

Opening comments to conference call of Hawesko Holding AG

Nine-month interim report

30 October 2002

Mr Alexander Margaritoff, Chief Executive Officer

Mr Sven Ohlzen, Chief Financial Officer

Welcome, this is Alexander Margaritoff. Thank you all for taking part in this conference call, which we will be holding in English because apart from our friends in Germany we also have participants in London, New York and Australia.

I am joined by Mr Sven Ohlzen our chief financial officer, as well as Thomas Hutchinson, our Investor Relations manager.

The nine-month interim report was sent to you by E-mail and has been available on our hawesko.com corporate site, we have isolated the third-quarter figures with respect to the profit and loss statement to help your analysis.

Let me just recall a few points about the trading environment in Germany in the last few months:

At the beginning of the year we had the introduction of the Euro which created a great amount of uncertainty in our economy. We have had a very difficult political situation with the Irak crises and other crisis that did not help customer confidence. We have had an election here in Germany, we had a lot of public discussions about new taxes and levies, we have had a flood, we have had a very very difficult first nine months in Germany – in particular with respect to customer spending. In fact statistics show us that it's been the worst year in customer spending since the War.

Within this environment Hawesko has done very well and has built up its market position in the third quarter. Sales have increased by 8%, EBIT was up by 59% against last year. As regards to turnover we have now come to a point where in the first nine months of the year we have a slight positive aspect in our turnover. In contrast to this the German wine market has been down quite significantly. Consumer spending in Germany was down by approximately 4.5 – 5% in the first six months, spending on wine has been down as well by approximately 5% in the first three quarters of this year and if we look at the different segments in which Hawesko has been active we can see that most of our competitors are having a very difficult time.

In the mail-order business a number of our competitors are struggling along with one or two of them we believe will discontinue their activities. Our mail-order activities by contrast have been picking up.

In the retail business there has been a great deal of price-aggressive activity in particular from companies like Lidl and Aldi. Here Jacques' Wein-Depot has benefited by placing its focus on value-for-money propositions and I think that many customers are also gradually moving away from these super cheap shops towards our Jacques' activities.

In the wholesale segment restaurants in Germany have been having a terrible time, some businesses being down by up to 50%. Smaller wine-wholesalers have gone out of business or have been looking for a "white knight". Our wholesale business has had a good success, especially in the top class segment of Italian wines. Generally speaking despite the fact that there has been a very difficult economic environment and in particular regarding the fact that wine has been under pressure and in particular prices have been under pressure the Hawesko group has done a good job in the third quarter. I would like to ask Mr. Ohlzen to go into the details of each of these segments.

Mr Ohlzen:

Good afternoon. I would like to start with the group sales of the third quarter. The Hawesko Group posted sales of € 57.8 million in the third quarter, which is an increase of 8 per cent against the third quarter of 2001.

We have an interesting pattern this year in the quarter-on-quarter development: Q2 was stronger than Q1, and now Q3 has been stronger than Q2. The typical pattern for years was a relatively strong Q1 followed by a weaker Q2, followed by a yet again weaker Q3. We see this year's development as a confirmation of our general forecast scenario, which calls for a stronger second half.

The gross margin you see in the nine-month report is 43.0%, against 41.2% last year. In the third quarter alone, the group showed a margin of 43.8%, against 41.4% in last year's third quarter. This improvement reflects a conscious effort to focus on higher-margin products in the sales mix.

Personnel costs in the group for the nine months represented 11.1% of sales, as opposed to 9.9% of sales last year. Most of the increase in personnel took place in the wholesale segment, where the increase in business – for example with Italian top wines – required more manpower.

On the other hand, we have in the mail-order segment a certain base capacity of personnel irrespective of momentary sales volume. As we move into the fourth quarter and closer to the all-important Christmas business, we have taken on the seasonal workers in the mail-order segment later to handle the expected volumes. If the expected volumes do not materialize, we can adjust the seasonal force to some degree.

The biggest position in "Other operating expenses" is advertising expense (€15.2 million (8.8% of sales), last year: €14.7 million, 8.6% of sales), sales commissions mostly to Jacques' Wein-Depot partners (€14.6 million, 8.5% of group sales; last year: €14.0 million 8.2% of group sales) and delivery costs (€7.2 million, 4.2% of sales; last year: € 6.8 million, 4.0% of sales).

This constant level of advertising expense does not give you the full picture, as we have been able to improve the quality of mail-order advertising – for example, now with printed envelopes for the mail-shots – and have produced one additional "Jacques' Journal" customer magazine for this same level of expense.

Operating profit – EBIT – , was € 5.2 million for the nine months (€ 6.2 million last year), or € 1.5 million for the third quarter (€1 million last year).

Now in greater detail the business lines:

Mail-order/E-commerce had sales of € 21 million in the third quarter, up 6% against last year. Sales of *Hanseatisches Wein- und Sekt-Kontor* were € 17.3 million (third quarter 2001: € 16.5 million) Tesdorpf sales amounted to € 1.2 million (third quarter 2001: € 0,7 million), sales in Austria were € 500 thousand (third quarter 2001: € 480 thousand), and *Château Classic – Le Monde des Grands Bordeaux* made sales of € 2 million (third quarter 2001: also € 2 million).

Mail-order/E-Commerce EBIT in the third quarter was a positive € 100 thousand, marking a swing from the negative € 150 thousand in the third quarter of 2001. The EBIT margin for this segment was 0.5%.

For the full year 2002 we expect sales in the mail-order segment to be slightly down against last year – Alexander Margaritoff will say a word about this in a minute. For the EBIT margin we think we can at least maintain last year's 5.9% and end up around 6%; after nine months we are at a 2.6% EBIT margin last year's EBIT margin after nine months was 1.8%.

Wine shop sales (Jacques' Wein Depot) were € 19.7 million in the third quarter, up by 9% against last year. The like-for-like sales in the quarter were up 1.5%, which could be achieved in spite of a declining average spend due to higher customer traffic. We must assume that the lower average spend will continue. We think we can continue to compensate for this in part through generating higher traffic, and will adjust the advertising to reflect the change in the types of products customers are demanding. The EBIT margin in the quarter was 6.6% (last year: 8.9%), down mostly because more depot locations are now being renovated. In this environment it is important to maintain the attractiveness of Jacques against the "only-cheap-wine" sellers.

For the full year of 2002 we now expect sales to be about 7% higher than the € 85 million from last year; and the EBIT margin to be at about the 9% to 9.5% level.

In **wholesale** we were able to post a 7.8% increase in sales in the quarter to € 17.1 million, of this, Wein-Wolf made € 15.1 million (€ 13.9 million last year) and CWD with € 2 million (€ 1.9 million last year). The biggest reason for the increase was sales of top Italian wines. EBIT was € 1.2 million so that the EBIT margin in the quarter was 7.3%, much improved on last year's third quarter of 0.4%.

We expect basically slightly higher sales in this segment for the full year 2002 (last year: € 73 million), and an EBIT margin of about 5 to 5.5 per cent on segment sales for the full fiscal year 2002.

The position "**Miscellaneous and Consolidation**" in the "Segments" section of the report on the last page relates to the Viniversität, our company which offers wine-appreciation courses; our in-house logistics and fulfillment provider, IWL Internationale Wein-Logistik, which runs the distribution center near Hamburg; as well as headquarter costs and consolidation items.

This position in the third quarter was just under € 1.1 million, against last year's € 500 thousand. The increase in costs in the third quarter are mostly due to extra work for the introduction of a new computerized fulfillment system. As you will remember at the half-year report, this system has proven to be more difficult to implement than we anticipated.

To the end of the year, we continue to expect the items in this position to come to about € 4.2 million, maybe a shade less (last year € 2.7 million).

Finance expenses in the third quarter were € 1.1 million. Of this amount, € 0.4 million were due to an IAS 39 non-cash expense and relate to interest-rate derivatives marked down to fair value. The derivatives were designed to hedge against rising interest rates. The **tax charge** for the quarter was € 0,2 million (last year a tax credit due to that quarter's loss). The charge for **minority interests** in the quarter was € 160 thousand, higher than last year's € 22 thousand due to the large amount of business done with Italian specialty wines through the wholesale subsidiary Ariane Abayan.

Net profit for the third quarter was € 68 thousand, against last year's loss of € 180 thousand.

Compared to the end of 2001 the **balance sheet** shows basically an unchanged sum total.

On the assets side there was a reduction of trade receivables of about € 12 million down to € 21 million and an increase of inventories of about € 14 million up to about € 91 million.

These changes are mostly due to seasonal influences – money is collected from Christmas sales after 31 December, inventories go up in the autumn before the next Christmas.

Typically one can expect inventories at 30 September to be 33% of trailing 12-month sales, which would be € 89 million at 30 September 2002. The € 3 million in inventories above this expected value are due to premium Italian wines such as Ornellaia and Cavalli. These wines are very popular and in demand; in the case of Ornellaia this inventory will allow us to continue selling into next year, when we will no longer have the distribution rights. Our best estimate for closing inventories is about € 82 million on 31 December 2002. I will come back to this point when I discuss cashflow.

The **cashflow statement** shows a cash outflow from operations of about € 12 million, as opposed to an inflow last year of € 5 million. The biggest swing factor is in the "Change in other short-term assets" of € 8.8 million against last year. At that time, we had cash inflows from the proceeds of a Sale- and Leaseback deal related to the office facilities in Tornesch of € 2.6 million and from tax refunds collected of € 3.6 million.

To the end of this year we expect cash flow from current operations to be between € 4 million and € 6 million.

This assumes closing inventories of € 82 – 84 million, as mentioned before, which is the biggest position in Hawesko's working capital. It is our best estimate, but could be affected by Christmas sales and their timing (early or late in December) on the one hand. On the other hand we are working on further actions to reduce working capital by the end of the year and beyond, which Alexander Margaritoff will address.

In short, we have temporarily come off the normalized cashflow track but are addressing the situation and actively working on the solution. And the cash has flowed into assets of value – namely, premium inventories with great demand in a growing part of our market – on which we will earn the cost of tying up this capital.

I now hand over to Alexander Margaritoff.

Mr Margaritoff

Yes, thank you.

Let me say a few more words about the fourth quarter. We were very satisfied with the third quarter and in fact we are looking forward to the last couple of months of this year. If we look at each of the different segments individually:

In the last few weeks in the mail-order business we have had very good order inflow at Hawesko. In fact we almost had 40% more orders in the last six weeks than in the same period of last year, which is quite substantial. The individual orders were lower in value but it shows that the development of our customer base is very positive. In this respect we are quite confident. Our new main catalog is coming out in the next two or three days, it is a bigger catalog it has more pages it is slightly more aggressive in its entire tone and we are very much looking forward to this catalog because we think it is going to be very well received amongst our customers. As usual the last couple of months the main aspect of our business is the Christmas gift business. The catalog has been out for some time and traditionally christmas business has been 80% B-to-B and 20% to private customers. Business to private customers has been quite normal until now; what has been rather sluggish was business from other companies which I think reflects the mood in Germany today. We hope that this is going to pick up in the next few weeks but it is very difficult to say what is going to happen. It very much depends on the mood in the country, it very much depends on the last six to eight weeks before the end of the year what the Christmas gift business is going to be like. We are relaunching our "hawesko.de" site next week. It is a newly-overhauled site which will be simpler to navigate and have a few features like a call-back button and other things that make it easier for customers to order in particular for the gift-business. This is an important aspect of our mail-order business and here again we think that we have done a good job.

On the whole in the mail-order business we are – as Mr. Ohlzen mentioned – taking a number of steps to reduce inventory and in particular our new general manager Mr. Paul Smyth has committed himself very strongly to reducing inventory investments now and in the next year. We are also looking at our entire process of taking care of orders from the time that a customer places his order to the time the goods leave our warehouse. This whole process has grown organically over the last years and is now being looked at very closely for improvements, not only in efficiency in time but also from the point of view of costs.

Jacques' Wein-Depot our shop-business here again as Mr. Ohlzen mentioned we are expanding there. There are two ways of looking at the business: One is the expansion of individual shops – increasing the number of shops – as of the first of January until the 30 of September we have secured 27 new shops in Germany which is more than ever before in the first nine months of the year this is very positive. We have been helped by a sometimes desperate situation in the retail business where many shops have gone out of business and we were able to secure very good locations. This is the one way of expanding our business. The other way is to acquire new customers for existing shops. This has never been done before at Jacques, we have had a test at the beginning of the year, another one in the summer and a third one now in October. These first tests have been very positive – we believe that in the future we will be able to acquire new customers for existing shops which should increase the profitability of each shop and also improve the possibility of getting new shops in Germany. It really is a question of getting the right mix between opening new shops and acquiring customers for existing shops. But I think we are doing a good job and as mentioned before we have opened more shops than ever before in the first nine months of the year.

In the wholesale business our main emphasis has been to improve our wine portfolio and this is what is going to be the main emphasis in the next months and years. We have had a tremendous success with Antinori in the last year and the first months of this year, we have also introduced Penfolds very, very successfully. We now have got four new top-exclusivities in France for our CWD wholesale-business, in Italy we have managed to get the exclusive rights for Collavini (Friaul), Biondi Santi (probably the top producer in Tuscany) as well as a couple of other italian producers, we have been quite successful here. This is something which is not only helping our wholesale business but it is part of our group strategy and obviously helps the shop-business as well as the mail-order business. Looking at just a few targets within the entire group I think as Mr. Ohlzen has mentioned we are looking very carefully at our cash-flow and working on it in great detail to improve this. We are looking at increasing the efficiency of our use of capital and this has become a criteria for some of our managers' bonus payments. That might do the trick. We are also working on better payment conditions and purchasing conditions with our suppliers to optimize working capital investment.

To wind up a general view of the situation, at the moment Germany is a very difficult place to do business in. In particular the retail business has been very, very sluggish. In fact some people say it has been dramatic. The government has not really been helping the situation with its continuous discussion about tax increases and other things. I think that within this context we have been doing very, very well in particular in the third quarter with respect to the market situation and with respect to our competitors. Generally speaking we will come out of this difficult economic situation with a much stronger position, with better systems, with better profitability and with a larger market share for Hawesko Holding AG – for the entire group.

Thank for your attention.