinary pressures on our team with multiple closures and openings through the period.

In the second half, after an initially slow start due to the Omicron outbreak, customers began enthusiastically coming back to our hotels, and this led to very strong sales and a financial outcome in the period with solid contributions across gaming, beverages, food and accommodation. This recovery was, however, not without challenges, particularly the continuing issue of team shortages.

Overall, it’s been a tough but rewarding 12 months for the hotels team, which makes it particularly pleasing to see our Voice of the Customer measure improved on the prior year, an outcome that speaks volumes about the exceptional commitment of our frontline team members.

Stepping forward to the slide talking through our digital business. A key part of investing for the future is building out our digital and data capabilities, which unlock efficiencies across the business and also drive significant new growth. When it comes to efficiency, we know there’s an ongoing opportunity to enhance our pricing and promotions capability by leveraging data to help make better decisions. And we equally think that there remains a great opportunity for us to unlock growth through expanding personalization.

In particular, we think there’s opportunities to continue to drive online sales, unlock unique and accessible marketing opportunities and diversify our revenue streams. These opportunities are underpinned by the strong foundation of our 4.5 million active My Dan’s members and around 260,000 monthly active users of the BWS app, both of which pleasingly continue to grow.

In F ’22, online sales grew 17% to exceed $1 billion for the first time. And importantly, online sales are increasingly profitable in F ’22, driven by scale, operating efficiencies and more premium baskets which are being driven by more personalized offers. We also expanded our online customer offers in the year with the launch of Dan Picked, our new subscription offering and the innovative Dan's Gifting Hub.

Our investment in digital isn't limited to our retail business, though, hotels, though earlier in their journey, have now seen more than 3.7 million order and pay at table transactions following the rollout of this service through the year.

On to Pinnacle and our F '22 highlights. As a reminder, of course, our Pinnacle team create, build and manage a portfolio of drinks brands, which is sold for Endeavour Group's channels and also through key strategic distribution partners. In the 12 months of the reporting period, we launched 479 high-quality new Pinnacle products, and I emphasize the word quality here, given our strategy to premiumize our portfolio in line with customers' increasing preference to drink less but to drink better.

And the quality continues to be recognized by third parties. In F '22, Pinnacle wines received over 560 awards, including 19 best-in-class trophies. Some of our wines deserve special mention, and I'd like to call out a couple. Firstly, The Ethereal One, Grenache 2020, which is only about $15 a bottle and was the first Australian wine to win the International Grenache Trophy of the 2022 International Wine Challenge, and of course, one of our flagship wines, the Oakridge 864 Chardonnay 2019 Vintage, which was awarded equal top rated Chardonnay at the 2022 Halliday Wine Companion Awards.

While those awards are great to receive, the most important thing is that customers love Pinnacle products with over 70% of our customers having purchased something from the Pinnacle portfolio in F '22. To further emphasize our commitment to the growth of this business, we expanded our premium wine footprint with the acquisition of Josef Chromy Wines in April 2022 and more recently shingled back line earlier this month.

And just before I hand over to Shane to talk the numbers, I just want to touch on the update we've provided today on our sustainability journey, and we've got some good early progress to share. I think everybody knows that at Endeavour, we're committed to leaving a positive imprint on each other and on the communities we serve.

And in October last year, we launched our first sustainability strategy, which was central to our purpose of creating a more social future together. Today, we released our first sustainability report, which details our progress to date. I won't read out all the examples of progress on that slide, but just to highlight a couple.

In F '22, we established our own program of leading in responsibility training. We want all of our team members with their frontline team or support team members to do that sort of training and this, in particular, because it's a key part of embedding a deep culture of responsibility right across the group.

We're also placing greater importance on community engagement, whether that's through our ESG reviews of all acquisition opportunities or through the increased community consultation that we're generating with the help of groups like our new Darwin Community Advisory Committee, which is a panel of diverse community leaders that are working with us up in Darwin.

I'd encourage you to read the report alongside our first modern slavery statement, which was also published today.

And now I'd like to hand over to Shane, who's going to go through the financial aspects of the results in more detail. Over to you, Shane.

Shane Gannon

Okay. Thanks, Steve, and good morning, everyone. I'm very pleased to be able to share with you our F '22 financial results. Our first full year results as an independently listed business. Endeavour Group's financial results demonstrate our ongoing focus to ensure sustainable earnings and distribution growth combined with maintaining a strong balance sheet.

The balance sheet positions us for long-term stability and equally provides financial capacity to support our development and growth opportunities, both short and longer term. As you can see from the financial result highlights, we delivered strong results in F '22. Steve has already stated, this is particularly impressive in light of the challenges we experienced trading through COVID and severe and disruptive weather events.

I will not go through everything on the slide, but select as a group, notable highlights. First of all, the sales of $11.6 billion, in line with the previous financial year's elevated levels and is up 15% on financial year '19, the last non-COVID full year comparative period, and our earnings per share of $0.276 per security and 11.3% improvement on the prior period.

We declared a dividend has declared a $0.077 per share final dividend. When you combine this with the interim dividend, it equates to $0.202 per share distributed to our shareholders in the year. Our strong cash and capital position represented by operating cash flow of $949 million in the year and debt headroom of just under $1 billion.

We continue to invest in the growth of our business, both short and long term, while achieving a return on funds of 11.4%. Turning now to the group profit outcomes. As mentioned earlier, we have delivered a strong group performance with net profit after tax, up 11.2% on the prior year. Underlying this at a group level, EBIT $924 million represents a 2.8% improvement on the prior period.

Dissecting the 3 key segments of our operations. The strong performance was underpinned by the retail segment, where we maintained EBIT $666 million, which is in line with a very robust F '21 result we achieved. Our EBIT from the hotel segment, $315 million was $54 million higher than F '21, primarily reflecting the recovery in the second half of the year as COVID restrictions were removed.

And other EBIT segment result, which is predominantly corporate cost was negative $57 million. This is in line with expectations set out at the time of the demerger from Woolworths Group and represents our first full year of trading independently. The finance costs were reduced by $42 million, where we benefited from the lower interest rates we locked in at the time of the demerger.

As we communicated at the time of the demerger, we intended to and we have continued to invest in line with strategy, including building a strong technology infrastructure to underpin the Endeavour business. This investment, including enhancing our digital platforms and stand-alone technology is increasingly expensed within the P&L.

Turning to our next slide and focusing on the retail segment performance. Our retail sales in F '22 were broadly in line with F '21 with COVID impacting both years. Looking through the impact of COVID, sales have grown strongly over the medium term and are up 19.3% on F '19, which was the last pre-COVID comparative period.

Retail gross profit margin, 23.2%, represented an improvement of 89 basis points compared to F '21 and was underpinned by the premiumization which was spoke of before, a shift to higher-margin new products, the demand for Pinnacle Drinks products and a lower level of promotional activity in the market.

The margin gains were strongest in the first half, driven by the lockdowns of hospitality venues, positive consumer trends and reduced competitive promotional activity. The second half saw an increase in supply chain costs and an increase in promotional activity compared to the first half. Our cost of doing business as a percentage of revenue was 16.6% increased by 86 basis points when compared to F '21.

The increase primarily in the second half reflects seasonal deleverage as fixed costs are fractionalized over a longer – lower sales base. The second half increase also reflects the higher levels of operating expenditure in the technology, which I called out in the previous slide.

During the year, we also experienced other cost challenges due to COVID-19 impact, staffing constraints, severe weather events and normal salary and wages inflation. Importantly, our efficiency initiatives, such as our successful Simpler for Store program, we're able to deliver productivity savings to mostly offset these cost challenges.

Now moving on to our hotel segment. The hotels posted a strong result considering the extensive challenges encountered, particularly across the first half of the year. And the key points to highlight here are sales for the hotel segment were $1.5 billion, 6.6% ahead of F '21, and that reflected the more extensive COVID-related closures in F '21.

The gross margin remained stable at 85.1% and the cost of doing business as a percentage of sales, 64.2% improved by 236 basis points, and that's just benefiting from higher sales and therefore, improved operating leverage, combined with some cost management term programs. The higher sales flowed through to deliver a much stronger EBIT at $315 million, which was 20.7% higher than F '21.

I should call out, looking forward, we expect hotels to continue to recover in F '23. Beyond normal operating costs, we remind investors that changes to the Victorian gaming taxes and gaming machine entitlements will have an impact on our P&L in F '23. We estimate this to be in the vicinity of $20 million at an EBIT level.

Looking at headline, sales performance of our 2 trading segments side by side just demonstrates the natural hedge we have experienced across the pandemic and highlights the resilience of the group. Retail sales remained well ahead of pre-COVID up 19.3% over 3 years, whilst hotels were down 7.9% over the same time frame.

Moving on to cash and liquidity. Endeavour is a highly cash-generated business. Our cash realization ratio in F ’22 was 93%, reflecting the strong operating performance and disciplined approach to cost management. The cash realization ratio is lower than last year, but it’s primarily due to payments relating to historical payer remediation and the timing of income tax payments made in F ’22.

We retain a strong funding position with net debt of $1.2 billion, which is actually $56 million lower than the end of F ’21. And as I mentioned before, we have significant head-room with undrawn debt facilities of $985 million, as well as some material cash balances as well.

Looking at the return to shareholders. We recently shared our capital management frame-work with the market. The slide updates for our performance in F ’22. You may recall, as I described at our Investor Day in May, we are fortunate to start in a very good place with a well-capitalized balance sheet and a business that’s delivering strong operating cash flow.

The strength of the framework starts with a strong cash realization. This has allowed us to sustain our core business and invest in a range of short-, medium- and longer-term growth opportunities while at the same time maintaining our investment-grade credit metrics. We also delivered substantial distributions to shareholders, equating to a payout ratio of 73.1% for the year.

In F ’22, the business demonstrated its resilience in tough times and its ability to sustain growth and create shareholder value by; we’re growing our EBIT ahead of sales, delivering a return on funds employed of 11.4%, earnings per share growth of 11.3%, and a dividend yield of 3%, which is fully franked.

Now the capital expenditure. We invested $349 million in capital expenditure in F ’22, which is up $37 million compared to F ’21. We have continued our successful renewals program, completing renewal projects at 40 hotels and 81 retail stores. We made further investments in the electronic gaming machine fleet, reducing the average age of the portfolio to 6.8 years, which is significantly reduced from the 9.6 years at the beginning of F ’21.

We have grown our network through 32 new retail stores, the acquisition of 5 hotels and as Steve mentioned, we continue to invest in our Paragon Wine Estates business. This year, we acquired Josef Chromy Wines in Tasmania. And after the balance date, we acquired the Shingleback Wine in McLaren Vale.

We have also invested in our endeavourX and digital capabilities in line with our strategic priorities. This represents a smaller portion of our capital expenditure but as I indicated earlier, a growing portion of technology and digital investments are operating expenses performing part of our cost of doing business.

So looking forward, our investment plans for F ’23 and beyond remain consistent with the strategy we spoke to at our Investor Days in May. We will continue to invest to enhance our leading customer offer in both our physical and digital networks. We are in the early stages of unlocking the major property development opportunities.

Progressively, we will keep you informed of our progress in this regard, and we are accelerating our program to develop stand-alone technology platform, which is likely to increase both our capital and operating investment levels in F ’23.

In closing, I wanted to provide a case study of our renewal program and the return profile that we achieved with this type of investment program. We undertook the renewal of the Sunnybank Hotel, which is in Queensland, back in March 2021, and we completed the project in July the same year.

Total investment in the hotel renewal project was approximately $3.1 million. That renewal involved upgrading the dining room, patio and sports bar, the renovation and extension of the gaming room and transforming office and storage space in the customer areas.

At the same time, we coordinated upgrades to the co located Dan Murphy's store and BWS drive-thru. Since the renewal, we have seen food and bar sales increase by greater than 40%, and the gaming room is now one of the most successful in Queensland. Overall, the renewal has already demonstrated a return on investment, which is well above our expected 15% hurdle rate, underlying the opportunity for organic high-returning, relatively low-risk investments existing within the group.

Before I pass back to Steve. In closing, I would also like to recognize and thank the Endeavour team for their achievements since the demerger. In addition to continuing to manage and excel the core operations of Endeavour, we have also well positioned the company for future success as an Australian publicly listed company. Thank you.

Steve Donohue

Thanks, Shane. I just want to step this forward now to talk about how we're traveling so far in F '23. So we're on Slide 24. I think the first thing to recognize is that the growth rates on a year-on-year basis are going to continue to be distorted by the impacts of COVID in the prior year. And that's why we've got the F '20 comparisons on that slide for you.

The key message here is that both businesses continue to grow strongly, with sales for the first 7 weeks in both hotels and retail, up 13% when compared to the same corresponding period in F '20, which is the most recent pre-COVID comparative. We didn't have COVID at that time.

And in comparison to F '22, though, what we are seeing is the retail sales moderating from

F ’22 COVID elevated levels and customers returning to a more normal pattern of in-store purchasing along with a shift back to local convenience. And that means that we’re seeing some short-term moderation in our online penetration. And our BWS stores are slightly outperforming Dan Murphy’s at the moment and cycling through the past-COVID demand spikes, where Dan’s actually got the bigger lift.

And of course, hotels are continuing their strong recovery consistent with their performance in the second half of F ’22 as thankfully, Australians are able to embrace the opportunity for social reconnection in the public, which is a great thing.

I’ll step forward on to our priorities for F ’23. Firstly, we’ll continue to maintain our disciplined approach to cost management and look for opportunities to optimize the group operations to offset the impact of the well-known inflationary pressures. Secondly, we’ll continue, as we spoke about at our recent Investor Days to unlock value from our property network via renewables and redevelopments, and Shane’s touched on that.

We’ll remain focused on improving customer experiences through our ongoing investments in the digital data spaces. We will also continue to work on our technology transition across from Woolies as we set up our own stand-alone capabilities. And most importantly, we’ll continue to embed the Endeavour culture focused on our purpose and our values. We’ll keep progressing on our sustainability ambitions. And we’ll always strive to leave a positive imprint on the communities we serve.

So just to wrap up in summary on the last slide. We’ve delivered a strong F ’22 financial results built on a resilient business and an adaptable and agile team. The performance of our retail businesses matched the strong performance of the prior year. While the hotel performance was as expected, severely impacted by COVID-19 lockdowns and restrictions before it recovered strongly in the second half.

During the year, we continued with disciplined investments for the future, focusing on expanding and renewing our retail and hotel networks, enhancing our stand-alone technology capabilities and improving our digital platforms.

In the current context, it's been hugely encouraging to see the return of people seeking social connection and celebrating social occasions again. It really does feel like things are getting back to normal.

When we look forward, we know that the operating environment is not without its challenges, particularly the increasing cost of living pressures for our customers. We have to see how that plays out fully, but we remain focused on delivering great experiences, great value, convenience and choice for everybody.

For us specifically, things returning to normal means that COVID-led elevated retail sales will continue to moderate from the recent highs and the positive recovery in hotels is expected to continue. That's it from us. Thanks for joining. I'd now like to open up to any questions.

Question and Answer

Operator
— ***Operator Instructions*** — Today's first question comes from Michael Simotas with Jefferies.

Michael Simotas
My question is on the operating deleverage in the retail business in the second half. I think sales were down about 1% year-on-year but EBIT down about 18%. I'll let someone else ask about gross margin, but I'd like to focus on the costs if we can. I think cost growth was about 5.5% in the second half on a cash basis. How do we think about that as a base for the go forward for the business?

It looks like you've got a couple more challenges coming next year, you've got an elevated wage increase from July, plus you've got additional OpEx associated with the system development. So how should we think about that flowing through into '23, please?

Steve Donohue

Yes. Thanks, Michael. It's a good probably big question, I suppose. I know it's one on a lot of people's minds. Shane touched on the way we've been allocating technology costs and that certainly played through the CODB line in H2. So there was more OpEx than CapEx previously. So there's a bit of a swing in that.

It's hard to actually exclude gross profit. I know you're talking about CODB, but the place where our supply chain costs manifest is in the gross profit line, and we've called out that we've had elevated costs there. There, as you point out to a variety of other things impacting the CODB line.

We're obviously adding the market with the appropriate adjustment we took to team wages, and that will also impact salary team members as well to a somewhat different extent, but nonetheless. So yes, you're right. We do have those cost side challenges.

To your point, though, about how we're going to manage it, there is movements in retail pricing off the back of CPI increases that have flowed through. And we've seen those price changes relatively well accepted, I would say, across both the market and customers. And it's a pretty regular feature of the drinks industry that CPI price increases flow through twice a year, once in August and once in February. So we just had the August ones flow through. So I guess the way we're feeling about the half ahead is that, yes, it will be challenging because primarily of the cycling of COVID from last year. But we do feel well placed to navigate those challenges with a variety of levers that we'll continue to manage for. Yes, I'll stop there. Did you want to add something, Shane?

Shane Gannon

Michael, just to underline a bit of what Steve is saying. So we are challenged with some of these cost increases like the wages that Steve referred to, but we – I think Endeavour has had a good success in terms of its efficiency programs or optimization programs, and that will continue. So a lot of our planning is around looking for efficiency in that space.

Equally, we have to recognize that we are committed to our digital and our technology transformation, and we make no apology of that we – not only for a stand-alone reasons, but we think longer-term benefits. The incremental cost on the technology in '22 transformation was $10 million. We expect that to be [lower] in '23.

The order of magnitude at this stage is in the $20 million to $30 million of additional costs in terms of that transformation. So that's just to give you a bit of a steer of that challenge. But what I would say, a lot of this is being programmed on the basis that we'll be able to find the ongoing benefits to of savings to offset that level of expenditure, and that's a work in progress.

Michael Simotas

Can I just ask a quick follow-up on flood costs. I think you called out $9 million previously. Has any of that been either recovered from insurance or a provision raised against it?

Shane Gannon

Yes. We've covered a small portion of it. There's still outstanding claims, which we're very confident we will see. But at this stage, we've taken a conservative position just flagged the norm.

Michael Simotas

Okay. So you've taken that through the P&L.

Operator

And our next question today comes from Bryan Raymond of JPMorgan.

Bryan Raymond

I might ask one on the hotels, I'm sure there'll be plenty of retail today. Just interested in the components of hotel performance in the second half, obviously, it was a very strong result. Just wanted to get a feel for where food and beverage sales are versus pre-COVID levels. Is that AGM mix still a bit under 50% of sales or certainly less than 50% of sales? And if there was any material cost benefits in the period. Just trying to understand that operating leverage is very strong in hotels.

Steve Donohue

Yes. Thanks, Bryan. I think the thematic that we're trying to talk to is things returning to normal. So we're really seeing a very balanced performance across what we describe as the drivers of hotel performance that is gaming, beverages, food, accommodation. And events too, we're seeing a really solid return in thankfully, light music and entertainment and those sorts of things.

So yes, it's kind of getting back to normal levels, which means that the parameters that we've talked to the market about before, in terms of mix and contribution and so on are pretty well as they were. I think it's really encouraging actually to see a balanced approach in hotels because they are a multifaceted entertainment venue, and we like them to be in a degree of balance, if you like.

Bryan Raymond

Steve, just a follow-up then. I mean, the second half earnings in hotels were $194 million to [H '19] albeit it was pre-AASB numbers at 100. Just trying to – and obviously, it's been very messy the last few years. Just trying to work out if the second half run rate, given we are getting back to normal, thankfully, is that something we should be using going forward? Or is there something we should be mindful of when modeling out hotel earnings contributions to the group going forward?

Steve Donohue

Yes. I think we've called out the impact that we're going to experience in F '23 of the Victorian gaming taxes that will be paid. So I think we've been clear about that, and you should — ***Indiscernible*** — to that. But yes, look, we are saying broadly, it's getting back to normal, but normal is pre-COVID. So you've got to cast your minds quite a ways back to see that. Yes, I wouldn't add anything actually. I think it's normality is what we're experiencing. But just note that gaming tax impact in F '23.

Operator

And our next question today comes from Shaun Cousins with UBS.

Shaun Cousins

Just a – questions on retail gross margins. Can you just talk a little bit about where you're seeing the benefits of ongoing Pinnacle penetration, ongoing premiumization, some of those seem to be offset by promotion. So can you just sort of dig into those? Do you think premiumization will continue when the consumer faces a higher cost of living and are promotions back at where they were pre-COVID? Or is there still some work to do, please?

Steve Donohue

I tend to think over the 30-odd years, I've been around the retail business that it's considered to be an affordable luxury for customers no matter what the economic cycle say. So it seems to be continuing to play out that way, Shaun, but we're not seeing a dramatic shift back in the growth of premiumization pursuit of craft, pursued of you, pursued of better for you.

And we're not talking about particularly expensive items at the unit price. So it continues

– whether it will continue is a good question for us to ask ourselves, but that's been an ongoing feature, certainly of recent times. And we're somewhat heartened by the continuation of that through August in context of what I talked about earlier.

So that continues to be the case. In terms of your question on Pinnacle, yes, we've – we're privileged to continue to be able to produce products that customers seem to love. We talked about 7 out of 10 customers actually enjoying a Pinnacle product through the course of the year. We know that our right with Pinnacle – to invest behind Pinnacle is very much linked to the level of quality that we're able to produce. So we're very focused on that.

And you asked the question about promotions in the market. We have called out that there has been increased promotional activity in H2, but it's not as pronounced as it was in a pre-COVID environment. So I think there's a degree of rational behavior generally out there.

The – there is, I think, a bit of a pursuit of customers in the e-com space that hasn't sort of existed perhaps pre-COVID. So we've been, I think, very lucky to have capitalized on the investments we've made in our digital platforms through October. We've come out the other side.

We kind of went into COVID with digital penetration at about 6%. We're coming into F '23 with it, not quiet at the 10% we saw in F '22, but pretty close to 9%. So we're on the back of pretty considerably increased sales, increased a lot of penetration. And more importantly, learnt a lot of our customers on the way through, if you think about the number of people that use them My Dan's card, the number of app users we've got in BWS, which gives us the opportunity to really improve our service and personalization and so on to those customers. So I think those things have paid off. But we've got that, and I think there's others out there that are probably trying to chase those customers.

Shaun Cousins

Great. And maybe just a follow-up on the cash flow. It's – has all of the pay remediation cash outflow that weighed on your cash conversion in fiscal '22? Has all of that been paid out? Or could that impact reported or impact your operating cash flows for fiscal '23, please?

Shane Gannon

Yes, I could. The provision balance at the end of June is a circa of $70 million. I think it's $71 million to be precise. So there's still some cash payments to be made to completely resolve that – the remediation issue.

Steve Donohue

I think I'd just add on that for the benefit of our team for whom this money is owed. We've made some payments in F '23 considerable amount and we're very focused on getting that money to our team members present and past as quickly as possible. So yes, we're not in – no interest in us hanging on to that money. We're very, very keen to return it to those that have earned it.

Shaun Cousins

So that should weigh on cash flow in first half '23.

Steve Donohue

$62 million.

Shane Gannon

$60-odd million is what we're forecasting for the current financial year F '23.

Operator

And our next question today comes from David Errington at Bank of America.

David Errington

Steve, look, I – and Shane, I'm a little bit still nonplussed despite the questions. I still can't quite get my head around. And as you know, I'm not a smart person, so I need it really dumb down, if you wouldn't mind. So if we can talk it really simplistic. And this is the gross margin and the cost of doing business because as I said, the stocks get – said, that the stock is getting hammered today, pretty much on the retail margin performance, not the sales, it's the margin. Your gross margin in the first half increased by 141 basis points. Your cost of doing business only increased by 62 basis points.

But in the second half, your gross margin was pretty flat. And your cost of doing business was up over 100 basis points. So clearly, everyone's – I'm trying to get my head around – I mean, there's been a couple of questions that had to go with it, but I still don't really based upon – I haven't got the handle on what's actually going on.

You basically mentioned that there wasn't promotions. Promotions are still pretty rational. You mentioned that there were some supply chains. There was some elevated costs that go into that gross profit line, but there's some other stuff there. So can you have a go because you're probably about $30 million shy in the gross margin line.

So I'd like to get an understanding because we're all trying to work out those costs. Are they going to be sustained? Are they one-off? Are they forward investments? But we're about $30 million short as to what would have been expected by us. And we're all trying to work out, just what's going on? What are they? What's impacting it, so then we can make forward predictions. As I said, I'm not real smart, I need a dumb answer. Can you have a go and dumbing it down as to what the components were toward that miss was, please?

Steve Donohue

Thanks, David. Yes, I'll do my best. I'm probably with you on the keeping it simple side of things. But we were probably impacted by supply chain costs a little bit later than perhaps some others in the market would be fair to say. And it was relatively acute for us in H2 relative to H1. So it's lumpy in that respect. The other lumpiness that you need to be conscious of is the very high performance in H1 given the operating environment COVID effective and all the rest of it.

So we had a somewhat abnormally high result in H1 and a contrast to historical performance, abnormally lower performance in H2, when you net that out across the year, the numbers have been explained. So supply chain would be the first 1, the impact of promotions, yes, that's right. It's not as acute as it was pre-COVID, but they are coming back.

We are seeing some more activity in the market in the second half, and that's prevailed somewhat into the current financial year. We talked about the technology investments, they have been not insignificant and they continued in the second half. They're continuing somewhat in '23. We're being very careful about the way we place those investments, but that is true.

So there's not a huge amount more to add. There's always a few different things that go on with mix and those sorts of things. Premiumization continued as I said before to Shaun. So I can't give you precision numbers on your [30] that you've talked about, but it certainly starts with supply chain costs in the second half.

Now your valid question, obviously, is what does that mean going forward? We're taking a really prudent approach to managing supply chain costs in H2. But we're probably – sorry, in H1 of the new financial, the current half. We're probably going to need to push some stock into our stores a bit earlier than we did last year.

Last year, it kind of flowed through just in time. There's all sorts of risks associated with supply chain this year when it comes to driver availability, pellet availability, team availability and DCs and those sorts of things. And of course, we procure our services from primary connectors part of Woolies in that regard.

So big efforts going into making sure we're well prepared to capitalize on the H1 opportunity this year, and it's so important for retail, as you know, through managing our inventory in the stores. There are some supply chain impacts in that H2 result that you're referring to.

Shane Gannon

In the headline...

David Errington

Sorry, sorry, Shane, I cut you off.

Shane Gannon

No, you go ahead mate and I'll just talk about CODB in a bit more detail, but...

David Errington

How much was the – how much are we talking? And was it the guys at Woolies that got a bit more greedy to charge you a bit more, trying to boost their profit? I mean, is it something like that? Or what is that supply chain? What is it? I mean how much? And what is it actually?

Steve Donohue

It's definitely not as you described it, David, for clarity.

David Errington

— ***Indiscernible*** — that one, Steve, sorry.

Steve Donohue

That's okay. Look, it's just legitimate operating costs that are flowing through in supply chain costs. I mean I don't think there's anybody out there that's not experiencing higher fuel costs, higher various impacts on costs. So we don't think of ourselves as unique in that respect.

These are all COVID impacts that have continued in that half and somewhat in this half, affecting our supply chain costs. It's not procure you to our provider, we are operating in a market that has been dramatically affected not just in Australia, but globally. And I think the point I really wanted to land with you, David, is that we are building in protections from the downside risk of not having stock in H1 this year, which is so, so important for retail. So it's a balancing act as ever. Things will get back more to normal, although H1 for retail this year is going to be a bit lumpy to put it mildly, given what things [offer]

David Errington

Sorry, Shane, you were talking about net COGS, is COBD…

Shane Gannon

Yes, it might be something to sort of have a bit more deeper analysis later in the afternoon we catch up. But just when I look at the cost from the year, first of all, and look at the increase, it's about $60 million, $70 million – call it, $70 million. There's a raft of points, but we shouldn't forget the store network, the increase that comes with expanding our store network.

There are some additional costs as part of the partnership and the standup function that we incurred. And some of these are more weighted to the second half, but they're not that – there are at some [nice], but some of it has an impact. There's certainly the CapEx to OpEx, which is just technology point we keep talking about. Most of that is in the second half, which has had a so-called material impact.

But it's not 1 point. What I want to leave with is it's not that this is accepted as the final result. We're certainly investing in the technology, and I'm not shying away from that. But the other cost of operations, we are looking for initiatives to offset those inflationary pressures.

Operator

And our next question today comes from Craig Woolford with MST Marquee.

Craig Woolford

I think I'll continue on about the gross margin. Perhaps if we can understand the seasonality expected in gross margins? I know things are not back to normal, but you are talking about higher supply chain costs in the first half.

Should the underlying gross margin, if it's normal operating conditions be fairly even between both halves? And when you talked about promotional activity, I guess, second half sounds like it was higher or more promotional than the first half just to be clear about that.

Steve Donohue

I think the short answer is yes. I mean, I've talked a lot about the structural resilience that we've built into gross margin over time. We've not seen a deterioration of that, whether it be from a – step away from customers wanting to drink better, whether it be the appetite for Pinnacle products.

And I've talked a bit about the nature of the market as it relates to promotional activity. Certainly, those things can change, and we've got this bigger picture macroeconomic situation playing out as it relates to customer purchasing power and their propensity to want to continue in their purchasing patterns as it was historically.

But as I touched on before, my experience has been that these are relatively affordable indulgence, if they are even considered indulgences by customers. And what it really does do that is the drinks business and the hotels business is underpinning sociability, which is such a strong thematic that's come through the other side of COVID.

People want to get back together, whether it be at home or in a pub or elsewhere and enjoy that social connection with one another, effectively, what these businesses do is enable that. So that's the big overriding thing. There's not going to, in my opinion, be a big shift in our ability to maintain that structural resilience in our GP line, but we operate in a very fluid environment, and the market is a competitive one.

Craig Woolford

Okay. So first half and second half should be theoretically fairly similar? It's not like a Christmas SKU product mix benefit in first half?

Steve Donohue

Not really. The big thing that shifts one half to the other is the sales and in particular, our Dan Murphy's business is a massive destination for customers through both November and December. So that's a big opportunity that's always existed.

Shane Gannon

Let me jump in, Craig, and just say, look, Murphy's being normal. There will be consistency of the gross margin, but the obvious thing is the EBIT because of the seasonality of that first half versus second half.

Craig Woolford

It was abnormally big H1 last year.

Steve Donohue

It was, It was.

Operator

Your next question today comes from Ben Gilbert with Jarden.

Ben Gilbert

Just on the hotel side of things. Shane, if we look pre-COVID, you CODB margin used to run around 48% – 48% in change. Is that sort of what we should think about as a normal base in the context of Murphy's obviously, all the work you've done around [AGMs] there's a decent amount of uplift that comes through there. I'm just trying to want to understand how we think about that cost side of things going forward?

Shane Gannon

I can't give you the bridge between the F '19 and current because I think there's a lot of sort of cost of operation that's flowed through since we – F '19…

Steve Donohue

So I just want to check, Ben, you said 49%, did you said CODB…

Ben Gilbert

About 48%. I think in '19, it was at 48.3%.

Steve Donohue

Back to [19] – Yes.

Shane Gannon

So in some ways, different business in terms of the overlays of the sort of costs that have been flowing through to hotels to support our publicly – in our public company representation. Mate I have to take that offline to give you a waterfall that gives you from that sort of low percentage, I haven't seen that before. So I just need to check that.

Steve Donohue

I have to go back and check that number. But what I can say about cost in hotels is being particularly well managed through COVID, and we expect that to continue through the current financial. We've actually being able to generate results off the back of much lower operating costs generally speaking.

And I don't think that, that – we don't expect to see a big shift in that. But if you're wondering whether the CODB rate for hotels in the current year is going to be at that level, no. I don't think so. But I'll go back and check your maths…

Shane Gannon

Look, I would just add, we'll answer that question, Ben, but the more sale end point for me is that I think the structure, the cost structure that we've got in place for the hotels will support its growth. So moving back to our thoughts around long – medium to longer term, the renewals program and improving our earnings profile there, plus acquisitions, we can leverage off the infrastructure that we've built in terms of our cost base.

Steve Donohue

I mean stand back from a pub, you want to make sure you're continuing to invest in the place, and that includes the gaming fleet, the technology that underpins the customer experience and the environment. So those investments are going to continue to be a factor in the future.

Shane Gannon

I'm not walking away for the question, but we'll answer it…

Steve Donohue

We'll come back on that specific at '19.

Operator

Next question then comes from Ross Curran with Macquarie.

Ross Curran

Just a quick question about the remuneration report. So the Board has failed you on customer VOC, sizing issues with deliveries and distribution in the first half. It seems that it's improved in the second half, but is that extra investment in the second half hardly to explain what the margins vary between first and second half?

Steve Donohue

It's an interesting bridge you've built there. But no, I don't think I could necessarily link it to, but let me talk to the specifics of your point. So we were – as I just said in my opening remarks, very proud of the efforts that the team went to on achieving growth in Voice of the Customer across both our – all of our businesses, I should say, BWS Dan Murphy's and our hotels collectively.

We had pretty aspirational targets coming into the year. And what obviously wasn't able to be anticipated was the impact of Omicron. And Omicron really did tighten up driver availability and the delivery experience for customers through December and January, which are, of course, peak trading periods.

Now understandably, our customers marked us down on their experience because perhaps things took longer or whatever the case might be in terms of that customer experience. I think with all of the puts and takes in the performance of the year, the remuneration report describes the approach that the board took. And obviously, as by the member of the board and management thought that, that was an appropriate outcome for the team but it takes nothing away from the level of pride we've got in the achievements of the team under the circumstances to actually improve their customer scores, we just had pretty tough targets for ourselves in the year.

Whether it links back to the cost side of things is good point. I hadn't sort of linked the 2 in my mind, as I said before. But certainly, we were paying more for drivers. We had to pay more for drivers because there was a tightening of availability, it wasn't the single biggest impact on the CODB side of things in H2, but it certainly did play out. Now pleasingly, there has been something of a shift in driver availability actually in the relatively short term. So that's a positive, and we're seeing a play-through to both customer experience and cost at the moment. But it's a – from the cost side of things, it is very, very small in these kind of things.

Ross Curran

And just on VOC and just a follow-up. Are you able to talk through staff absenteeism through July and August, how that split?

Steve Donohue

Yes, it's gotten considerably better, thankfully. So I think we all know that there's been, obviously, the COVID impact, but there's been a variety of other flu and so on that has affected people. So we really kind of did it quite tough actually through sort of April, May – June and July have gotten considerably better, but we are still suffering somewhat from team availability impacts, which, of course, overall, for the most part, legitimate, people not well shouldn't come to work.

So I respect that does put a bit more pressure on the team that are there, and we're very thankful for those efforts. But yes, it's gotten better. It's about half the impact that it was back in April, now that we're in August, still a thing though.

Operator

And our next question today comes from Richard Barwick with CLSA.

Richard Barwick

I had a question on CapEx. If you think back to the Investor Day, you were talking about total CapEx being in the range of $320 million to $460 million. But at that time, I think there's a bit of a question mark. Some of the technology transition stuff was detailed as a bit of a work in progress. So given some of your comments today, I mean, obviously, a lot of that investment seems like it's falling into OpEx.

Just be keen to hear any updates you might have on FY '23 CapEx. And it would sort of look like you've spilled out this technology transition in a bit more detail. So what the flow-on effects would then be in the '24, '25 given it's quite a long-term project.

Shane Gannon

Yes, let me tackle the CapEx question. Clearly, it's going to be – it will fluctuate based on our success of acquisitions, and we're very focused on looking for new opportunities, particularly in the hotel space, but as we've demonstrated, we're taking a sensible approach in terms of acquisitions, given certain valuations.

But we are encouraged that there are opportunities emerging. So over the next 12 months, so I'd like to see us acquire more hotels. The renewals program, probably similar numbers at this stage. So no dramatic change in that. Over time, what you're probably going to see is probably the average spend for each renewal sort of might improve as we sort of look at each hotel and how we can enhance even further the value of those hotels.

But they'll be only on the basis of meeting our hurdle rates. So in substance, I would say our CapEx for next year is going to be in the order of $350 million to $400 million. That's where I would sit today based on the landscape we're looking at. But I underline the point. We see opportunities that can enhance the value of this organization in hotels and retail, and we're certainly going to look at it.

But to answer your question. And on the technology side, yes, so what we've tried to do at the moment is just give you a bit more of a profile about the timing of the projects. And we are – some of those projects being more moving into F '24, a bit of planning in F

’23, but I did give you a steer that from an OpEx point of view, the spend would be about $30 million in F ’23.

But what we will be doing is as we increase that spend, it will only be on the basis of a clear business case, which we will share with the market when we make those investment decisions.

Steve Donohue

Yes, still very fluid.

Shane Gannon

I hope that answers your question.

Operator

And our next question today comes from Tom Kierath with Barrenjoey.

Thomas Kierath

Just looking at the disclosure on your payments to Woolies. It looks like it’s up about $80 million in the year. Can you just give us a breakdown of how that compared first half versus second half in terms of the growth rate? Just trying to understand this uptick in the supply chain costs and where that’s kind of going to?

Steve Donohue

Yes. Thanks, Tom. The majority of that is not supply chain. Most of that is the acquisition that Woolies made at PFD, which are our largest food supplier in hotels. So that’s been the big tick up there. It’s not a big H1, H2 swing. I don’t think I do have to go back and check the timing, but I think it was all the way through the financials. So I think the comments we made earlier on the impacts of supply chain costs in H2 stand.

Operator

Our next question comes from Lisa Deng with Goldman Sachs.

Lisa Deng

Just 2 quick questions. One is actually on the technology investment of around $30 million next year. I think Shane made a comment that it's going to be sort of recuperated with cost savings of the same magnitude. Is it in year cost savings? Or are we talking about future cost savings? So that's number one.

The second one is, can we please get guidance on the magnitude of the price increase in August across the portfolio and a potential outlook on the February round of price increases?

Steve Donohue

Yes. Thanks, Lisa. I appreciate those questions. Let me just bring some specificity to what Shane touched on earlier. He said there was about $20 million to $30 million in incremental OpEx costs in F '23. And the reason that number is such a broad – those numbers are in such a broad ranges that there's still a lot of work to bring determination to exactly what we're going to do.

What he was also saying was that when we make those calls, they're underpinned by very strong business cases, which deliver value, if not over the short term, certainly over the medium to long term. So we'll keep the market abreast of that. I think it's more likely to be at the lower end of that range than the upper end based on my experience of our capacity to execute those sorts of programs.

So hopefully, that answers your first question. On the second question, the CPI increase that came through. I think it was about 4.4 was – so as I said, you've got in August and a February excise increase that comes through, and that's indexed against inflation.

And it came through around that 4.4 mark. That flowed through to a similar number actually in terms of retail sales prices. But it's got lumpiness in it, too. Spirits are a bit higher than beer and wine is generally the lowest because it doesn't have the direct link to excise. But that's sort of around about the level of price appreciation that's going on post August at the moment.

Operator

And our next question today comes from Phil Kimber with E&P Capital.

Phillip Kimber

Just a question back on the hotel business and regarding seasonality. Historically, the business had a 60%, 40% split first half – second half. So I just wanted to check that was our earnings split. I just wanted to check whether anything significantly changing that business to make that no longer relevant. And then outside of the $20 million increase in – or impact from higher Victorian taxes, is there anything that we should be aware of in that second half?

I mean I think there might have been some freight cost, there was Omicron issues. Just that we should be aware of when we're thinking about that sort of seasonality and trying to get some sort of run rate on the hotel business?

Steve Donohue

Phil, sorry, just for clarity, you are talking about hotels in terms of that mix you just described here because…

Phillip Kimber

Yes, hotels only and just earnings mix was 60-40 first half, second half historically.

Steve Donohue

My recollection is we're pretty flat on earnings mix half to half, but I think, yes, in hotels – it's different in retail. Retail has got a much bigger indexation to H4 – H1, sorry, sort of

60-40 in retail. But hotels is pretty consistent, but maybe we can unpack that question in a bit more detail.

And then I think the other part of your – separately, I should say – the other part of your question was the gaming entitlements cost in the current financial that we think we touched on that before. So it's in the vicinity of $20-odd million in the year – in F '23 if so. Happy to unpack your question in a bit more detail offline, Phil, in relation to the split of earnings, H1 to H2 in hotels.

Operator
Thank you. And ladies and gentlemen, this concludes your question-and-answer session. I'd like to turn the conference back over to Steve Donohue for closing remarks.

Steve Donohue
Well, thank you all for joining us today. I would underscore our presentation by saying we really do appreciate the efforts of all of the team right across Endeavour Group to deliver what I would consider to be a very strong result under very challenging circumstances that have been throughout the year.

We feel as though we're well placed to achieve a good result again in F '23. We're very focused on managing the volatility that lies ahead. We're rack to have people back in the past and engaging in those social occasions, again. I hope you've been as to one yourself and if you haven't, get to one soon. Thanks for joining us today and look forward to speaking to you all again soon. Cheers.

Operator
Thank you. Ladies and gentlemen, this concludes today's conference call. We thank you for your participation.