THE BIG STORY

How Conviviality lost its fizz

Once the toast of the town, Conviviality now looks likely to go bust. Luke Tugby reveals what went wrong

As remarkable as it sounds given the benefit of hindsight, at the beginning of the year Conviviality was one of the darlings of the City.

The Bargain Booze and Wine Rack owner was actively tackling the seismic changes sweeping across the retail and wholesale industries with what retail watchers described as a "visionary" strategy.

In addition to growing its store-based footprint, the business snapped up the UK's largest independent drinks distributor, Matthew Clark, for a cool £200m back in September 2015.

And it followed up that acquisition by purchasing wine wholesaler Bibendum for £60m the following May, transforming Conviviality into a supplier to thousands of pubs, bars and restaurants across the country.

The ambitious growth blueprint to combine retail and wholesale – a precursor to Tesco's £3.7bn swoop for Booker and the supply deals Morrisons struck with both Amazon and McColl's – appeared to be one that would future-proof the business.

Instead, it has sparked Conviviality's demise. The business revealed last month that it has filed a notice of intention to appoint administrators following a tumultuous start to the year.

What makes the alcohol specialist's rapid fall from grace all the more shocking is the fact that nobody appeared to see it coming.

Diana Hunter

Bungled acquisitions

Conviviality's numbers, on paper at least, told the story of a business in rude health.

In its last full year to April 30, 2017, pre-tax profit surged 147% to £22.5m as revenues climbed 85% to almost £1.6bn. As Shore Capital analyst Phil Carroll says: "Sales were improving, the 'one-stop shop' model seemed to be gaining traction and 2017 numbers were in line with what we expected.

"There was no reason to believe that there were any issues."

Indeed, Conviviality itself hailed the progress it had made during a "transformational" 12 months, while then-chief executive Diana Hunter, who exited the business last month, voiced her "confidence in the future success of the business".

Maybe even Hunter herself wasn't aware of it at the time, but those words masked an operation that was unravelling behind the scenes.

The trigger? Not the £30m tax bill that Conviviality's stock exchange statement led many onlookers to blame for its failure, but the "extremely problematic" combination of the Matthew Clark and Bibendum businesses.

Central to Conviviality's masterplan was driving synergies by consolidating the back-of-house operations at the wholesale businesses, working together under the Conviviality Direct banner. But that cost-cutting drive is said to have dominated – and ultimately hindered – the company's strategic progress.

"The pressure to take cost out was enormous and they rushed at it like a bull in a china shop," one source says of Conviviality's "bungled" attempt to integrate Matthew Clark and Bibendum.

"Fundamentally, the back of the business didn't keep up with the front of the business," another well-connected source adds.

It seemingly created a situation where Bibendum's stock was consolidated into Matthew Clark warehouses, but Conviviality's systems – described as "outdated" – would not allow it to get those products back out of the depots to its customers.

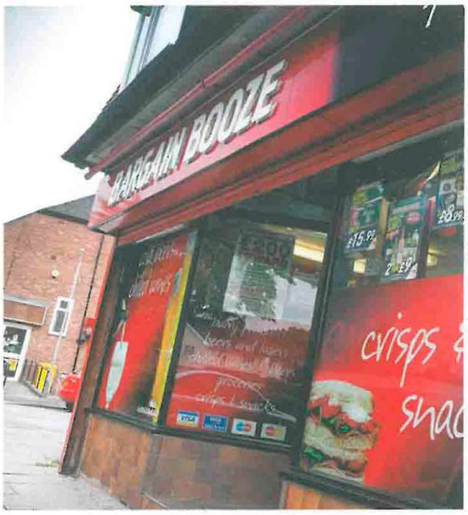
As a result, pub, bar and restaurant clients suffered a lack of availability, and understandably refused to pay up.

Conviviality was consequently left short of cash and unable to pay its own suppliers.

Aggressive sales tactics and zero margins

Remarkably, it is believed that Conviviality staff, clients and suppliers all failed to shout about the problems loud enough until it was too late.

Even when the missed payments to its suppliers were uncovered more widely, management were said to have seen it as a "weakness, not a burning bridge".



Their salesmen were being told to pursue sales at all cost. That always ends in tears

But the latter is exactly what it ultimately became. Rather than costs falling, Conviviality was compelled to take manual measures to fulfil orders placed by clients – and keep stock on shelves at Wine Rack and Bargain Booze.

Retail Week understands that Conviviality employees were embarrassingly forced into buying key lines such as Champagne and Prosecco from various supermarket operators and Majestic Wine stores, at retail prices.

While that clearly had a negative impact on margins within the Direct wholesaling arm, the margin squeeze was already being felt as a result of what have been described as "aggressive" sales tactics.

Supply deals were being struck with big, often nationwide clients at "either very fine or zero margins", one source suggests.

"The logic was to go and secure the sales, then take so much cost out of the operation that, although margins were poor today, their contracts would become profitable by the time the costs had been taken out."

Another person close to the business tells Retail Week: "Their salesmen were being told to pursue sales at all cost. That always ends in tears."

Indeed, it did. Conviviality issued a profit warning at the start of March, which it attributed to "a material error" in forecasts and a "softening" of margins.

It is understood the business "rushed through" an 8% price increase to its customers in February – when those contracts were not due for renewal for another five weeks – in an attempt to boost ailing margins.

Even with what Conviviality described as "appropriate corrective actions" being implemented, there was more bad news to come.

Tax turmoil

Its shares were suspended when markets opened on March 14, and hours later Conviviality dropped the bombshell that it had "identified" a £30m tax bill which had apparently "not been accrued for within its short-term cash-flow projections".

Sources close to the business lament the "very bad" communication around the tax bill and insist that the payment wasn't as unexpected as the stock exchange statement made it sound.

The regular payment was, seemingly, in its ledgers, but had been caught up within "archaic systems", one source suggests.

After the £30m bill emerged, leaving it with cash-flow problems, Retail Week understands that the Conviviality board and representatives from PwC were locked in a meeting until the early hours of March 14 discussing its options.

When those talks ended at around 2am, they were unaware that AIM was preparing to suspend trading in its shares.

That decision was made shortly before markets opened, leaving Conviviality with limited time to cobble together a reactionary statement to explain the situation.

"The problem with the statement is that it raised all sorts of questions around the credibility of the business and that in turn has caused fears among stakeholders, whether it be customers, suppliers or otherwise," Carroll says.

"Suppliers would be unwilling to supply the business with product, and customers were probably going elsewhere to guarantee they receive their orders."

Search for investors

As credit insurance quickly "drained out of the business", similar fears were stoked among the investor community – the same community Conviviality had hoped to tap up to raise the £125m required to "recapitalise the business" through a share placing.

Conviviality is thought to have approached around 50 institutional investors – and it is understood the business came within £10m of reaching the sum that would have paid off banks, suppliers and other creditors, securing its immediate future.

Yet one industry insider insists he is not surprised the placing failed. "The investment required to fix the business from where it is now would be so completely out of proportion to the benefit," he concludes.

But with Conviviality insisting that a number of parties are interested in acquiring all or part of the company, can it yet be saved?

Privately, management continue to insist that Conviviality is a "good business that has gone wrong" and maintain that its failed acquisitions of Matthew Clark and Bibendum were the correct strategic moves.

Carroll agrees. "Fundamentally, there is value in the businesses. I'm massively surprised it's got to this stage," he says. "The risk at the moment is that they are losing suppliers and customers so fast that it could all fall apart. Something needs to be done sooner rather than later to avoid that happening."

If a white knight does step forward, it is likely to take heaps of time and money to restore Conviviality's status in the City. **RW**