Beverage market update

Industry Consulting Team | Q2 2022

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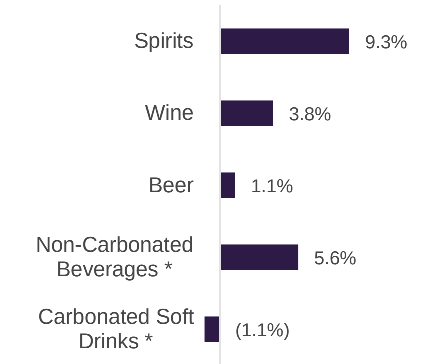
Table 1

Total Beverage Industry Volume LTM March 2022 vs. 2021 *



** CSD & NCB data as of YE 21*

Table 2

US Spirit Industry Volume YoY LTM March 2022 vs. 2021

1: Unless otherwise noted, YTD and YoY statistics throughout the newsletter reflect data through Q1-22

Highlights

- The total Beverage category continued to perform well through 2021 and 1Q’22; broadly, markets are recalibrating as the on-premise channel reopens and consumption returns shifting back from the off-premise
- Wine & Spirits accelerated growth over Beer; Wine +3.8% YoY LTM through 1Q’22 while Spirits are +11%
- Beer shipments are stable at +1% YoY through LTM 1Q’22; despite rocky start in Jan/Feb
- Non-Alcoholic (NA) beverage volumes continue to show mixed results FYE 21, Carbonated Soft Drinks (CSDs) faced steep 2020 comps while certain Non-Carbonated Beverages (NCBs) continue to grow

2022 Industry Trends & Observations [1]

NOTE: Certain data sources typically cited in the newsletter have been delayed and are not yet available. As a result, the trend analysis below has been slightly abbreviated.

BEER: Beer trends through Q1’22 have been somewhat mixed. Volumes started the year out soft in January and February and then rebounded in March. Beer shipments for the quarter increased 1.7% YoY and maintained a modest growth on an LTM period at +1%. While volumes bounced around during the quarter, many suppliers took sizable pricing increases across their portfolios, which have pushed revenues higher, broadly. Imports and particularly Mexican imports have continued to perform strongly. Total imported beer shipments gained nearly 10% YoY on an LTM basis led by Mexican imports, which grew at nearly twice the total category rate at ~18% during the same period. Large suppliers Anheuser Busch InBev (ABI) and Molson Coors (MC) produced mixed results with ABI being flat on shipments YoY LTM Q1’22 while MC saw shipment volumes drop slightly less than (1%) during the same period. As noted above, consumers are migrating back to the on-premise trade which jumped ~84% YoY compared to the off-premise channel that observed a (7%) decline during the same period.

SPIRITS: The spirits sector continued its strength over other bev-alcohol categories with YoY volume growth of more than 11% through LTM ending 1Q’22. Within spirits, the Ready-to-Drink (RTD) or canned cocktails have continued their meteoric rise posting +58% YoY growth on a still small but rapidly expanding base. RTDs only account for roughly 5% of spirit volumes but contributed more than 20% of the entire category's growth YoY through LTM 1Q’22. Tequila is the other part of the category that remains on fire growing +20% YoY on a volume basis. Total Tequila revenue growth exceeds volume gains given the particularly strong growth in high-end and luxury tier pricing segments. Whiskey continued to show strong gains at ~8% YoY. Whiskey’s ongoing growth is impressive given the segment’s size as the second largest spirit category by volume and the largest category by revenue. Other spirits segments demonstrated mixed results with vodka declining (2%), gin was +3% while rum declined (~6%).

WINE: Total wine volumes increased ~3.8% YoY through LTM 1Q’22, led by sparkling wines. Sparkling wine snapped back from soft comps in 2020 and early 2021 gaining volume by nearly 35%. Table wines continue their strong growth adding 3.8% YoY for the total category. Domestic table wines were flat at 0.4% growth, while imported table wines drove the category increasing 12.7% during the same period. Table wines still make up more than 80% of total wine sales, so strong table wine performance is critical to the category‘s health.

NON-ALCOHOLIC: Total Non-Alcoholic beverages (NAs) delivered mixed results through FY 2021 comping periods of pantry loading and panic buying weeks from 2020. Energy continued to lead the category in growth for FY21 with volume gaining 12.8%. Carbonated soft drinks have slowed with FY21 volume declining (1.1%) in the face of tough comps from FY20 along with the ongoing shift to other more health-conscious carbonated beverages. Keurig Dr. Pepper (KDP) led in CSDs with 1.6% volume gains, ahead of PepsiCo’s and The Coca-Cola Company’s (0.6%) and (1.1%) declines; respectively. Enhanced and flavored waters are another expanding category within NAs and one of the direct beneficiaries of the increasingly health-conscious consumer. Enhanced and flavored waters gained ~9% YoY, followed by plain bottled waters +6% in volume at FY21. Lastly, sports drinks and functional beverages showed good growth at 5% in FY21 and are squarely on-trend with where consumer purchases and behaviors are aligned.

Beverage Sectors In-Focus

The Impact of the Russian Invasion in Ukraine – Russia Invaded Ukraine on February 24th of this year which created uncertainty both on a human and economic level. Ukraine is widely known as the breadbasket of Europe while Russia is a large proponent of metals and oil. Both represent key input costs for Beverage Companies and have already begun to put pricing pressure on beverage staples with the effects likely picking up in the summer and beyond. **Continued to the following page…**

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Table 3

US Wine Industry
YoY LTM March 2022 vs. 2021

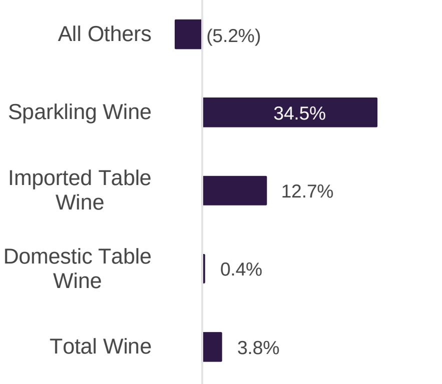
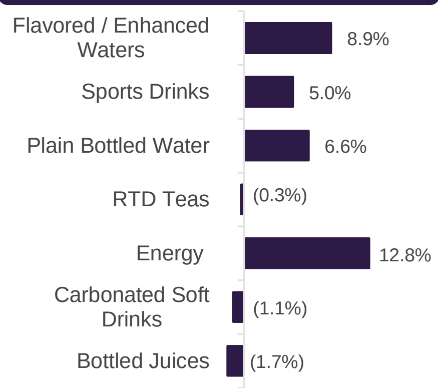


Table 4

Total Non-Alcoholic Beverages
FY 2021 vs. 2020 Volume Trends



Beverage Sectors In-Focus (Continued)

Grains- The majority of Ukraine's global wheat exports take place at the beginning of the marketing year which begins in July. For the 21/22 marketing year, Ukraine accounted for 10% of global wheat exports while Russia accounted for nearly 16%. Russia has already begun taxing exports and implemented an export quota on February 15th. Despite the United States, the 22nd largest importer and exporter of 11% of global supply, not being reliant on either for wheat, it still faces inflationary pressures. Wheat prices have grown 36% from February 21st to April 21st, a time frame that captures when speculation began and then the invasion on the 24th. Wheat prices saw their peak on March 7th at over $12.50 a bushel or almost a 60% increase from February 21. While these effects may not be felt as strong currently, companies should anticipate a larger impact once the new marketing year begins.

Corn is another main export of Ukraine which exports 14% of the world's supply in the 2021/2022 season, while Russia exports 2%. As noted above Ukraine has forecasted lower exports due to port closures, while Russian exports remain unchanged as they will export through the Caspian Sea. The United States ranks as the 39th largest importer of corn. Corn prices have increased by over 20% from February 21st to April 21st. This marks the second-highest price in the last 25 years.

Barley is yet another grain of which Ukraine and Russia are top exporters. Ukraine accounts for 17% while Russia exports 13%. Ukraine barley exports are generally front-loaded after harvest and a majority of their exports have already been shipped, therefore the effect of port closures is anticipated to be less than that of corn. The United States ranks 22nd for the import of barley.

While the United States may not be reliant upon the grain production of these two countries, it certainly will have an impact on global grain prices and not just from the region.

Containers– Now that we've delved into the input materials and costs needed to produce beverage products, how about the containers that store the liquid. In 2020, 67% of beer sold in the United States was sold in an aluminum can while 28% was sold in a glass bottle. The number one importer of Aluminum in the world is the United States doubling the second largest importer in Japan. While Russia stands as the third-largest exporter of aluminum and the impact on American business remains minimal as the cost of aluminum has risen under 1% from February 21st to April 21st, despite aluminum hitting a 25-year high on March 4th.This is on top of the fact that before the invasion American Canning indicated that aluminum cans were believed to be oversold by the billions in 2021 which would lead to a shortage of supply for the years to come. That impact has already taken place as the cost of aluminum has risen 55% from April '21 to '22.

The United States also happens to be the largest importer of glass in the world nearly 50% more than Germany, the second largest. The positive side is that neither Ukraine nor Russia is a top 15 exporter of glass. The largest impact will be felt by European Nations that need to fly over the contested areas in order to import glass from China, the world's number one exporter of glass counting for over 25% of glass exports. However, providers may choose to spread the impact of the conflict to accounts not directly tied to the cost increases of transportation over the Black Sea.

Transportation Costs – Not only do the supply constraints affect cost but also the mere transportation cost to get the materials to the states is affected. The primary driver of an increase in transportation costs is energy and how it relates to oil. Oil has been an interesting mover as the Brent Oil index jumped over 35% from February 21st to March 8th but has similarly fallen back to just under 18% growth for the February 21st through April 21st period.

The fallback is likely due to hopes that Saudi Arabia and UAE could boost oil supply and demand from China could drop due to the impact of Coronavirus on major Chinese cities. These factors continue to be fluid and create real volatility in oil and therefore transportation costs. Another factor to take under consideration is insurance premiums. Shipments surrounding the contested area provide much greater risk which in turn drives higher premiums. Trade routes are not nearly as impacted to the US as most routes from Europe and Asia can avoid the Black Sea area. However, companies will attempt to increase the cost of transportation across all shipments to try and mitigate the impact on their shipments that may be directly impacted by the conflict.

Inflation and Pricing Elasticity– Inflation continues to be cause for concern with some of the key drivers talked about above. In a 12-month period of Feb 21-22 the CPI for Urban Consumers illustrates a growth rate near 8% for all items while CPI for alcoholic and non-alcoholic beverages is 3.5% and 6.7% respectively. These pricing changes will impact each of the segments differently. Carbonated Soft Drinks over the course of 2021 saw pricing grow over 8%, which makes sense as the margins are tighter and they're reliant upon a higher velocity. This causes them to be more reactionary to input cost and inflationary pressures. The same goes for beer. While not as drastic, beer has seen a price mix change of just over 4 and 5 percent over the course of the last year and quarter through March 26th. While Spirits in turn have seen under 1% in the same period due to their operating model affording them the margin cushion to be able to maintain their price points to consumers.

Most of the key beverage manufacturers were already implementing price increases in 2021 and now with further increases in costs, it may be wise to anticipate more in 2022. One dynamic to monitor is consumers have generally accepted pricing changes or opted to move downstream to more value options, however, the question must be asked what is the breaking point before they reconsider their buying habits? This will continue to drive innovation and joint brand agreements in order to justify the value proposition for higher pricing and premium offerings.

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Sources: bw166, Beer Institute, DISCUS, Beverage Digest, Brewers Association, Nielsen, CGA