Constellation Brands Inc, Q1 2017, Earnings Call 2016-06-30

Presentation

Operator

Welcome to the Constellation Brands First Quarter 2017 Earnings Conference Call. — ***Operator Instructions*** —

I'll now turn the call over to Patty Yahn-Urlaub, Vice President of Investor Relations. Please go ahead.

Patty Yahn-Urlaub

Thank you, Maria. Good morning, everyone, and welcome to Constellation's First Quarter Fiscal 2017 Conference Call. I'm here this morning with Rob Sands, our President and Chief Executive Officer; and David Klein, our Chief Financial Officer. This call complements our news release, which has also been furnished to the SEC.

During this call, we may discuss financial information on a GAAP comparable, organic and constant currency basis. However, discussions will generally focus on comparable financial results. Reconciliations between the most directly comparable GAAP measure and these and other non-GAAP financial measures are included in the news release or otherwise available on the company's website at www.cbrands.com.

Please also be aware that we may make forward-looking statements during this call. While those statements represent our best estimates and expectations, actual results could differ materially from our estimates and expectations. For a detailed list of risk factors that may impact the company's estimates, please refer to the news release and Constellation's SEC filings.

— ***Operator Instructions*** — This has been our practice for the last several quarters and helps us end our call on schedule. Thanks in advance. And now here's Rob.

Robert Sands

Thank you, Patty, and good morning, and welcome to our discussion of Constellation's first quarter fiscal 2017 sales and earnings results. We are off to a great start to our new fiscal year with sales and earnings up double digits. Across the business, we're seeing the results of our efforts to drive consumer demand for premium products through best-in-class marketing and sales execution while improving margins through financial discipline and a focus on core premium products. This, combined with the successful integration of and growth from our recently acquired brands, provides a healthy foundation for achieving our fiscal 2017 objectives.

Our beer business continues to deliver industry-leading results while expanding their operational footprint with planned capital investments in Mexico. During the quarter, the beer business generated depletion growth of almost 10% and was the #1 share gainer in the high-end segment of the U.S. beer business. Constellation's beer portfolio led volume gains amongst U.S. brewers, contributing almost 20% of category dollar growth during the quarter, as each brand in our Mexican beer portfolio grew across most channels and packages.

Corona Extra and Modelo Especial remained 2 of the hottest brands in the U.S. beer industry and held category-leading positions as the #3 and #2 players, respectively, among overall brand share gainers. These results are due in part to focused market execution as well as optimization of key marketing and advertising initiatives. We launched fresh, new Spanish and English language national television advertising for the Corona Extra brand in canned format, including the brand's first-ever boxing TV ad. New national TV advertising was also launched for Modelo Especial in English and Spanish and for the Modelo

Especial Chelada in Spanish, both of which continue to have double-digit growth and are among the fastest-growing brands in the category.

Our new Pacifico 24-ounce canned format is the #1 new import so far in 2016, and we are supporting the brand by expanding targeted television advertising. Pacifico grew depletions more than 15% for the quarter.

And last but certainly not least, let's not forget about Ballast Point, which continues to be the fastest-growing major craft brand in the U.S., posting depletion growth of more than 60% in the first quarter. As you know, our plan for Ballast Point this year is to expand distribution and make their brand available in all 50 states. And to date, we now have distribution in more than 40 states and expect to complete our overall goal sometime before calendar year-end. This distribution push, along with successful new flavor and style launches, is expected to deliver the strong double-digit growth we are targeting for Ballast Point in fiscal 2017.

It was recently announced that we plan to establish a Ballast Point brewery in Virginia. This will allow us to develop an East Coast presence to provide the best-quality, freshest craft beer to all of our customers.

I'd now like to take a minute to discuss recently published IRI and Nielsen consumer takeaway data for our beer business as there seems to be significant discussion and debate related to the growth trends for some of our brands. First, IRI channels represent about 50% of our overall beer business at retail and therefore provide only a partial picture of the brand and portfolio performance outside of the sales, shipment and depletion results we report every quarter. Within IRI channels, over the last quarter, we've seen significant variability from week to week. Much of this relates to year-over-year timing and selling day comparison issues for important holidays during the quarter, including Cinco and Memorial Day. We saw some impact from our fiscal 2016 fourth quarter recall of certain

Corona Extra packages, which created temporary product shortages in select areas. We also experienced pockets of poor weather, especially in the Northeast, and we are cycling very strong Corona Extra can growth following last year's first quarter intro of the canned format for this brand.

Despite these temporary headwinds, our recent brand health assessment for Corona Extra indicates a consistent or increased drinking on key brand health scores nationally since fiscal 2016. While consumer takeaway is a standard measurement, depletions represent our entire business or an even more comprehensive indicator of growth and health. I'm very proud of our nearly double-digit beer depletion growth trend for the first quarter, given some of the factors I just mentioned. And preliminary beer depletion results for the month of June are progressing in line with our forecast. We anticipate similar timing issues around the upcoming key holidays in the second quarter related to the July 4 and Labor Day weekends.

Operationally, during the quarter, we completed a significant expansion milestone at Nava by doubling the size of the brewery that we acquired and bringing annual production capacity to 20 million hectoliters. All support areas are in place for this added capacity, including packaging, utilities, warehouse and rail infrastructure. As many of you are aware, the expansion of the Nava Brewery to 25 million hectoliters is our next critical capacity milestone, and I'm pleased to report that this work is proceeding as scheduled.

In addition, we have officially broken ground at Mexicali. And although this project is in the early phase, it is also progressing as planned.

Finally, we recently fired up our second furnace at our Nava glass plant and expect that it will be producing glass shortly. As a reminder, it takes several months for a new furnace to ramp up in order to produce optimal capacity.

And now I would like to focus on the operational results for our wine and spirits business. During the quarter, our wine and spirits business grew earnings and expanded margins while successfully integrating and growing our newly acquired premium wine brands, Meiomi and The Prisoner, which posted IRI dollar growth of about 90% and 30%, respectively.

Since the acquisition of The Prisoner, Constellation has gained 2 share points in the IRI luxury plus segment, extending the lead in our #1 luxury plus position. Constellation is now ranked #3 in super-luxury wine at the greater-than-$25 retail price point. The U.S. wine business posted strong sales growth and gained IRI dollar share, driven by our core Focus Brands, where we're building momentum across multiple price segments.

Let me provide a few examples. In the IRI $20-plus luxury and super-luxury price segments combined, Meiomi is not only the largest pinot noir, but also the largest dollar share gainer for the entire quarter. Kim Crawford is the #1 Sauvignon Blanc in the IRI super-premium segment and posted dollar sales growth of more than 20% during the quarter. Clos du Bois is the #1 chardonnay in the IRI premium segment. And Black Box is the leader in the fast-growing premium box segment.

In aggregate, our Focus Brands grew depletions at 12% for the quarter. Our innovation platform is also gaining traction, thanks to new margin-enhancing offerings like the Robert Mondavi Private Selection, Bourbon Barrel-Aged Cabernet, SVEDKA Cucumber Lime, Ruffino Sparkling Rosé and Ravage Cabernet Sauvignon.

The Canadian business delivered a solid quarter, posting mid-single-digit net sales growth while continuing to gain market share across both the import and domestic wine segments. Overall, our first quarter wine and spirits results are a testament to our ability to achieve our goal of growing profits ahead of sales and improving margins.

So what are the key enablers? We are reaping the benefits of our targeted investments for a subset of our Focus Brands in order to drive key brands that have scale, higher margin and greater growth potential. We remain committed to mix and margin-accretive innovation and new product development and have several new products in the hopper, a few of which I just mentioned. We continue to optimize COGS through global blend management initiatives, productivity improvements and lower grape costs. We are capitalizing on the market-leading growth of our margin-enhancing wine acquisitions, Meiomi and The Prisoner. And we have recently made some leadership changes within wine and spirits to enable a stronger, more competitive business.

Now before I turn the call over to David, I would like to touch on 2 more high-level topics of interest for our business. The first is related to the exploration of a possible IPO of our Canadian business discussed last quarter. Our evaluation of this strategic option continues, and we plan to provide you with an update as soon as possible. Since this evaluation is ongoing, there is not much else to add at this time. The second is the recent referendum in favor of the U.K. exiting the European Union. As a reminder, Constellation is primarily a U.S. business. Our sales outside the U.S. represent about 10% of our total consolidated sales and are primarily related to our Canada business. As such, our exposure to European markets, in particular, is limited, and a strong dollar generally benefits us financially.

In closing, our first quarter results have set the stage for fiscal 2017. We are off to a very positive start for the year, gaining market share across our beer and wine businesses. We have been working diligently to build a solid and sustainable foundation of operational excellence, financial strength and innovation. And we expect to continue to execute on these areas throughout the remainder of the year.

With that, I would now like to turn the call over to David, who will review our first quarter financial results.

David Klein

Thank you, Rob, and good morning, everyone. On the last call, we provided guidance which represented an impressive mid-teens EPS growth. I'm happy to report that we're steadily executing against our plan. Comparable basis diluted EPS for the quarter came in at $1.54, up 22%, putting us on a path to achieve our full year comparable basis diluted EPS goal of $6.05 to $6.35 per share.

Let's look at Q1 fiscal '17 performance in more detail, where I'll generally focus on comparable basis financial results. Organic beer net sales increased 15%, primarily due to organic volume growth of 12% and favorable pricing. Beer depletion growth for the quarter came in at almost 10%. This includes Ballast Point depletions for the quarter and in the corresponding period last year. Excluding Ballast Point, depletions for our Mexican portfolio grew 9%.

Beer shipment volume for the first quarter generally runs ahead of depletion volume as distributors build inventory for the summer selling season. This year, we also benefited from a shift in shipment volume from Q4 fiscal '16 into Q1 fiscal '17 related to the beer recall we discussed last quarter. Distributor inventory days at the end of Q1 fiscal '17 were fairly level with the prior year quarter.

Wine and spirits net sales on an organic constant currency basis increased 3%. This primarily reflects volume growth and favorable mix for the segment, driven by solid financial results for the organic U.S. wine business in the quarter.

Beer operating margin increased 80 basis points to 35.6%. This reflects benefits from pricing, foreign currency and timing of marketing spend for our Mexican portfolio. As expected, these positive factors were partially offset by higher COGS, including increased depreciation as additional capacity came online; SG&A investments; and the consolidation of Ballast Point. If you exclude the marketing timing benefit, beer operating margin for the quarter would have been flattish to up slightly.

I'd also like to note we have reduced the level of product we receive under the Interim Supply Agreement with ABI as Nava has reached the 20 million hectoliter capacity milestone. Wine and spirits operating margin improved 160 basis points to 23.3%. The increase was primarily related to the benefit from the Meiomi acquisition.

Interest expense for the quarter increased 9%, primarily due to higher average borrowings. When factoring in cash on hand, our net debt totaled $8.1 billion, an increase of $143 million since the end of fiscal '16. This increase primarily reflects funding for The Prisoner acquisition, which closed at the end of April, partially offset by our free cash flow generation.

Our net debt to comparable basis EBITDA leverage ratio came in at 3.7x at the end of Q1 fiscal '17 versus 3.8x at the end of fiscal '16. Our leverage ratio at the end of Q1 does not yet reflect a full year EBITDA benefit from the Ballast Point, Meiomi and Prisoner acquisitions.

Our comparable basis effective tax rate for the quarter came in at 31.6%, which is essentially even with Q1 of last year. We anticipate that our Q2 fiscal '17 effective tax rate will be similar to the Q1 rate. However, we continue to expect our full year fiscal '17 effective tax rate to approximate 29%.

Now let's review free cash flow, which we define as net cash provided by operating activities less CapEx. For Q1, we generated $177 million of free cash flow compared to $76 million for Q1 last year. Operating cash flow totaled $346 million, up 68%. This increase was primarily driven by our earnings growth.

CapEx for the quarter was $169 million compared to $130 million for Q1 last year. While CapEx was up for the quarter, we still have significant spending plan for the balance of the year as our full year CapEx guidance of $1.25 billion to $1.35 billion remains unchanged. As a reminder, this guidance includes approximately $1.1 billion to $1.2 billion related to our beer business operational expansion projects in Mexico. We continue to expect fiscal '17 free cash flow to be in the range of $250 million to $350 million. This reflects operating cash flow in the range of $1.5 billion to $1.7 billion and the CapEx spend that I just outlined.

Moving to our full year fiscal '17 P&L outlook. We continue to project our comparable basis EPS to be in the range of $6.05 to $6.35. Our comparable basis guidance excludes comparable adjustments, which are detailed in the release. The beer business continues to target net sales and operating income growth in the range of 14% to 17%. We also continue to expect organic net sales and operating income growth to be in the 10% to 13% range. This includes 1% to 2% of anticipated pricing benefit for our Mexican portfolio.

For the wine and spirits business, we continue to expect net sales growth in the mid-single-digit range and operating income growth in the mid- to high single-digit range. In addition, we continue to project organic net sales and operating income growth to be in the low to mid-single-digit range, with operating income growth targeted ahead of sales growth as we are forecasting some mix benefits.

In closing, we're off to a great start to the year and on track to achieve our financial performance goals for fiscal '17. While we still have much to accomplish with our Mexican brewing operations, we're excited that we achieved a critical milestone by reaching the 20 million hectoliter capacity mark at Nava.

With that, Rob and I are happy to take your questions.

Question and Answer

Operator

— ***Operator Instructions*** — Our first question comes from the line of Nik Modi of RBC Capital Markets.

Nik Modi

Just a quick question on the wine business. The depletion growth looked pretty good on the organic side, and I know you talked about a lot of brands growing. But what exactly is underpinning some of the improvement there? Maybe you can share some of the early things that Bill Newlands is doing in that business. And then just a quick follow-up. Just wanted to get an update on how the Kim Crawford test is doing out in Texas. I believe you guys are spending some marketing dollars behind that brand. I just wanted to get kind of an update on that.

Robert Sands

Yes. So as I mentioned a few minutes ago, it's really a subset of our Focus Brands that are driving that depletion growth. That is excluding our newly acquired brands, Meiomi and Prisoner. But we've got a few brands right now that are really on fire like Black Box. Clos du Bois is up heavy double digits. Kim Crawford is up very significantly. And even our largest brand, which is Robert Mondavi. The Woodbridge brand is up very significantly on a very large base. The Mark West brand, the pinot noir brand that we acquired a few years ago, is also up very sharply. So I guess that we're – it's fortunate that we can report that our brand portfolio includes some really hot brands at the moment. What was your question about Texas, Nik?

Nik Modi

Yes. Just the Kim Crawford test. Just looking at how that's progressing.

Robert Sands

Yes. That test has gone extremely well. I think that the test has demonstrated that the brand responds and performs very well to advertising. And consequently, we will be increasing our advertising for this brand. And the test was basically – the test basically demonstrates that, that's an investment that will more than pay back. So we're pretty excited about that as well.

Operator

Our next question comes from the line of Tim Ramey of Pivotal Research Group.

Timothy Ramey

You mentioned the FX impact. And I think of all the things that you buy from other places in the world, not just beer, but barrels and so on, we've had some pretty substantial moves, particularly against the peso. I wonder if you could kind of give us any quantification about what that contribution might look like now.

David Klein

Yes. So Tim, as it relates specifically to the peso, about 20% of our COGS for beer are denominated in peso. And so clearly, as the dollar strengthens, we get a benefit. What I'll say, though, is that we also – as we sit here today, we're about 70% to 75% hedged on our exposures against all currencies for the remainder of the fiscal year. So the strengthening dollar clearly benefits us, but some of that benefit is muted by the hedges that we have in place.

Timothy Ramey

Okay. And Rob, maybe – you're always good at commentating on the kind of the big picture in wine. I think the category is performing well, and you're outperforming the category. How do you see that performing for maybe the 12- to 18-month time horizon?

Robert Sands

Yes. I think, actually, the category, as you mentioned, has accelerated a bit lately, and therefore, I would say that it's very robust. I would say that trading up and premiumization in the category is probably stronger than ever, okay, and things have really kind of shifted. Maybe 2 or 3 years ago, we would have been talking about the $8 to $10 or $12 segment really being the hottest segment in the industry, but I would say that, that shifted up to even the $15 and $20 segments. Hence, our interest in brands like Meiomi and Prisoner in that segment because I think we really see the future continuing to favor premiumization and trading up even into these more expensive categories. And then as it relates to our own business, we're constantly working on positioning our – our portfolio, okay, to take advantage of those trends. And I think that we have very successfully done that and have great brands in all of these hot price segments and categories. And it's not just price segments, right? It's categories, a perfect example being pinot noir, okay? We're a leader in pinot noir today. And pinot noir is just an extremely hot varietal. And I would say that the good news there is that – I would say we expect it to continue to be a hot varietal for well into the future in that it is not a trendy kind of a thing that will be fleeting and that, of course, pinot noir is one of the noble varieties and has always been highly sought after. And we – and as I said, we've got the hottest brands. Red blends continue to be hot. As you know, we've got hot brands in the red blend category. I mean, Prisoner, I mean, is a perfect example of that, albeit a newly acquired brand, but you only have to go and sort of see what people are drinking in any major metropolitan area or talk to people and Prisoner is the hottest brand in its price point and has taken advantage of that as well. Again, I don't think that's particularly trendy in that it's gotten fantastic scores and is considered to be, let me put it this way, a real fine wine. So that's basically the answer to your question, Tim.

Operator

Our next question comes from the line of Judy Hong of Goldman Sachs.

Judy Hong

So first, in terms of the beer depletion, Rob, as you pointed out, pretty choppy, weather and some of the factors in the first quarter. So when you look at your 9% depletion for the core organic, you kind of have a sense of how much some of these one-off factors dampen that growth. And then I think you said June depletions are progressing. Can you give us a little bit more color just in terms of what you're seeing in June? I mean, some of the Nielsen data actually looked pretty strong as we've seen in the last few weeks. So maybe just a little bit more color just on the June trend. And then as it relates to your full year depletion growth, it seems like you're kind of still expecting relatively healthy organic sales growth for your core business. Any sort of concern around the competitive environment as you think about the marketplace?

Robert Sands

Yes. So look, it's hard to get into specific numbers, okay, on what the growth would have been had these factors not affected us. But as I said, there were 2 or 3 factors. I'd say first quarter was kind of not a great quarter for the beer business – the beer category in general. I mean, that said, our beer portfolio grew a little bit shy of 10%, which is an outstanding result on a relative or comparative basis. Yes, there were a few things that affected our business, which I talked about. The recall affected it, for sure. Hence, we would have done better in the first quarter had that not been the case. The can overlap, i.e., overlapping the intro, was a factor. There was definitely some promo activity in first quarter last year, which was not duplicated this year, again due to some packs not being in supply during that period. And then I guess, to your point, you can see all that kind of clearing itself up by simply looking at the June IRI trends, which I think are reflective of the overall health of the business. So we have no concerns whatsoever about the brand health of the import portfolio or Corona, period. So we fully expect to be on our forecast for the year for the portfolio. And that's our import portfolio, right? Ballast Point, we're not even talking about that because the growth is so high that, what can you even say?

It's the fastest-growing beer in the entire craft segment in the entire U.S. on what's getting to be a very big base, okay? I mean, you don't – we can't even talk about double-digit growth because it's so high. It's triple digits sometimes.

Judy Hong

Right. Right. Okay. That's helpful. And then, David, just in terms of the phasing of, I guess, the beer gross margin progression for the balance of the year. As we think about, certainly, Nava having now the 20 million hectoliter capacity, I think you have one of – one more furnace in Nava up and running as well, but obviously, some of the start-up costs on the Nava site. So just – can you just help us understand sort of the phasing of gross margin? Is second quarter kind of more negatively impacted? Is it more of a heavy volume quarter? Or how we should think about it, the phasing?

David Klein

Yes. So in the first quarter, we benefited from pricing in general, which somewhat offset COGS increases, which were driven by increased depreciation. We did receive some benefits from FX. But probably the biggest driver in the quarter was the timing of marketing spend. And now I'm talking about operating margins, right? So we'll see that spend come back as we progress in the fiscal year, which will have a bit of a dampening effect on the margin. So we still expect flat margins roughly year-over-year, and we're just – we're pleased with the progress we're making in terms of margin expansion and getting the Nava facility functioning at 20 million hectoliters. The other comment I want to make, Judy, relates to glass. So yes, we fired up the second furnace at Nava. We won't be producing glass out of that facility really until the end of July. And then even when that happens, the facility itself won't be producing at what we would expect are acceptable levels of utilization for many months. It takes a long time to get the furnaces functioning in a way that we'll be happy with. So I would say that the benefit from that furnace really won't show up until the back half of this year if it shows up this year at all.

Operator

Our next question comes from the line of Dara Mohsenian of Morgan Stanley.

Dara Mohsenian

Rob, I was hoping you could review for us your cash flow priorities in terms of M&A versus returning cash to shareholders, given some of the rumors in the press lately. And is M&A a big focus at this point? And what range or size of deal are you generally comfortable with from an M&A standpoint?

Robert Sands

Yes. So I would say that our capital priorities haven't changed at all. They sort of remained #1 at keeping our debt levels in that sort of mid-3 to 4 range, where we actually are at the current time. Returning dollars to shareholders continues to be a big and important focus for us. As you know, we did increase our annual dividend at the end of the year, and we have made some stock repurchases. So we continue to prioritize that as a key priority. And then as we've said in the past, we'll continue to look at and potentially make selective acquisitions of things like Meiomi, Prisoner as we go on. So I think that those kind of things are somewhat reflective of being tuck-in-type acquisitions of the things that we would look at, and I would say that, that strategy is working very well. And then I think to the – your question about the magnitude, I think that goes back to my first point relative to maintaining our debt levels in that sort of 3x to 4x, okay? We will be, I'll say, guided in terms of magnitude by that priority. And then as I mentioned in my script, we continue to evaluate the Canadian IPO, right? But that's a disposition. So if we were to complete that, that will actually bring in cash, right? So we're being, I would say, pretty judicious in terms of how we're managing the whole capital allocation process and our priorities. So I think that we've got – we've struck a really good balance there. Let me put it that way.

Dara Mohsenian

Okay. That's helpful. And then beer pricing was strong in the quarter at 3%. Obviously, part of that is Ballast mix, but still strong on an underlying basis at a time when industry discounting looks like it's picked up. So I was just hoping you could review if you're comfortable in the 2% pricing range going forward for your business and anything you're seeing from a competitive standpoint in the industry.

Robert Sands

Yes. Our position on pricing and our plans haven't changed at all, and we don't really – yes, there's been some competitive activity. But I would say that there's really nothing indicative that, from a competitive point of view, that that's really changed very significantly. I don't think anybody is like falling off a log and change their general modus operandi in the industry in general. That's sort of our view of things.

Operator

Our next question comes from the line of Robert Ottenstein of Evercore.

Robert Ottenstein

So 2 questions. One, if you look at – and I know it's tough to get to, so just – I appreciate any kind of way to think about our estimate. So if you look at roughly 9% depletion growth on the Mexican brands, can you break out roughly what percent of that is coming from Mexican-American consumers and what percent would be coming out from the general market?

David Klein

So Robert, the way we think about it when we look at our FY '17 numbers, we think that about 40% of our year-over-year growth will come from increasing distribution in the business. So this doesn't get to the demographics, but this is how we think about our numbers. So about 40% coming from growing distribution; about 10% coming from pack innovation during the fiscal year; and then the remainder is really driven by demographic shifts like Hispanic and millennial consumers. But we also have included in that remaining 50% other environmental factors, so it gets a little bit muddy. But when we're putting our plans together, that's how we think about it.

Robert Ottenstein

All right. Well, in terms of the 40%, would it be fair to say that most of that 40% would be the general market? Because presumably, Modelo Especial is pretty well distributed in Mexican-American accounts. And Corona is already there so...

David Klein

It is some of the – yes, some of the distribution growth, though, isn't necessarily just getting a pack into an individual store. It's getting different pack sizes into individual stores, which will take place across all of the retail establishments.

Robert Ottenstein

Got it. And then my second question. Rob, as you look out at the – on the environment or the opportunity set for potential wine acquisitions and the possible targets, how does that look today? And how does that compare with what you may have seen a few years ago? Is it a more target-rich environment? Less? Are you excited about what's out there in terms of what you can bring into the portfolio? Maybe just kind of give us a sense of what the landscape looks like.

Robert Sands

Yes. I don't think that we see anything that's largely different than what has been the case over the last several years, especially for perhaps the kind of things that we might be interested in. It really remains a one-off kind of opportunistic situation. There has been sort of a lot of activity in sort of the smaller end of the market, which – meaning small deals that we don't really plan because they wouldn't be particularly significant or material to us. But of the kind of brands that we might be interested in, I would say that there's no fundamental change in the activity in that arena.

Robert Ottenstein

I mean, perhaps another way of asking it. Just kind of for modeling purposes or just thinking about it, should we kind of think about maybe one deal a year averaging out to that? Obviously, it's opportunistic…

Robert Sands

It's totally unpredictable. Follow up later, Rob.

Operator

Our next question comes from the line of Vivien Azer of Cowen.

Vivien Azer

So 2 questions on Ballast, please. On the depletion growth that you guys noted, would it be possible to unpack that and give us a sense for how much distribution added to that?

David Klein

Yes. We have grown distribution about 40%. Since the time we took on Ballast Point, I think we're at about a 20 ACV. And it's – however, we're still seeing growth in our existing markets and our existing stores. So I would say we're seeing growth in big markets like California as well as growing incremental markets across the U.S.

Vivien Azer

That's great. And as you target the full national distribution by the end of the calendar year, how would you anticipate your ACV tracking with that?

David Klein

Yes. I think coming back to the growth that we've seen so far, I would just expect that we'll continue to drive ACV as that brand becomes one of the biggest craft brands in the marketplace. We'll continue to see more retailer uptake and more consumer demand for the product. In terms of quantifying what happens with ACV, I don't have that at hand.

Vivien Azer

Okay. That's great. And then my second question, also Ballast related, please. I know it's a little bit of a ways out. But as you think about the construction of the Virginia brewery, can you just give us a sense of how you're thinking about the margin opportunity there?

David Klein

Yes. Well, again, we – one of the reasons we really like this brand, and we've said this since we first announced the purchase, is that this brand has very healthy operating margins as we sit here today. It's a little dilutive to our overall beer business, but we would expect over time – as the brand gains a little scale and we get some benefits of East Coast production in the Virginia facility, we would expect that the margins begin to close the gap with our import portfolio margins.

Operator

Our next question comes from the line of Caroline Levy of CLSA.

Caroline Levy

My question is on – I wonder if you could get specific, David, on A&M as a percent of sales for beer in the quarter and if you still see it at sort of 8.5% to 9% for the year?

David Klein

Yes. 8.5% to 9%, and that's across our entire beer business, although most of the spend at this point, as you know, is focused on the import portfolio. And we're seeing – on that point, Caroline, I'll say that we've begun advertising on a brand like Pacifico on a broader scale than we have in the past and as a result, we saw very healthy depletion growth on

Pacifico of around 17% in the quarter.

Caroline Levy

And in the quarter, what was A&M as a percent of revenue? Because you said there are some timing differences, so it sounds like they'll spike in the second quarter.

David Klein

Yes. So in the quarter, it – yes, in – I don't have that number. We can get back to you with a specific number in the quarter.

Caroline Levy

Okay. What would also be helpful, and I don't know if you're willing to give this. But D&A didn't seem to go up that much, first quarter over fourth quarter. But you have called it out as a margin pressure for beer going forward as you bring on the Nava capacity. So like – would you be able to tell us what D&A was for the beer business in the quarter?

David Klein

Yes. It's – we're going to file the Q today, and it will – that information will be in the 10-Q when it's filed.

Caroline Levy

Okay. Just finally, on the timing of advertising, does this suggest that you have more programs coming up than usual in the second quarter, which could be helpful to sales?

David Klein

Yes. And again, I think you have to think about it in the context – I know you're asking a question that I'm not answering actually. But you have to think about it in the context of a percentage because on an absolute dollar basis, we – I'm not suggesting that we've spent less in the first quarter; it's just less as a percentage of the business. So we still executed our normal marketing programs in the first quarter of the year, but yes, we do have that activity ramping up in 2Q and then going into the fall sports season.

Operator

Our next question comes from the line of Bill Chappell of SunTrust.

William Chappell

My question is on – one, Rob, you had talked about only 50% of your business is tracked by IRI, which I get. But are you seeing any meaningful changes or growth rates or anything in the non-tracked channels? Or I mean, should we not be looking at IRI as closely?

Robert Sands

No. I think IRI is fairly reflective of our business. But remember that the on prem – IRI would not be reflective of the on premise, which constitutes about 15% or so of the business. And it also is not reflective of what goes on in wine and spirits in control states and regular store states. So the biggest chunk there is probably on-premise, which, in our business, is running up about mid-single digits in the beer business – in our beer business and low single digits in our wine business and from a market perspective is down in both categories – in all categories: wine, spirits and beer. On-premise was down as a category or as a market segment for the category for the quarter. So that is probably one of the bigger callouts is on premise not being reflective – not being reflected by IRI.

William Chappell

Yes. No, that helps. And then second, just to follow on Ballast Point. Now as the distribution has expanded, can you kind of tell us what's your learnings for a product that's at the high end of the price range, that was largely a West Coast regional brand? I mean, how has it resonated versus kind of expectations as you've moved it more and more to the east and with the price points kind of compared to other things on the shelf?

Robert Sands

Well, I think it's resonated really well. I mean, where we have gotten new distribution as we've moved it to the east, I think that it's resonating particularly well. I'm not sure that it's perceived with any geographic specificity as we bring it into new markets. And as it grows in new markets, I think that it's really more viewed as a really high-end, high-quality, award-winning brand. And it's all about sort of styles and flavors. And I think the thing that's kind of unique or somewhat unique about Ballast Point is that it does have a lot of different styles like Commodore stout or the Sculpin IPA. And that's got flavors, in essence, like the Grapefruit Sculpin or the new Pineapple Sculpin, which is really hot, or a new product, which we just intro-ed, called Barmy, which is a honey – apricot- and honey-flavored pale ale. But this is very subtle stuff, right? It's not like it's flavored like a flavored alco – a FAB, okay, like my father's root beer or Mike's or something. These are very subtle flavors that accentuate, okay, the sort of exotic hops that are used in the product and sort of bring out some of the qualities of those hops. And therefore, it's – I'd say real beer – and appeals to, I would say, real beer aficionados, which is one of the reasons why I think that it is able to command the premium pricing that it does command is because of the fact that it really is viewed by beer people, okay, as a super high-quality, award-winning product. A lot like wine in that regard, right? High-end wine. Think of its acceptance in that vein by real craft beer drinkers who know and follow what's really being held as super high-quality examples of that type of product. So it's much more like that, it's much more like high-end wine, is the way I would think about Ballast Point.

Operator

Our next question comes from the line of Mark Swartzberg of Stifel, Nicolaus.

Mark Swartzberg

Two questions. One on Modelo Especial. Rob, if we could perhaps go a little deeper there? It's growing stronger than Corona Extra. I'm sure that was true again in the quarter. I didn't catch the depletion rate. Could you just give us a flavor for not only what the depletion rate for the brand was in the quarter, but what your plans are to perhaps accelerate the rate of depletion growth for that brand specifically? I'm interested in ACV intentions, spend rate, trying to get a better sense of where we are with that success story.

Robert Sands

Yes. So Modelo Especial depletion growth rate first quarter, about 20%. And we've got big plans to, I'll say, accelerate that growth rate or at least maintain it. But as you pointed out, it's all about distribution. I mean, Modelo Especial is growing and is the size that it is without being in full distribution, okay, compared to other major brands of its size. It's one of the top beer brands now in the entire country. And if you look at beer brands that are – have full distribution, I mean, you're talking like 80%, 90%, okay, Modelo Especial has about 70% ACV. So it's got a pretty good distribution runway. And I think that the thing that you should realize is, in general, okay, it's distribution growth that drives depletion growth probably the most of anything. So a pretty big runway there. The good news is that – probably the second most important thing, right, is velocity per point of distribution. And if you look at our portfolio in general, whether it's wine, beer, spirits, Modelo Especial, our fast-growing brands are achieving their growth through both velocity growth as well as distribution growth.

Mark Swartzberg

Got it. Got it. And what I'm hoping to better understand is – this summer or the next few quarters, is there the intent to pick up the pace of ACV gains for that brand versus what they've been given what you just said? Or – because the other choice, of course, is to say no, Corona Extra is the horse here.

Robert Sands

ACV growth is the number – has been and will continue to be a #1 priority for the beer business and Modelo Especial in particular. When you say pickup, it's not like we raft [ph] at a particular point in time on distribution growth. It's what – that is what the sales organization, basically, is all about and does, okay? When companies like ourselves talk about execution or sales execution, they are talking about growing distribution, first and foremost. And then probably, the #2 thing in sales organization execution is all about merchandising and ad activity at retail. So that's what sales forces do. It's all they do. They run out and get distribution. They grow distribution, and they work with the distributors and the retailers to maximize the merchandising opportunities.

Mark Swartzberg

Got it. Okay. And my second question, I'll stay on that brand, media spend for Modelo Especial, rate of growth. Can you give us a sense do you – we heard about the portfolio rate of growth picking up here over the next few quarters. Is it fair to think that, that particular brand is getting an outsized rate of increase versus Corona Extra and some other brands? Or is that not the right way to think about it?

David Klein

Yes. We don't really break down the spend between the brands publicly. But I would say that we know that last year, we started to spend more in terms of general market advertising as it relates to Modelo Especial. You'll continue to see that ramp up for the remainder of this year.

Robert Sands

Yes. I'd also point out that – and I think that this was mentioned previously. I mean, we have put some media advertising in place for Pacifico. And Pacifico is absolutely on fire with 17% depletion growth in the first quarter. And I would say there's a lot of chatter beginning – we're beginning to hear a lot of chatter about that particular brand and its general – and its appeal, in particular, to craft drinkers. It seems to be a brand that – when craft drinkers aren't drinking, I would say, traditional craft, okay? And sort of their next go-to session item seems to be Pacifico. And we're seeing a lot of interest and growth in that particular product. And that 24-ounce can has been on fire. So I would say that is something you should watch as the next up-and-comer.

Operator

And that was our final question. I would now like to turn the floor back over to Rob Sands for any additional or closing remarks.

Robert Sands

Okay. Well, thank you, everybody, for joining our call today. As we wrap up our discussion, I want to reiterate how pleased we are with the overall excellent performance of our business this quarter. Our fiscal '17 is off to a fantastic start, and we're confident in our ability to achieve our full year guidance. As we head into the 4th of July holiday weekend, I hope you remember to bring some of our fine products to your celebrations and to please enjoy them, of course, responsibly. Hopefully, you've received the save-the-date notice for our planned New York City investor meeting on November 9. At that time, we look forward to speaking with you about the future strategy for our business. Thanks, and have a great July 4 holiday.

Operator

Thank you, ladies and gentlemen. This does conclude today's conference call. You may now disconnect.