

Beverage market update

Industry Consulting Team | Q4 2021

Joseph Goode

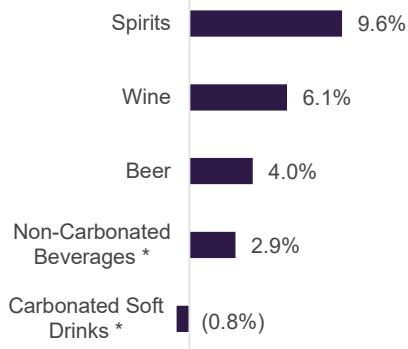
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Table 1

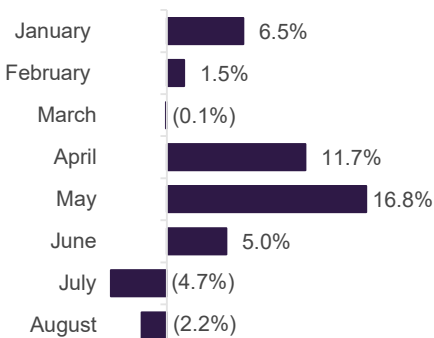
Total Beverage Industry Volume YTD August 2021 vs. 2020



* CSD & NCB data as of Q2-21

Table 2

2021 vs. 2020 US Beer Volume Dom & Imp Shipments by Month



1: Unless otherwise noted, YTD and YoY statistics throughout the newsletter reflect data through August 2021

Highlights

- The total Beverage category continues to perform well in 2021; volumes and pricing have sustained and in most cases surpassed 2020 levels although degrees of softness are developing with tough Q3 & Q4 comps
- Beer posts growth through YTD August; however, volumes fell short in key July / August summer months
- Wine & Spirits accelerate growth trends and emerge as strongest segments of Total Beverage Alcohol (TBA)
- Non-Alcoholic (NA) beverage volumes yield mixed results in first half of 2021, Carbonated Soft Drinks (CSDs) face steep 2020 comps while Non-Carbonated Beverages (NCBs) continue growth trajectory

2021 Industry Trends & Observations ¹

BEER: Beer trends continue to grow with total domestic + import YTD volume gains of ~4.0% through August. Domestic shipments increased 1.8%, while imports shipments jumped 14.7% during the same period reflecting international COVID forced closures in FY20 and an improving although still challenged supply chain. Mexican shipments which account for nearly 74% of all imports gained ~17% YTD. Despite strong growth YoY the beleaguered Mexican supply chain remains challenged causing wide spread inventory shortages and out-of-stocks in many markets. Inventory and supply chain issues will likely carry into 2022 before abating. Hard seltzers remain as the other hot sector in broader beer. Hard seltzers will approach \$7Bn in sales in FY21 and the segment is still growing in the +20% range; however, growth rates have slowed from their triple digit rocket ship. As discussed throughout, seltzers and RTDs are arguably the most competitive space in all of beverage right now. COVID reopening trends have continued, but the spreading Delta variant has slowed the full return to the on-premise.

SPIRITS: The spirits sector continues to demonstrate strength over other bev-alcohol industries with YoY volume growth of 9.6% through August 2021. Spirits' growth has actually accelerated in 2021 with 9, 6, and 3 month volume gains increasing from 10.4%, 12.7%, and 15.0% respectively. Similar to hard seltzers in the beer category, Ready-to-Drink (RTD) or canned cocktails have emerged as a growth engine within the broader spirits sector posting +45% YoY growth on a still small but rapidly expanding base. Spirit based RTDs are becoming a meaningful competitor to malt based hard seltzers despite sales channel restrictions and generally higher price points due to higher tax levels. Tequila is the other rising star in spirits gaining +27% volume YoY. Tequila and similarly mezcal brands have observed years of consistent growth but through FY20 and 21 growth has accelerated. Discussed further below the premiumization of beverage brands has been widely noted as consumers continue to seek out higher quality products; however, in certain categories premiumization trends have exploded. Other spirits segments have moderated illustrating the strong comps from FY20. Vodka declined (1.6%) as well as gin which fell (4%) while rum and whiskey have edged higher at 1.6% and 2.8% volume gains respectively.

WINE: Total wine volumes increased just over 6% YoY led by still wines and the 'All Other' segment which includes sangria, coolers, and wine based RTDs. Like spirits, wine based RTDs are still a small segment within the wine category, but driving meaningful growth. All Other - sangrias, coolers, and wine based RTDs - increased nearly 17% YoY and contributed more than 40% of the wine category's volume growth through August. Domestic table wines showed continued health adding nearly 2% in volume terms while imported table wines gained 8% YoY. Table wines make up more than 75% of total wine sales, so while total table wines grew 3.3% they contributed +40% of wine's total category growth. Sparkling wines showed marked improvement growing nearly 15% YoY, cycling past periods of COVID forced closures and rebounding as the supply chain is being restored.

NON-ALCOHOLIC: Total Non-Alcoholic beverages (NAs) are keeping pace YoY through Q2 of 2021 comping some of the pantry loading and panic buying weeks of 2020. Energy and sports drinks are leading category growth with volume gains of 15.1% and 11.5% through Q2-21, respectively. Carbonated soft drinks have slowed facing tough comps from FY20 with volume declining just under (1%) YoY. Keurig Dr. Pepper (KDP) continues to lead in CSDs with 2.6% volume gains, ahead of PepsiCo's 0.5% while The Coca-Cola Company declined (1.2%). Enhanced and flavored waters continue to show strong trends increasing +8% YoY, followed by plain bottled waters gaining 6.2% in volume and RTD teas added 4.7% in volume terms through Q2-21. The "Healthier / Better-For-You" trend is still clearly a top influencing factor of consumer's purchasing decisions.

Beverage Sectors In-Focus

SPIRITS ARE HIGH IN THE LIQUOR INDUSTRY – Recently attending the DISCUS conference in Austin, TX the energy and excitement in the room and throughout the conference was palpable; and rightfully so. The spirits industry is riding years of strong growth and growth is accelerating through 2021 to nearly 10% volume gains as we note above. RTD cocktails have expanded rapidly through 2021 growing +45% YoY and accounting for more than 15% of the total spirits category's growth. Thus far base liquids in RTDs have been concentrated in vodka and gin, but tequila and whiskey based cocktail innovations have come on strong in recent periods to broaden RTD offerings further. Beyond RTDs, Tequila and mezcal has been a leading segment within the spirits industry outpacing total category growth since 2013. In FY 20 Tequila and mezcal eclipsed 22 million 9L cases, growing 10.2% YoY. Through August 2021 tequila / mezcal volumes are up ~27% YoY, now totaling more than 28 million 9L cases. Tequila & mezcal accounts for more than 25% of the total spirits industry's gains during the same period.



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Beverage Sectors In-Focus (Continued)

Diving deeper into the tequila and mezcal segment, high quality super premium and luxury priced products have emerged as the category leader. Prior to 2013 the premium price category led tequila and mezcal both in terms of volume and revenue; however, super premium and luxury priced products have consistently outpaced other price segments over the last decade. Super premium brands have averaged volume growth of 12.7% over a 10-year period compared to 5.3% in the premium segment and 1.7% growth in value priced brands. Super premium and luxury brands now account for 23% of total tequila and mezcal category volumes but make up 47% of total category revenues.

DISCUS recently published their Luxury Brand Index tracking brands with retail price points of more than \$50 per 750ml bottle across spirit categories; highlighting the tremendous growth being observed at the highest pricing levels throughout the industry. DISCUS outlines that luxury priced brands only make up 3-4% of total industry volumes reflecting ~105 million bottles and +\$10 billion in revenue. Luxury brands have also developed differently across spirits categories, making up +/- 30% of the cognac segment, but estimated at only ~2% of American whiskey. The index tracks cognac, American whiskey, Irish whiskey, Japanese whisky, scotch whisky, and tequila. Consumer's ongoing premiumization from lower priced products to higher priced brands has been widely recognized and observed across the bev-alcohol space, but consumer's willingness to up-tier and invest in their spirit selections is driving out paced growth and shifting the spirits category into another gear.

American whiskey represents another category moving heavily towards super premium and luxury price points. Over the 5-year period from 2015 - 2020 American whiskeys have generated a total category CAGR of 8.3% while the luxury priced tier grew 41% over the same period. Similarly the tequila category has increased 11.4% CAGR over the 5-year period while top end luxury brands gained ~31% at the same time. See the table to the right for additional comparisons of cognac, Irish whiskey, and scotch categories.

What is driving consumer interests in top shelf brands? There is no singular event or catalyst that has empirically reprogrammed consumers; however, several events and supporting themes that are occurring, some of which for years. For example, spirit brands have long been marketing the prestige, allure and sophistication of their products, and in lieu of straight line price increases at retail spirit companies have increased pricing levels through innovations and product mix. Add in the widespread closure of on-premise accounts, which per the National Restaurant Association reallocated approximately \$25Bn of consumer discretionary dollars back into consumers' pockets. Stuck at home consumers redeployed those dollars in various ways, including the enjoyment of top shelf liquor as a now affordable luxury item. While these themes are merely supporting factors of what is being observed across bev-alcohol and particularly the spirits industry, one fact is, consumers are voting with their dollars and they're voting super premium and above.

SHAKING IT UP IN THE NON-ALCOHOLIC SPACE – In past memos we've covered the convergence of the historically segmented bev-alcohol industry where beer, wine, and spirits are all vying for the same shelf space through hard seltzers and RTDs. Now NAs are making their move into the category. Coca-Cola announced through a partnership with MolsonCoors the expansion of their Topo Chico brand into a new hard seltzer product which will be a national brand by FYE 21 and is distributed by the MolsonCoors network of distributors. Then PepsiCo. announced their entry with a new Hard Mountain Dew brand which will be produced in collaboration with Boston Beer Co.. Interestingly, PepsiCo. will set up a new distribution arm dubbed "Blue Cloud" as a distributor of their new Hard Mountain Dew offering. It is believed Blue Cloud will service a number of markets with the remaining distribution being facilitated by a combination of existing Pepsi bottlers and Boston Beer wholesalers. In our opinion, the creation of Blue Cloud clearly signals a strategy from PepsiCo. to build a portfolio of alcoholic brands over time. There are certainly more efficient ways to distribute Hard Mountain Dew if it were a singular concept. More importantly, these moves mark a departure from long term core strategies of NA companies staying in the non-alcoholic space and out of bev-alcohol. As we've observed and reported, nearly every large beverage company is now focused on becoming a "Total Beverage Company" playing in multiple sectors and segments. Only time will tell what the ultimate outcome and impact these shifts will have on brand strategies, M&A, and distribution.

Premiumization and innovation are the other prevailing undercurrents within NAs. Consumers moving up in price tiers into premium products is being led by innovation and enhancements. Through 2020 and continuing into FY21 premium and enhanced products are outpacing traditional lines. Enhanced and flavored waters are accelerating beyond plain bottled waters growing at +8% vs. 6% respectively. Energy and sports drinks are eclipsing traditional CSDs at +15% and +11% vs. (~1%), respectively. With consumers shift towards "Healthier" and "Better for you" interests they are being met with functional innovations all at a premium price. Companies will welcome the added margin, but must manage the shift from large traditional product lines and the cost and complexity of innovation.

Table 3

US Wine Industry YTD August 2021 vs. 2020

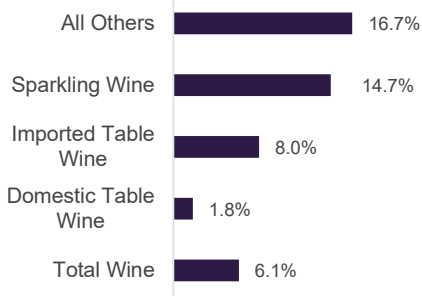


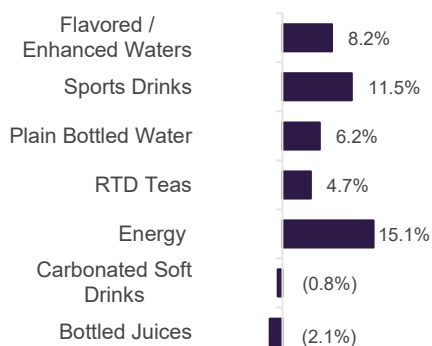
Table 4

US Spirit Industry Volume YTD August 2021 vs. 2020



Table 5

Total Non-Alcoholic Beverages YoY Q2-21 Volume Trends



Luxury Brand Growth vs. Total Category

