BSVI – CAMPARI EQUITY RESEARCH

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COMPANY OVERVIEW

Gruppo Campari is a key player in the global alcoholic beverage industry. The Milan-based company, founded by Gaspare Campari in 1860, manufactures and markets well-known aperitif brands such as Campari and Aperol. Today, the Italian group's portfolio includes over 50 premium and super premium spirits, wine and soft drink brands which are sold in more than 190 countries. The Group, employing 2,000 people, boasts a rich and diverse portfolio across three segments: spirits, wine, and soft drinks. Gruppo Campari is the sixth-largest group globally in branded spirits and the leading Italian group in the sector. It holds a leadership position in Italy and Brazil and prominent positions in the USA and continental Europe.

The shares of the parent company, Davide Campari-Milano S.p.A., are listed on the Italian stock market.

SECTOR & STRATEGY ANALYSIS

The alcoholic beverages industry comprises companies that manufacture and sell beverages containing alcohol from various sources. The main segments of the industry are beer, wine, and spirits. Among these exist various subsegments differentiated by their production materials and techniques, and the flavors and alcohol content they produce. All alcoholic beverages share the commonality of fermenting some source of sugar at some stage in their production to produce alcohol.

Beer is the most consumed alcoholic beverage on the planet and for this reason, the world's largest beer brewers are also the largest alcoholic drink manufacturers on the planet, with Belgian AB InBev leading the pack. Spirits, which are produced by distilling after fermentation are the next largest market, are led by the British company Diageo. Finally, wine, made from fermented grapes, is the smallest major alcohol segment. The largest producer is E&J Gallo Winery. The alcoholic beverages market is expected to grow by nearly 33 percent by 2025 to nearly two trillion U.S. dollars in value from 2022's value of 1.48 trillion dollars. Much of the alcoholic beverages market revenue comes from the two largest country markets in the world, the United States and China. In terms of categories, beer is the dominant beverage in the industry. Beer accounted for 41.9 percent of all alcoholic beverage sales in the United States in 2022. Spirits surpassed beer for the first time at 42.1 percent of the market. Wine has declined to a 16 percent share. Beer has been steadily losing market share since 2000 when it accounted for over half of all sales. Spirits have been the main benefactor of this slump, picking up over ten points of market share since that time. Meanwhile, wine has stayed relatively unchanged in its position.

Recently, with the advent of legal recreational cannabis markets in the United States and Canada, many alcoholic beverage companies have begun investing in cannabis businesses as a new revenue stream and as a hedge against revenue loss to a competing industry. Another emerging trend in the industry follows the general trend towards health and wellness in the overall food and beverage industry. As more and more people are trying to limit their intake of alcohol, more companies across the spectrum of the industry have begun offering low and no-alcoholic options, to great success. Additionally, consumers are showing growing interest in alternative beverages like hard seltzer and other ready-to-drink offerings.

CUSTOMER PREFERENCES:

Consumers are increasingly seeking unique and premium alcoholic beverages. They are willing to pay more for high-quality products that offer a distinct

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taste and experience. This has led to a rise in the demand for craft beers, artisanal spirits, and small-batch wines. Additionally, health-conscious consumers are opting for low-alcohol or alcohol-free alternatives, such as non-alcoholic beers and mocktails. The growing popularity of these products are driving innovation in the industry, with manufacturers introducing new flavors and varieties to cater to diverse customer preferences.

LOCAL SPECIAL CIRCUMSTANCES:
The Alcoholic Drinks market Worldwide is characterized by diverse local special circumstances. For example, in countries with a strong wine culture, such as France and Italy, wine consumption remains high and is deeply rooted in the local traditions and lifestyle. On the other hand, countries with a long history of beer brewing, such as Germany and Belgium, have a thriving beer market with a wide variety of traditional and craft beers. Additionally, cultural and religious factors influence the consumption patterns in certain regions, with some countries having stricter regulations on alcohol sales and consumption.

UNDERLYING MACROECONOMIC FACTORS:
The Alcoholic Drinks market in Worldwide is influenced by various macroeconomic factors. Economic growth, rising disposable incomes, and urbanization are key drivers of market expansion. As economies grow, consumers have more purchasing power and are willing to spend on premium alcoholic beverages. Additionally, the increasing urban population, particularly in emerging markets, has led to a rise in the number of bars, restaurants, and entertainment venues, creating a favorable environment for the growth of the market. Furthermore, demographic shifts, such as changing age structures and evolving lifestyles, are shaping the market dynamics. Millennials, for example, have different preferences and consumption habits compared to previous generations. They are more likely to experiment with new flavors and brands, seek authentic experiences, and prioritize social and environmental values. As this generation becomes a significant consumer group, companies in the Alcoholic Drinks market are adapting their strategies to cater to their needs and preferences. In conclusion, the Alcoholic Drinks market in Worldwide is experiencing growth and development driven by changing customer preferences, emerging trends, local special circumstances, and underlying macroeconomic factors. The demand for unique and premium products, the rise of e-commerce, the focus on sustainability, and the influence of local traditions and regulations are shaping the market landscape. Understanding these factors and adapting to the evolving market dynamics will be crucial for companies in the industry to stay competitive and meet the changing demands of consumers.

FIVE FORCES ANALYSIS

SUPPLIER BARGAINING POWER (LOW):
The company engages with over 120 suppliers globally, segmented by strategic production regions, including South America, North America, Asia, and Europe. Since 2004, the Campari Group has established its distribution network in 20 markets, with distribution subsidiaries contributing to over 90% of its revenue, primarily situated in Europe and the Americas. In pursuit of product excellence and ethical conduct, the Campari Group has mandated all raw material, packaging, and point-of-sale material suppliers to adhere to a Supplier Code since 2012. In Italy, the company has opted not to directly distribute its products since 2011 due to high taxes, choosing instead to rely on existing large retailers for economic and logistical advantages.

BUYER BARGAINING POWER (MODERATE):
Campari's reputation is pivotal in retaining its customer base. This necessitates maintaining exceedingly high standards, as any misstep would have financial repercussions and challenges for the company. It's worth noting that Campari is the undisputed worldwide leader in aperitif products, which grants access to a diverse consumer base enjoying the company's flagship products, Aperol and Campari. Similar to suppliers, retailers also subscribe to the Supplier Code, safeguarding both customers and the company.

THREAT OF SUBSTITUTES (MODERATE):
Campari does not just offer an excellent product with a solid reputation but strives to create the ideal context for consumption. Therefore, it provides a comprehensive experience package, making product consumption complementary to the environment. The only product capable of offering a similar experience is beer, thanks to its versatility in accompanying various social occasions, including aperitifs. Given the increasing consumption of beer, it represents a potential threat to traditional aperitif beverages.

***LIFE CYCLE*:**
The flagship products of the group Aperol and Campari can both be considered in their maturity phase. Campari may invest in innovation or marketing strategies to extend their life cycle. If and when entering the decline phase, diversification into new products or markets might be considered.

***DEGREE OF INTERNALIZATION AND OUTSOURCING*:**
Campari's decision not to distribute directly in Italy

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since 2011, relying on existing large retailers, reflects a strategic response to high taxes. Assessing the advantages and risks of internalization and outsourcing remains crucial. It enables Campari to optimize economic and logistical advantages while mitigating risks associated with direct distribution.

***DEGREE OF INTERNATIONALIZATION*:**
Campari's international presence, with distribution subsidiaries contributing to over 90% of its revenue, is a strategic advantage. It allows Campari to diversify its market exposure and potentially mitigate risks associated with economic fluctuations in specific regions.

***SUBSTITUTION CYCLE*:**
Recognizing substitution cycles is vital for anticipating shifts in consumer preferences. As beer represents a potential threat due to its versatility in social occasions, Campari needs to continuously innovate and adapt its products and marketing strategies to maintain its appeal and prevent consumers from shifting to substitutes.

COMPETITIVE RIVALRY (HIGH):
Direct competitors are represented by holding companies ranking among the top three in the Branded Spirits sector: Diageo, Pernod Ricard, and Bacardi Ltd. These entities operate within the same market, exuding brand reliability and prestige, posing a threat to Campari. The sustained high level of competition results from the production and sale of the four primary spirits (Vodka, Rum, Gin, and Tequila), which are introduced by nearly all holding companies in the Branded Spirits sector. Consequently, this leads to significant brand differentiation, oversupply, and a reduction in demand for each individual company, fostering intense price competition. Each holding's strength lies in its potential to dominate a specific niche within the beverage sector." The high level of competition among industry giants (Diageo, Pernod Ricard, and Bacardi Ltd) increases the likelihood of aggressive responses to any strategic moves by Campari (retaliation by competitors).

CHANGES IN COMPETITIVE SYSTEM DYNAMICS:
***CONJUNCTURAL DYNAMICS*:**
Short-term changes, like fluctuations in exchange rates affecting product prices are reversible and may require agile responses but may not fundamentally alter market structures.

***STRUCTURAL DYNAMICS INTERNAL TO A COMPETITIVE SYSTEM*:**
Permanent changes modifying economic combinations and player interrelationships, such as mergers, acquisitions, or changes in market preferences, can reshape the competitive landscape and impact long-term strategies. Campari, expanding its group with strategic acquisitions (for example Tannico to leverage e-commerce capabilities) models its landscape to maintain competitiveness.

THREAT OF ENTRY (LOW):
Barriers to entry into the market are high in the liquor industry due to high capital requirements (fixed costs, specialist equipment expenses, and plant construction costs) and the consolidating effect of economies of scale (-)

Competition is both restricted and enhanced by the regulation of Federal, State, and Local governments. Alcohol-containing products are subject to complex production requirements that could reduce the competitiveness of medium and small enterprises. On the other hand National and European regulations tend to enhance competition. (+-)

Existing firms do possess *trademarks* and have well established brand reputation (-)

Access to distribution channels became easier for small competitors and new entrants thank to the rise of e-commerce (+)

PEST ANALYSIS

POLITICAL FACTORS:
Factors:
- Legislative measures and regulations
- Taxation on alcoholic products

Opportunity:
Some of the laws and regulations may impose a disproportionate burden on small and medium-sized producers without corresponding justifications based in public health or the prevention of anticompetitive behavior (labeling pre approval requirements, and complex application requirements to qualify for a permit to produce alcohol)

Threat:
Evident goal of the FAA Act (USA) and European commission, to combat monopolies and regulate oligopolies in the alcohol beverage industry. -Increased taxation on products containing alcohol may drive a reduction in demand

ECONOMIC FACTORS:
Factors:
- Rise in disposable income drives market growth
- The market is projected to exhibit a CAGR of 9.78% during the 2022-2029
- Inflation and Cost of Energy

Opportunity:
- In 2021, according to OECD*, 43% of individuals showed increased drinking frequency.

- The rise in growth can result in increased purchases of premium alcoholic beverages

Threat:

Inflation and energy cost increases may affect production and distribution expenses, while also reducing the buying power of consumers

SOCIAL FACTORS:

Factors:

- Increased alcohol consumption among young adults
- Rising consumer inclination to pick healthier and natural alternatives

Opportunity:

- Potential market expansion with a strategy aimed at capturing the younger segments
- Increased inclusion of natural and functional ingredients in premium segments provides a massive differentiation opportunity

Threat:

- Perception of contributing to negative social impacts due to increased alcohol consumption among young adults could lead to public opinion and social responsibility concerns, ultimately affecting the company's image, and potentially leading to boycotts or negative publicity.
- Changing attitudes towards alcohol consumption (shift to non-alcoholic beverages) may impact demand.

TECHNOLOGY FACTORS:

Factors:

- Rise of e-commerce

Opportunity:

- Opening of new distribution channels for both established brands and small-scale producers, that enables them to reach a larger customer base

Threat:

- Rapid technological changes require continuous investments to maintain competitiveness and may pose a threat if not adapted promptly

INDUSTRY TRENDS

One of the key trends in the worldwide Alcoholic Drinks market is the rise of e-commerce. Online platforms have made it easier for consumers to explore and purchase a wide range of alcoholic beverages from the comfort of their homes. This has opened up new distribution channels for both established brands and small-scale producers, enabling them to reach a larger customer base. The rise of e-commerce presents a significant opportunity for Gruppo Campari to expand its market reach and enhance distribution channels. By strategically embracing online platforms, Campari can offer consumers a convenient way to explore and purchase its diverse range of alcoholic beverages. The acquisition of nearly 40% of Tannico S.p.a. for €33 million, represents a strategic move to exploit the technological capabilities of the acquired startup. In tandem with the trend of digitalization, Gruppo Campari has the chance to capitalize on social media and digital marketing to boost brand awareness and foster consumer engagement. Through creative and interactive campaigns on platforms like Instagram and Facebook, Campari can connect with consumers, potentially cultivating brand loyalty. Partnerships with influencers and the development of engaging content could further amplify its online presence. "160 years since its foundation, Campari is focused on digital transformation to accelerate growth. Thanks to this transformation, we can adapt quickly to market changes," commented Chad Niemuth, Vice President Global IT of Campari Group.

Another trend in the market is the increasing focus on sustainability and environmental responsibility. Consumers are becoming more conscious of the environmental impact of their choices and are seeking brands that prioritize sustainability. This has led to a rise in the demand for organic and biodynamic wines, as well as eco-friendly packaging solutions. Companies that embrace sustainable practices and communicate their efforts effectively are likely to gain a competitive edge in the market. The Campari Group's internationalization process, which today sees it present in 23 markets and 23 production sites around the world, has required an ever-increasing commitment also with regard to the management of its social and environmental impacts, in order to ensure a homogeneous approach in all contexts and aligned with its standards. For this reason, Campari Group deemed it necessary to define a structured path dedicated to sustainability, with the aim of spreading the culture of corporate responsibility internally, implementing projects to support people and protect the environment and sharing the results obtained with its stakeholders. The Campari Group's sustainability path was officially launched in 2011, with the ambition of making sustainability one of the strategic levers for Group growth and for defining corporate policies. As its business grows, Campari Group constantly comes across new opportunities to generate positive economic, social and environmental impacts. A culture of ethics permeates the entire company, ensuring that every business is managed with probity and integrity. As shown in the group's annual sustainability reports, Campari Group's approach to sustainability identifies the following four areas through which the Group's Commitment to creating value in each business area is structured: people, environment, responsible practices, community involvement

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FINANCIAL STATEMENTS ANALYSIS

Head of FSA division:
Russello Salvatore

Financial Statement Analysis division members:
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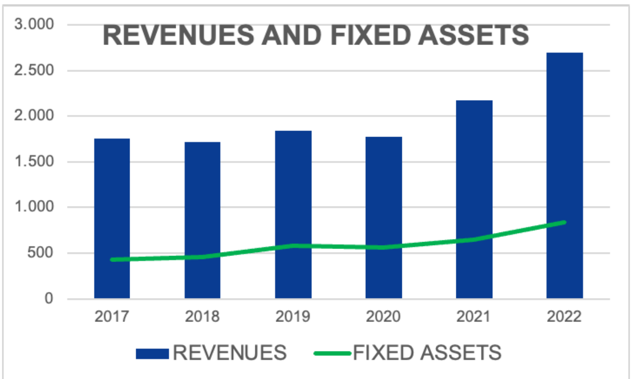

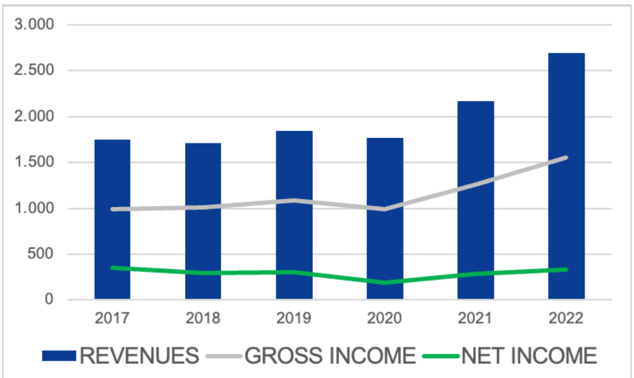

Income Statement: Over the past three years, the company consistently achieved profit increases, although the current value still lags behind that of 2017. The net sales for 2022 have reached an all-time high, and the parity in net income is attributed to the elevated value of Cost of Goods Sold (COGS). Campari Group employs a diversified set of strategies tailored to different brand categories (global, regional, local). Regional priority brands significantly contribute to sales, accounting for 25.4%, followed by local priority brands at 8.3%. Notably, regional priority brands have exhibited impressive double-digit growth of +18.7% in 2022, and the overall portfolio reflects positive growth trends.

Balance Sheet: Despite Campari's impressive organic performance, marked by double-digit growth in net sales, gross profit, contribution margin, and operational results, the company has experienced a rise in net financial debt compared to previous years. The increase in long-term debt from 1.27b USD in 2021 to 1.68b USD in 2022 is attributable to a series of strategic moves, including recent acquisitions, asset deals, long-term loan subscriptions, and investments in manufacturing capacities.

During the same period, the company increased net assets by around 1b USD, with the contribution of accounts receivable, inventories, and net PP&E.
The company emphasizes positive exchange rate effects (+7.9%) observed in financial statements over the past year due to the appreciation of key currencies against the euro.

RATIO ANALYSIS

Liquidity: The company has a considerably lower liquidity compared to the past year due to acquisitions and investments. Liquidity ratios suggest that the company may face challenges in meeting its short-term liabilities with its most liquid assets.

LIQUIDITY RATIOS		
YEAR	Quick Ratio	Cash Ratio
2022	0.83	0.47
2021	1.16	0.84
2020	1.10	0.73
2019	0.89	0.61

Solvency: A long-term debt ratio of 0.28 suggests that 28% of the company's total assets are financed through long-term debt. This indicates a moderate reliance on long-term borrowing for financing. The debt to equity ratio is exceptionally high, also compared to competitors in the premium spirits industry (Diageo, Pernod Ricard, Brown Forman), which could imply that the company is highly leveraged, relying heavily on debt for financing, which can pose financial risk.

SOLVENCY RATIOS		
YEAR	Long Term Debt	Debt to Equity
2022	0.28	94.3%
2021	0.25	85.3%
2020	0.28	103.11%
2019	0.14	58.1%

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Profitability: A ROA of 6% suggests moderate efficiency in generating profits from its asset base, but is within the industry standards. The gross profit margin suggests efficient cost management while EPS is higher compared to competitors.

PROFITABILITY RATIOS		
YEAR	ROA	ROE
2022	6.1%	12.5%
2021	5.9%	12.1%
2020	4%	9.5%
2019	6.5%	12.9%

CONCLUSION

With the impending leadership transition to Matteo Fantacchiotti, the current Managing Director of Asia Pacific, Campari underscores its growth ambitions in the Asia-Pacific region, with a particular focus on Australia, its largest market. The company's operations are segmented into four regions: Americas (45.6% of sales), Southern Europe, Middle East, and Africa (27.7% of sales, with Italy as a key player), North, Central, and Eastern Europe, and Asia-Pacific.

In summary, the alcohol market is poised for sustained growth, driven by the introduction of premium and ready-to-enjoy spirits into households during the pandemic. Campari Group, with its distinctive portfolio of over 50 premium brands, strategically pursues both organic and external growth to solidify its position in key markets, aspiring to be the "Smallest Big Company" in the spirits industry.

However, the current global landscape, marked by heightened volatility due to Russia's invasion of Ukraine, poses challenges, influencing commodity prices and complicating future forecasts. Concurrently, restrictive monetary policies, high inflation anticipation, and projections of negative or below-average GDP growth in key markets add layers of complexity.

Despite these economic challenges and conservative growth forecasts, Campari Group remains confident in its expansion endeavors, drawing strength from a rich brand history steeped in decades of consumer loyalty and a commitment to innovation. The strategic acquisitions undertaken serve as essential pillars of resilience, offering valuable expertise and market insights, positioning the company optimistically for growth amid the dynamic global market conditions.

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COMPANY VALUATION

(under the finance division)

Head of finance division:
Passioni Lorenzo

Finance divisions members:
Scichilone Emanuele
Gribaudo Luca
Ogliastro Francesco

In order to decide what growth rate to use in the DCF model the fundamental growth rate has been used.

YEAR	REVENUES (in million €)	GROWTH RATE
2021	2.173	22,61%
2022	2.698	24,16%
2023	3.247	20,38%
2024	3.786	16,60%
2025	4.271	12,81%
2026	4.657	9,03%
2027	4.901,61	5,25%

After 2021 and 2022 extreme high revenues growth of 23% and 24% respectively, we forecast that in the next five years, from 2023 to 2027, the growth rate will converge to the forecasted luxury industry average CAGR of 5,25% by statista, as shown in the exhibit above. From that onward for the Terminal Value computation, we used a stable growth rate of 2%, equal to the FED inflation target rate.

WACC

Beta: Given the source of revenues for capcom, to compute the WACC an average of the US and Japan Cost of Equity were computed and therefore the Beta between capcom and the **S&P 500** and the **Nikkey225** were both used, which respectively were **0.97** and **0.29.**

Cost of equity: Using the Beta computed above and the risk-free rates illustrated in the first section of this page, the US cost of Equity for Capcom was computed to be 10.8, while the Japanese one 1.9%. Considering the average of the two the **Cost of Equity** used for the DCF was **6.35%**.

WACC: Weighting cost of debt and equity, we obtained the weighted average cost of capital of 6.31%. It must in fact be considered that the company finances itself almost absolutely through equity and therefore the WACC depends mainly on the cost of equity.

DISCOUNTED CASH FLOW MODEL

After deciding the growth rate to apply, and the discount rate to use we managed to run a Discounted cash flow model to compute Campari's intrinsic value. Also thanks to the free cash flow projection illustrated below we can see that the **enterprise value** derived from the DCF is of **€ 10,999.24 mil**. After subtracting the net financial position and dividing by the number of shares we obtained the **share price of € 8.20.**

DISCOUNTED CASH FLOW MODEL

Year	2023	2024	2025	2026	2027	Terminal Value
FCFF	€ 70.20	€ 143.92	€ 331.64	€ 415.09	€ 498.64	€ 13,857.44
Disc. Rate (WACC based)	0.93	0.87	0.82	0.76	0.71	0.71
Discounted F CFF	€ 65.59	€ 125.63	€ 270.49	€ 316.31	€ 355.02	€ 9,866.19
ENTERPRISE VALUE						€ 10,999.24

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MULTIPLE ANALYSIS

CAMPARI'S MULTIPLES	
BOOK TO MARKET	0.13
P/E	34.18
PEG RATIO	3.42
EV/FCFE	85.37

Here below are the comments we would like to present for each of the four multiples listed in the table above:

- **Book to market** is well above the generally accepted threshold of 3, showing that Campari stock is trading many times more than its book value, suggesting it might be overvalued.
- **Price to Earnings** is above 30, a number usually associated with overvalued stocks especially if free cash flow growth is expected to lie in the high single digits.
- **EV/EBITDA:** this multiple is higher than the industry's median, "Beverage - Alcoholic" (source: Damodaran database), equal to 15.91. We again reach the conclusion that Campari's shares might be overvalued.
- **The EV/SALES** multiple is in line with the median of comparables equal to 4.07, industry: "Beverage - Alcoholic" (source: Damodaran database).

CONCLUSION

Considering the results of an Asset side discounted cash flow analysis we reach the conclusion that **on 11/28/2023 the stock is 20% overvalued** and therefore we take the decision of selling the stock.

The financial analysis of Campari Group highlights strong profitability and growth in regional priority brands, yet liquidity concerns arise due to recent acquisitions. The balance sheet reflects a rise in net financial debt resulting from strategic maneuvers, with an emphasis on positive exchange rate effects and an increase in net assets. However, the elevated long-term debt and a high debt-to-equity ratio pose solvency challenges. Notably, the P/E ratio surpassing the industry average indicates potential overvaluation. As the company undergoes leadership changes and pursues expansion in the Asia-Pacific region, prudent investors are advised to exercise caution.

OVERVALUED

Fair Price = €8.50
VS
Current Price = €10.21

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