

Lynch Group Holdings Limited

Some green shoots in FY23

Lynch Group Holdings Limited (ASX:LGL) is Australia's largest vertically integrated wholesaler and grower of flowers and potted plants with >100-years of operating history. The group also has ~17 years' operating history in China as a grower and wholesaler. In FY22 the sales split between Australia and China was 77%/23%, while the EBITDA contribution was 48%/52% respectively. The group listed in April 2021 issuing 35.4m shares at \$3.60/share for debt reduction, capacity expansion in China, and the acquisition of the 80% of VDB in Asia they did not own, while at the same time transferring 21.9m shares from existing owners to the public. Trading since the IPO has been impacted by a number of issues including the rolling Australian lockdowns (H1 FY22), higher freight costs (FY22) and, more recently, rolling China lockdowns (Q4 FY22). The speed of cost increases was unable to be recouped from a timing perspective and as a result FY22 NPATA declined 30% despite revenues growth of 10.7%. Revenue benefited from an additional 18ha or 23% capacity in China and improved H2 FY22 demand in Australia. Looking forward, management expects revenue growth across both Australia and China, a gradual improvement in Australian margins from already negotiated price increases and range management, and pressure on China margins due to energy costs and pricing pressures related to weakening consumer confidence.

Business model

LGL is a vertically integrated wholesaler and grower of flowers and potted plants across Australia and China, and uses the resulting experience and scale to create significant barriers to entry. Flowers have a complex supply chain given they're a highly perishable product, have a short shelf life and face biosecurity regulations. LGL has built a network of growing farms (five in Australia including two third-party and four in China), processing facilities (four in Australia and two in China) and retailer relationships. As a result, LGL supplies ~88% of the fresh flowers sold by Australian supermarkets across >2,000 stores. Growth is expected from greater penetration of flower supermarket sales as a percentage of the total market and increased capacity in China both in growing and processing.

Cost recoupment and China production growth key for FY23

In FY22, Australian operating costs of ~\$11m including domestic and international freight and labour rose faster than the levers for recoupment could be implemented. A moderation of these pressures in FY23 together with price increases is expected to see improvement in Australian margins over FY22. Cycling lockdowns, Australian revenue growth is +10% for the first six weeks in FY23. In China the benefits of higher production including a further 10ha (+13%) planned for H2 FY23 should result in continued revenues growth, but higher energy costs and some selling price pressure may impact margins. An update on trading is expected at the AGM in November.

Comparables are vertically integrated produce wholesalers

LGL has similar characteristics to fruit and vegetable wholesaler Costa Group Holdings (ASX:CGC) and salmon farmer Tassal (ASX:TGR) with respect to perishable products, shelf-life, end-markets and freight costs. LGL is arguably more discretionary, and event-driven, while Costa is more prone to weather events. Tassal is the subject of a takeover offer.

Historical earnings and ratios

Year end	Revenue	EBITDA adj.*	NPAT adj.	EPS adj.	EV/EBITDA adj.	PER (x)	Dividend (cps)	Yield (%)
06/20a	255.2	30.4	12.1	0.18	7.0	12.6	0	0.0
06/21a	331.0	58.6	32.4	0.41	3.9	5.6	0	0.0
06/22a	366.5	48.2	24.7	0.20	6.9	11.3	0.12	5.2

Source: Company data; *EBIT, NPAT and EPS adjusted for one-time, non-cash items

Wholesaling

9th September 2022

Share Details

ASX code	LGL
Share price (8-Sept)	\$2.29
Market capitalisation	\$279.6M
Shares on issue	122.1M
Net debt at 26-Jun-2022	\$51.7M
Free float	47.8%

Share Performance (12 months)



Upside Case

- Easing of freight costs
- Supermarkets grow share of floral segment
- Further capacity growth in China

Downside Case

- Geopolitical risks in China
- Supermarket pricing pressure in Australia impact gross margins
- Energy costs and consumer confidence in China

Catalysts

- AGM trading update
- New China capacity

Comparable Companies (Aust/NZ)

Costa Group (ASX:CGC), Tassal (ASX:TGR)

Board and Management

Hugh Toll	CEO & Executive Director
Steve Wood	CFO
Patrick Elliot	Chair & Non-Exec Director
Peter Clare	Ind. Non-Executive Director
Elizabeth Hallet	Ind. Non-Executive Director
Peter Arkell	Ind. Non-Executive Director

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FINANCIAL SERVICES GUIDE

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