

Towards Start up winery profit



“When do I start making Money?”

My Background

- **Biologist by education – animal science**
- **Career:**
 - **8 years in animal science field**
 - **15 years as commercial loan officer for many agricultural operations including wineries**
 - **2 years as Business Consultant – serving winery and dairy farm clients**
 - **Since 2011 – director of the Winery Benchmark**

Outline

- **Winery Accounting – basic fundamentals**
- **The 5 to 10 year phase – how to analyze**
- **Budgeting from the bottom up**
- **Q&A**

Accounting for wineries

- **GAAP/Tax requirements – not always the best for management decisions**
- **Cost accounting – be careful....it's the key to accuracy, but hard to do right.**
- **Small wineries – don't make it complicated**

Profit/Loss Statement

Income

Less COGS

= Gross Profit

Less Sales Expenses

Less Overhead

=Net Profit

Less Draws (Owner Salaries)

=Available Profit (for Debt or Investment)

Simpler

Income

Less COGS

= Gross Profit

Less Overhead (include sales expenses & draw here)

=Net Profit

What goes where

COGS

**“Costs of Goods sold”, or
“Variable” expenses**

- **includes direct labor**
- **cost to produce wine (glass, cork, grapes, etc)**

Overhead

Overhead

“Fixed Costs, or

“Sales, General & Administrative costs”

Includes:

- All other labor
- Utilities
- Taxes
- Insurance
- Interest

Typical Winery Start Up

- **5 years of vineyard development**
- **Other costs during this phase may include:**
 - Licensing
 - Permits
 - Production area
 - Wine equipment
 - Tasting Room

The 5 to 10 year phase

- **Marketing, Marketing, Marketing**
 - First solid income of the business
 - Did you make a profit?
 - But what about cash flow?
- **Build Inventory**
 - Common mistake is to under estimate this equity drain
 - Necessary for sales growth
 - How should you finance this?

Inventory

- **Lesser of Cost or Market (Value) – in this presentation assume inventory is at cost**
- **Examplecost per case**
 - **\$10 Labor**
 - **\$13 Bottle, cork, labels**
 - **\$40 grapes**
 - **\$4 supplies****Result: \$67 per case**

Example

- John's winery sells \$60,000 of wine at an average of \$100/case (600 cases sold)
- The cost to produce wine at this winery is \$67/case
- John bottled 1,000 cases of wine in the same year
- Did John's winery make a profit?
- Did John's winery cash flow?

Example of mistake

John incorrectly conducts his cost study. He estimates cost of production at \$40/case. He thinks he will see this:

\$60,000 Income	600 cases	\$100/cs
-24,000 COGS	600 cases	\$40/cs
\$36,000 Gross Profit		

COGS Calculation:

	“Cost”	# cases	Cost/Case
Beginning Inventory	\$20,000	500	\$40
+ Costs	\$67,000	1000	\$67
- Ending Inventory	\$36,000	900	\$40
= COGS	\$51,000	600	\$85

Result of Mistake

John is surprised when his accountant shows him the Profit/Loss Statement including:

\$60,000 Income	600 cases	\$100/cs
-51,000 COGS	600 cases	\$85/cs
\$9,000 Gross Profit		

Corrected Inventory

John corrects his production cost study, and determines costs correctly at \$67/case. He expects to see this P/L Statement:

\$60,000 Income	600 cases	\$100/cs
-40,200 COGS	600 cases	\$67/cs
\$19,800 Gross Profit		

COGS calculation:

	"Cost"	# cases	Cost/Case
Beginning Inv	\$33,500	500	\$67
+ Costs	\$67,000	1000	\$67
- Ending Inv	\$60,300	900	\$67
= COGS	\$40,200	600	\$67

Results of Third Try

\$60,000 Income	600 cases	\$100/cs
-40,200 COGS	600 cases	\$67/cs
\$19,800 Gross Profit		

The original estimated P/L statement was correct and the COGS calculation showed that costs are being properly allocated.

Finish with Overhead

\$60,000 Income
-40,200 COGS
\$19,800 Gross Profit
- \$18,000 Overhead
= \$1,800 Net Profit

John's winery made it's first profit!!

Actual Cash Flow

\$60,000 Income 600 cases \$100/cs

-67,000 Prod Costs 1000 cases \$67/cs

= -7,000 Cash Flow after production

-18,000 Overhead

= -25,000 Cash Flow before loan payments

-12,000 Principal payments

= -37,000 Cash deficit

Concept to remember

To generate cash flow as a start up winery, you must either:

1. Be extremely profitable, or
2. Level off inventory growth

Managing Inventory

- **Monitor inventory and make more of what sells quickly**
- **Make more white wines – faster turns**
- **Plan your “inventory build” as part of your capital costs**
- **Avoid operating lines for the purpose of inventory build (i.e. it’s not a cycle, it’s a permanent level of inventory)**

Estimate Inventory Growth

	2013	2014	2015
Cases sold	1000	2000	2500
			Assume level going forward
Est. Cost to produce	\$70/case		
Inventory req'd	1.3 x cases sold		
Cash required to "build inventory"	\$91,000	\$45,500	\$0
Sales (say \$125/cs)	\$125,000	\$250,000	\$312,500
Cash Prod. Costs	\$161,000	\$185,500	\$175,000

Budgeting from the Bottom Up

- How much profit do you need to break-even?
- How do you figure out what an appropriate sales target is?
- How feasible is your plan?

Start from the “Bottom”

- Overhead
- Note: Owner draw – we have included this in overhead in examples so far
- Principal & Interest debt payments
- These 2 items (overhead and debt payments) are where you start

Revised Profit/Loss

Income

Less COGS

Gross Profit

Less Overhead (includes owner draw)

Net Profit

Add interest Expense back

=Total Available Funds (EBITDA)

Subtract all debt payments (Principal & Interest)

Bottom – Principal & Int

- Let's say you have payments of
 - Wine equipment \$675/mo
 - Mortgage \$1,200/mo

- Annual Principal and Interest payments are:
 - \$22,500

Build it

Loan Payments	\$22,500	

Build it

Overhead	\$18,000	Don't include interest here
Loan Payments	\$22,500	

Build it

Gross Profit	\$40,500	Use your Gross Profit per case (\$33) to determine cases to be sold (results in 1230 cases)
Overhead	\$18,000	Don't include interest here
Loan Payments	\$22,500	

Build it

COGS	\$82,500	Use your cost of production per case (\$67) x cases sold (1230)
Gross Profit	\$40,500	Use your Gross Profit per case (\$33) to determine cases to be sold
Overhead	\$18,000	Don't include interest here
Loan Payments	\$22,500	

Break-Even

Income	\$123,000	Cases sold as determined below x average price
COGS	\$82,500	Use your cost of production per case (\$67) x cases sold (1230)
Gross Profit	\$40,500	Use your Gross Profit per case (\$33) to determine cases to be sold
Overhead	\$18,000	Don't include interest here
Loan Payments	\$22,500	

Revised Profit/Loss

Income	\$123,000
Less COGS	82,500
Gross Profit	40,500
Less Overhead (let's say \$2,000 interest)	20,000
Net Profit	20,500
Add interest Expense back	2,000
Total Available Funds (EBITDA)	22,500
Subtract all debt payments	22,500
Excess/Deficit	0

Optional

- If Retail/Wholesale “mix” will change, then run this optional calculation

Total Required Sales = Retail Sales % x (Gross Profit Req'd / Retail Gross Profit %) + Wholesale Sales % x (Gross Profit Req'd / Wholesale Gross Profit %)

Result of this exercise

- Sales target of at least \$123,000 has been established
- With average price of \$100/case, that's 1,230 cases sold
- If wholesale sales increase to reach this target, the cases sold will need to increase dramatically
- Make a feasible plan to make a profit.

Key Concepts

- Don't forget the cost of “building” inventory
- Have a plan to finance this (cash or mortgage best)
- Have a record keeping system & accounting plan that will tell your story accurately
- Vineyard economics: low yield = high cost grapes & high cost wine....lowers GP%
- Build the right size winery!

Questions?

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