# AUGA: Q1 2020 Results Review

**A good start to the new year**

AUGA Group ('Auga' or the 'Group') published a strong set of first-quarter results last Friday. The Group's revenues increased by 14.5% y-o-y to EUR 17.0m, which was 3.3% higher than the top end of our estimated revenue range. The revenues were supported by growth across all segments, particularly the crop growing and mushroom segments, which increased from EUR 5.1m and EUR 6.6m in Q1 2019 to EUR 6.1m and EUR 7.3m in Q1 2020, respectively.

The Group showed significant improvements in the consolidated gross and operating profits. The gross profit improved by 26.7% y-o-y to EUR 3.7m, and the operating profit rose by 43.9% y-o-y to EUR 1.6m.

Financial costs increased from EUR 1.0m to EUR 1.4m y-o-y, mostly on account of IFRS16 related interest expenses (which increased from EUR 0.3m in Q1 2019 to EUR 0.6m in Q1 2020) and nearly EUR 0.4m attributable to interest relating to the bond issue. Nonetheless, the Group still managed to generate a net profit of EUR 0.2m, which was 6.8% higher than the Q1 2019 net profit. Overall, we are satisfied with the Group's performance.

The Group has set a limit of EUR 6m for its 2020 capital expenditure, with its focus being set on:

*"securing its own organic combined feedstock production capacity, improving animal welfare and agricultural operations, allocating available resources to strategic development projects to follow a newly released five-year strategy that focuses on improving efficiency in existing business units, designing a sustainable organic food architecture and reducing greenhouse gas emissions."*

Below is the discussion about segmentwise performance:

- **Crop Growing**

The Group's crop-growing segment experienced a strong 18% annual increase in sales from EUR 5.1m to EUR 6.1m. However, the gross loss remained relatively unchanged at c.a. EUR 3.0m. The weather conditions, though, are favourable for the Group and the winter crops are in good condition. The Group mentioned that it has managed to properly prepare the remaining crops for spring sowing, which leaves it optimistic about this year's harvest potential.

- **Mushroom Segment**

The mushroom segment experienced a 10% annual increase in revenues from EUR 6.6m to EUR 7.3m. This was supported by the stronger harvest, though average selling prices were slightly down. However, the COVID-19 pandemic had some negative impact on the segment due to the loss of HoReCa clients (though this was compensated by retail sales)

| Key Numbers (EURm) | 2016 | 2017 | 2018 | 2019 | 2020* | 2021* |
|---|---|---|---|---|---|---|
| Sales (EURm) | 39.6 | 48.8 | 54.7 | 71.1 | 77.2 | 82.9 |
| Sales growth (%) | (16.4) | 23.1 | 12.2 | 29.9 | 8.6 | 7.4 |
| Net profit (EURm) | 2.2 | 4.9 | (6.0) | (3.0) | 2.2 | 5.7 |
| EPS (EUR) | 0.01 | 0.03 | (0.03) | (0.01) | 0.01 | 0.03 |
| P/E (x) | 42.3 | 20.5 | n.m. | n.m. | 36.9 | 14.4 |
| Payout per share (EUR)# | - | - | - | - | - | - |
| Payout yield (%) | - | - | - | - | - | - |
| P/B (x) | 1.3 | 1.3 | 0.9 | 0.9 | 0.9 | 0.8 |
| EV/Sales (x) | 3.1 | 3.0 | 2.5 | 2.4 | 2.1 | 1.8 |
| EV/EBITDA (x) | 12.1 | 10.7 | 32.6 | 10.1 | 7.5 | 6.2 |
| EV/EBIT (x) | 31.1 | 21.8 | n.m. | 152.9 | 18.5 | 12.6 |
| ROE (%) | 3.1 | 6.5 | (7.0) | (3.3) | 2.4 | 6.0 |

Source: Auga, LHV *2020E-2021E multiples are based on the share price (1st June 2020) of EUR 0.368 per share. # Payout per share include dividends and share capital reduction

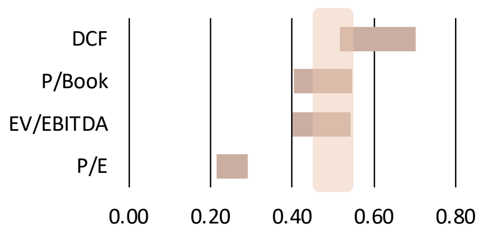
| Company Profile | |
|---|---|
| Listing Market: | Baltic Main List |
| Bloomberg Ticker: | AUG1L LH |
| ISIN: | LT0000127466 |
| Industry: | Consumer Goods |
| Sector: | Food & Beverage |
| No. of Employees: | 1,193 |
| Website: | www.auga.lt |

| Share Data, as of 1st June 2020 | |
|---|---|
| Current Share Price (EUR): | 0.368 |
| Fair Value Range, EUR (FVR): | 0.45-0.55 |
| Upside, % (to mid-point of FVR): | 35.87 |
| 52-week High/Low (EUR): | 0.406-0.260 |
| 3m Avg. Daily Volume (th): | 56.46 |
| Market Cap (EURm): | 83.69 |
| Ordinary Shares (m): | 227.42 |

| Key Shareholders, as of 31st March 2020 | |
|---|---|
| Baltic Champs Group, UAB | 55.04% |
| EBRD | 8.71% |
| ME Investicija UAB | 8.39% |
| Žilvinas Marcinkevičius | 7.00% |

**12-Month Price Performance**


**LHV Fair Value Range: EUR 0.45-0.55***




* As of 8th May 2020

| AUG1L LH : Results Review, EURm | Q1/20A | Q1/19A | % y-o-y | Q1/20E | Dev, abs | Dev, % |
|---|---|---|---|---|---|---|
| Revenue | 17.0 | 14.9 | 14.5 | 15.5 to 16.5 | 0.5 to 1.5 | 3.3 to 9.9 |
| Gross profit | 3.7 | 2.9 | 26.7 | n.a. | n.a. | n.a. |
| Operating profit | 1.6 | 1.1 | 43.9 | n.a. | n.a. | n.a. |
| Net profit | 0.2 | 0.2 | 6.8 | (1.1) to (0.9) | 1.1 to 1.3 | n.m. |
| | | | | | | |
| Gross margin, % | 15.5 | 23.4 | | n.a. | | |
| Operating margin, % | 6.7 | 8.9 | | n.a. | | |
| Net margin, % | 0.8 | 1.4 | | (7.1) to (5.5) | | |

Source: AUGA Group, LHV

| AUG1L: Segment Results Review | Q1/20A | Q1/19A | % y-o-y |
|---|---|---|---|
| **Crop Growing, EURm** | | | |
| Total revenue of sold agricultural produce | 6.1 | 5.1 | 18.4 |
| Total cost of sold agricultural produce | 6.0 | 5.1 | 17.5 |
| Total inventory write-offs | (0.2) | (0.2) | n.a. |
| **Result of sales of agricultural produce** | **(0.2)** | **(0.2)** | **n.a.** |
| Gain (loss) on revaluation of agricultural produce | 1.3 | 1.3 | (4.9) |
| Total subsidies | 1.9 | 1.8 | 7.5 |
| **Gross profit of crop growing segment per period** | **3.0** | **2.9** | **4.4** |
| | | | |
| **Mushroom Segment, EURm** | | | - |
| Total revenues from mushroom sales | 6.7 | 6.0 | 12.5 |
| Total cost of mushrooms sold | 6.2 | 5.7 | 7.9 |
| Total revenues from sales of mushroom seedbed | 0.6 | 0.7 | (15.4) |
| Total cost from sales of mushroom seedbed | 0.5 | 0.6 | (22.4) |
| **Gross profit of mushroom growing segment** | **0.6** | **0.3** | **117.9** |
| | | | |
| **Dairy Segment, EURm** | | | |
| Total revenues of dairy segment | 2.8 | 2.6 | 6.1 |
| Total cost of dairy segment | 2.5 | 2.6 | (5.7) |
| Revaluation of biological assets | (0.7) | (0.8) | n.a. |
| Total subsidies | 0.5 | 0.6 | (10.8) |
| **Gross profit of dairy segment** | **0.1** | **(0.2)** | n.a. |
| | | | |
| **End-Consumer Packaged Goods, EURm** | | | |
| Total revenue from end-consumer packaged goods sales | 0.9 | 0.5 | 78.7 |
| Total cost of sales of end-consumer packaged goods | 0.8 | 0.5 | 82.6 |
| **Total cost of sales of end-consumer packaged goods** | **0.1** | **0.0** | **37.2** |

Source: AUGA Group, LHV

and reduced compost sales to Russia (though this is not a large contributor to the segment). That said, the increased harvest resulted in a relatively lower cost of cultivated mushrooms. As a result, the segment's gross profit more than doubled y-o-y from EUR 0.3m to EUR 0.6m.

- **Dairy Segment**

The Group's dairy segment experienced a 6.1% y-o-y increase in revenues and managed to generate a small gross profit for the period, with improved operating efficiency. The Group stated that the growth was due to the increase in both milk yields and average selling prices. The average selling price rose on account of the shift from non-organic to organic milk (which now accounts for 86% of milk sold), with the latter commanding a price premium. In April 2020, the Group finally received organic certification from China for its milk.

- **Fast-Moving Consumer Goods ('FMCG')**

The fast-moving consumer goods segment experienced a significant increase of 79% y-o-y to EUR 0.9m during Q1 2020. The growth was witnessed across all markets, with the greatest growth coming from the US. With higher sales, the segment managed to improve its gross margin, though it still remains relatively small (at just above breakeven).

### Expected Efficiency Gains

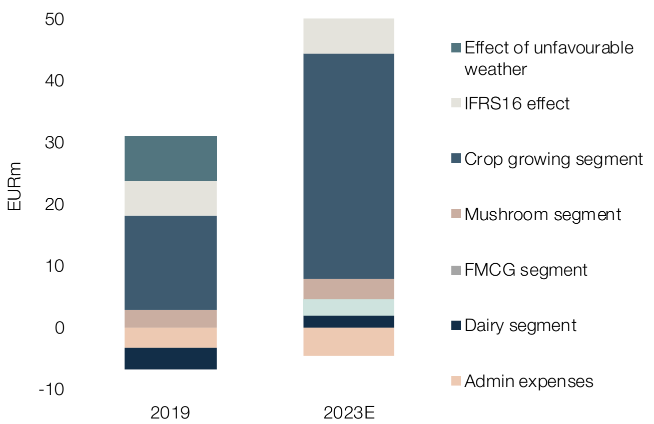
As a supplement to its Q1 2020 results publication, the Group presented more detailed information in terms of the planned efficiency gains that could be created by 2023 as a result of the below-mentioned strategy. On an EBITDA level, it is expected that the strategy (which includes an investment into efficiency improvements and re-investment of EUR 35.5m) could result in efficiency gains worth EUR 21.3m, taking EBITDA to EUR 45.5m in 2023, as depicted in the chart below.

This is a significant improvement expected by the Group across all of it segments, with the largest gain, in absolute terms, expected from the crop growing segment. Under these conditions, the Group plans to achieve the following targets:

- Debt service coverage ratio: at least 1.5x
- Annual dividend distribution: 25-50% of annual profits
- ROE on new investments: 20-25%
- Return on capital: at least 15%

We believe that this is a strong signal by the Group in terms of its future expectations. If the Group can achieve this result, which is significantly higher than our current estimates, it will become a formidable market player, both within the industry and as a blue-chip Baltic stock.

**EBITDA Potential**




Source: Auga

### SOFA Strategy

To follow on with its ESG policies and aiming to fully integrate sustainability into its culture, the Group has developed a new operating strategy that it has coined the "Sustainable Organic Food Architecture" ('SOFA') that will enable it to deliver climate (carbon and equivalent) neutral organic food.

SOFA allows the Group to position itself with consumers, farmers, lenders, and shareholders to align with their sustainable-centric preferences with their consumption, work, and investment activities. It will allow the Group to create the opportunity for high quality, healthy food at no additional cost to nature. As such, Auga plans to reposition itself as an, asset-light, agtech company that adopts a self-sufficient circular model and allows the world to live more sustainably. In doing so, Auga plans to integrate responsible technology that:

- aims to increase animal welfare and productivity;
- aims to minimise the effects on the environment; and
- proves such a track record valid for every unit of organic produce throughout the value chain.

Auga plans to meet the 2020s with an innovation agenda having the goal of becoming a $CO_2$ equivalent neutral player in organic food by 2030. To achieve this, the Group intends to:

- improve efficiency in existing business units to be able to align yields and costs structures between conventional and organic;
- design SOFA to create a multi-level innovation scheme to address the most pressing technological bottlenecks in the world of food production while retaining scale, quality, and yield productivity as it grows; and
- reduce $CO_2$ equivalent emissions to a minimum point through the value chain and neutralise the balance.

The Group is splitting the goals into short, medium, and long term strategies. It plans to achieve a twofold undertaking of increasing the efficiency of existing business units in the short-term (2020-2023) and constructing the SOFA in the medium-term (2020-2025). The Group's strategic initiatives for efficiency include the following:

- Crop growing segment foresees the introduction of regenerative crop rotation plans with more expedient seed mechanisms and a higher level of grass cultivation and processing efficiency, drawing from the best practices generated at AUGA academy.
- Dairy segment embarks on an initiative to increase animal welfare via a customised animal care programme, defining the key components of everyday well-being from milking to feeding.
- Mushroom growing segment seeks to revisit the entire cycle of the mushroom cultivation blueprint with the introduction of technology in key labour-intensive areas, such as picking and packaging.
- Fast-moving consumer goods segment undertake a mission to consolidate its market positions with own and private label brands, not only in established but also new markets.

| Sustainable for AUGA community | | | |
|---|---|---|---|
| **Consumers** | **Farmers** | **Private and Institutional Lenders** | **Shareholders** |
| Means eating while remaining aware that the most basic need is not inflicting damage on the planet but is helping to save it. | Means presenting farmers with an alternative standard of sustainability in agriculture. | Means empowering lenders to have the highest impact on the greening of the food value chain. | Means endowing shareholders with a threefold opportunity to multiply their investment, empower the future of the food value chain, and help save the planet. |
| **Success for AUGA in 2025** | | | |
| Ability to deliver consumer basket with the least cost to nature. | Functionality of the SOFA. | Resilience in business structure through long-term financing and impact-driven lenders. | Unique asset-light business model, able to demonstrate ROE ≥15%, multiply the Group value by 3x and retain growth dynamics in the periods to follow. |

Source: Auga

The SOFA that Auga plans to develop is a multi-level innovation scheme that addresses the most pressing technological bottlenecks in the world of farming. These include issues such as solving the cost to nature of the produce; namely, the ability to deliver climate-neutral food under the key conditions of an incremental increase in quality, efficiency, and yield productivity by 2030. This includes adapting three levels of technology into its SOFA blueprint (in addition to the existing closed-loop sustainable farming model), including:

- Biogas cycle infrastructure and vehicles to enable farm operations to run without fossil fuels, and tighter integration of the circular business model, whereby the secondary role of manure in the cycle will be utilised both for fertilisation, as well as for powering farm operations as biofuel.
- Specialised feed technology to reduce methane emissions from ruminants per animal unit and decrease the $CO_2$ equivalent emission rate per the corresponding group of products.
- Regenerative crop-rotation to substitute the share of cereal cultures with leguminous grasses that demonstrate carbon sequestration and nitrogen fixation capabilities, in an attempt to reduce the absolute rate of emissions and to become an integral part of livestock operations.

The Group is also working on implementing a practical set of standards for the consumer basket, which will be accompanied by a list of $CO_2$ equivalent emission reduction goals. By 2025, the Group is aiming to cut emissions from the use of fossil fuels on its farms by 40% (and by 50% in the consumption of fuels in its farming operations), methane emissions from enteric fermentation in livestock at least by 33% (and by 50% per tonne of cow's milk produced) and emissions from managed soil by 20% (and by 30% per cent per tonne of agricultural dry matter yield).

The SOFA strategy ties in with the EU's latest Farm to Fork strategy that was announced in May 2020. This strategy forms the base of the EU Green Deal, which aims to make Europe the first carbon-neutral continent by 2050. The strategy includes:

- Ensuring that at least 25% of agricultural land in the EU is organic by 2030 (currently it is 7.7%);
- Increasing the greenhouse gases emission reduction target to 50% by 2030 (or 55% compared to the 1990 level);
- Improving incomes of primary producers and reinforcing the EU competitiveness; and
- 50% reduction in the use of chemicals and hazardous pesticides by 2030.

Our fair value range for the Group is EUR 0.45-0.55 (closing price as of 1st June 2020 was EUR 0.368 per share).

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Date and time of sign-off: Tuesday 2nd June, 17:00

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