Constellation Brands Inc, Q3 2023, Earnings Call 2023-01-05

Presentation

Operator

Greetings, and welcome to Constellation Brands' Third Quarter Full Year 2023 Earnings Conference Call.

— Operator Instructions —

As a reminder, this conference is being recorded. I would now like to turn the conference over to your host, Mr. Joseph Suarez. Thank you. You may begin.

Joseph Suarez

Thank you, Rob. Good morning, all, and happy new year. Welcome to Constellation Brands Third Quarter Fiscal 2023 Conference Call. I'm here this morning with our CEO, Bill Newlands; and our CFO, Garth Hankinson. As a reminder, reconciliations between the most directly comparable GAAP measures and any non-GAAP financial measures discussed on this call are included in our news release or otherwise available on the company's website at www.cbrands.com. Please refer to the news release and Constellation's SEC filings for risk factors, which may impact forward-looking statements made on this call. Before turning the call over to Bill, in line with prior quarters or like last, let me limit everyone to one question per person, which will help us to end our call on time. Thanks in advance, and now here's Bill..

William Newlands

Thank you, Joe, and good morning, everyone. Happy New Year to everyone, and welcome to our fiscal third quarter call. I hope you all had a great holiday season and that our products were able to play a role in some of your special moments with your family and friends. Since our last call in October, Constellation Brands reached a notable milestone in its history as a public company.

As most of you know, in November, our shareholders approved the elimination of our Class B common stock. With that came the transition of our company to a single class of publicly listed stock, our Class A common stock, which provides our shareholders with equal 1 share, 1 vote rights. I want to thank everyone who supported this important enhancement to our company's corporate governance profile and capital structure. We believe that our leadership team now has an even stronger foundation to continue to build shareholder value through the strategic initiatives we adopted and have steadily advanced over the past nearly 4 years since I assumed the role of CEO.

Since fiscal 2020, we agreed to focus on and put in place plans to: number one, continue to build powerful brands that people love; number two, develop consumer-led innovations aligned with emerging trends and consistently shape our portfolio for growth; number three, deploy capital in line with disciplined and balanced priorities; and number four, operate in a way that is good for business and good for the world. I'm pleased to say that we continue to build on a strong track record we have established against all of these strategic initiatives.

Starting with number one, building our powerful portfolio of brands. Our beer business, despite a more recent series of headwinds, which we'll address in a few minutes, delivered its sixth consecutive quarter of leading share gains across the entire U.S. beer category in IRI channels that was primarily driven by our 2 largest brands, Modelo Especial and Corona Extra.

In the third quarter, Modelo Especial maintained its position as the top share gainer and is the #1 high-end beer brand, and Corona Extra was the third largest share gainer and the #3 high-end beer brand. In fact, our beer business delivered 3.5 points of share gains and 54% in dollar sales growth when comparing the 52-week period that ended with our latest fiscal third quarter against the 52-week period that ended with our fiscal 2019. And comparing the same periods, the business contributed the highest dollar sales growth in the category, amounting to over $2.5 billion.

In our Wine & Spirits business, our largest higher-end brands Meiomi, Kim Crawford, The Prisoner and High West, all delivered dollar sales growth and share gains in the third quarter. And comparing the 52-week period that ended our latest fiscal third quarter, against the 52-week period that ended our fiscal 2019, these brands achieved 72% dollar sales growth.

Moving on to number two, consumer-led innovation and shaping our portfolio for growth. Many of you may be surprised to know that in our beer portfolio, our SKUs introduced over the past 3 years have driven 20% of the growth delivered by the business since the start of fiscal 2020. An important part of this growth has come from our Modelo, Chelada brands, which have evolved from a niche business to a sizable platform. In fiscal 2023 year-to-date, it has delivered 13.6 million cases of depletions, which already exceeds the brand's total deflations for all of last fiscal year. And in the third quarter, Modelo Chelada limoncello moved up 9 spots to become the sixth largest share gaining brand in IRI tracked channels. Beyond the Chelada brands, we continue to build on the opportunities within the Modelo family with a clear focus on maintaining brand investments. We are excited about the national launch of Modelo Oro in March which has surpassed internal and external benchmarks in test markets.

In our Wine & Spirits business, innovation has also yielded strong results, increasing its contribution to net sales from 1% in fiscal 2020 to approximately 8% in fiscal '23 year-to-date. This expansion has been primarily driven by extending our largest higher-end brand, once again, Meiomi Kim, The Prisoner and High West. Notably, extensions in The Prisoner brand family, Blindfold, Saldo and Unshackled have contributed significant growth, especially Unshackled, which has grown to be half the size of The Prisoner brand in just 4 years.

In addition, since the beginning of fiscal 2020, we have added 5 brands through acquisitions, like Bronco Wines, My Favorite Neighbor, Empathy Wines, Halpern and Kings and Austin Cocktails, all of which are in the higher-end segments of the wines and spirits categories that are contributing to growth. And we divested 36 brands, the vast majority of which were in the mainstream segment, which has mainly been in decline due to consumer-led premiumization trends. Given this free shaping of our portfolio, including the recent additional divestiture 62% of net sales in fiscal ’23 year-to-date were from our higher-end brands. This is a dramatic shift from the 34% higher-end brands represented at the end of fiscal ’19.

Now turning to number three, capital allocation. In fiscal 2020, we introduced a thoughtfully structured approach designed to consistently deploy capital with discipline and balance. We made maintaining our investment-grade credit rating, our top capital allocation priority and reduced our net leverage ratio, excluding Canopy equity and earnings, from 4.5x at the end of fiscal ’19 to 3x by the end of the second quarter of this fiscal year. This was partly driven by a $3.2 billion reduction in our debt levels and partly by strong earnings growth in our beer business.

And then in the third quarter, these efforts gave us the flexibility to both accommodate the $1.5 billion financing for the elimination of our Class B shares and to maintain our investment-grade rating. As our net leverage ratio remained in line with our prior 3.5x target. However, we recently updated that set target to 3x, given our ability to previously achieve that target and the continued strong cash flow generation capabilities of our businesses.

Our second priority became delivering cash returns to our shareholders, and we set a goal to return $5 billion in dividends and buybacks between fiscal 2020 and '23. We virtually completed that goal ahead of schedule in the third quarter and we're now on track to exceed the $5 billion target with the fourth quarter dividend payment announced today. As to our third priority, we sought to advance growing capacity expansions to support the strong growth in our beer business. Since the start of fiscal 2020, we added approximately 9 million hectoliters of capacity through growth investments and another 2 million through brewery optimization and productivity initiatives.

We are also on track to further diversify our production footprint with the development of our new brewery in Veracruz, where we have recently broken ground. And last in our capital allocation priorities was M&A, and since the start of fiscal '20, we have judiciously deployed excess cash through acquisitions with a strict focus on small gap filling higher-end brands. And the key strategic acquisitions we have executed over the last nearly 4 years are delivering top line growth. All in, we believe we have unquestionably upheld our capital allocation priorities and have even exceeded some of the associated targets we set out to achieve.

Moving on to strategic initiative number four, operate in a way that is good for business and good for the world by advancing ESG goals. Our ambitions are to protect the environment and natural resources by serving as a model for water stewardship in our industry while reducing greenhouse gas emissions, to champion the professional development and advancement of women within our company, industry and communities, to enhance the economic development and prosperity in disadvantaged communities and to promote responsible beverage alcohol consumption. While we still have much work to do, I am proud to say we are making good progress towards our goals.

To that end, in the third quarter, we released our 2022 ESG Impact Report, which included several enhancements on the information shared on these important topics and our work towards our targets, including, for the first time, references aligned to the Sustainability Accounting Standards Board framework and taking into consideration recommendations from the task force on climate-related financial disclosures.

So as with our capital allocation priorities, we have been consistently working to deliver against our strategic initiatives. Net, we have done we have said what we do, and we have done what we said. And despite current inflationary pressures and the risk of recessionary headwinds we remain confident in our ability to continue to advance and create value through these initiatives.

And on that note, let's move on to a more fulsome discussion of our performance in the third quarter. Depletion growth for our beer business decelerated to 5.7%, which, as I mentioned earlier, was largely due to a recent series of headwinds that developed towards the latter part of the quarter. First, as we shared on our last call, we decided to introduce all pricing changes above our usual algorithm due to cost pressures across the chain, and historically, the impact of these types of notable pricing actions take a few months to settle in.

Second, distribution growth is returning to more normalized levels after lapping a softer summer period last year when we were managing supply constraints. That said, distribution growth remains at exceptionally healthy levels as well as aligned with our full year expectations. And third, some of these headwinds were particularly accentuated in a few key regions for our brands, such as California, where we lapped double-digit depletion growth rates and better weather in November of last year as well as more favorable economic conditions.

All of that said, our beer business continues to perform strongly relative to the wider market and to resonate with consumers who continue to shift to higher-end brands. In

IRI channels, we gained 1.5 points across the entire category and 2.3 points in the higher-end segment in the third quarter, which is higher, let me repeat that, which is higher than the share gains in the same quarter last fiscal year.

And when looking at depletions fiscal ’23 year-to-date, our beer business achieved growth of 7.8%, which continues to be in line with our annual expectations. Importantly, based on the prior activity we have seen in retail, as they adjust to the continued inflationary environment, we expect trends to return to more historical rates over the next few months.

Now shifting to the performance of our beer brands. Modelo Especial delivered depletion growth of 4.4% in the third quarter lapping a tough 13.2% depletion growth comparison in the corresponding period of the last fiscal year. That said, the brand has achieved depletion growth of 9.9% over fiscal ’23 year-to-date.

In the recent quarter, it continued to strengthen its position in the 5 states where it is already the #1 beer brand in dollar sales, delivering another approximately 0.2 points in share gains. Importantly, in the other 39 states tracked by IRI data, Modelo Especial delivered more than 4x the share gains at over 0.8 points. More broadly, Modelo Especial’s depletion growth in its secondary markets outpaced the growth in its top 5 states by over 10 points. As such, we continue to see significant incremental opportunities to maintain the momentum of Modelo Especial, particularly through distribution gains in the states where it is under represented.

Corona Extra delivered depletion growth of 1.3% in the third quarter and 4% in fiscal ’23 year-to-date. As noted earlier, the brand has maintained its momentum as the #3 share gainer in track channels. We continue to invest in the growth of Corona Extra through a thoughtful and authentic evolution of the brand’s market such as the augmented reality addition to our O Tannenpalm campaign, which is one of the more enduring holiday themed commercials running for over 30 years now. And we continue to see growth potential for Corona Extra with younger legal drinking age and multicultural consumers.

Pacifico's depletion growth accelerated in the third quarter to 40.7%. And over fiscal '23, year-to-date, its depletion growth was 32.9%. The brand remains a top 10 share gainer in track channels in the third quarter, mainly supported by its growing footprint in states like California, Nevada, Utah, Colorado and Arizona. We continue to see fantastic growth runway for Pacifico as one of our new wave brands with significant distribution potential relative to Modelo and even more so relative to Corona Extra. Particularly as the brand also continues to build momentum by shifting east in the U.S., building on the 26% depletion growth delivered in our Eastern business unit in the third quarter.

Lastly, our Modelo Chelada brands achieved depletion growth of 44% in the third quarter and 48% over fiscal '23 year-to-date. Our Model Chelada brand remained the #1 set in the Chelada space, and the brands gained nearly half a share point across all U.S. beer and track channels. For perspective, that is as much as Corona Extra's gain. In fact, these gains were largely driven by innovations launched this fiscal year, including Naranja Picosa flavor, the Limon y Sal 12 ounce 12 pack, which is a top 10 new patent SKU and our new variety pack, which is among the top 15 new brands.

We continue to expect significant growth from the Modelo Chelada brands as we invest in marketing to the general market consumer to broaden the demographic appeal for this product. All in, the strong demand for our brands in the third quarter supported a net sales increase of approximately 8% for our beer business. And despite the impact of inflationary headwinds on operating income, we were able to maintain operating margin at 37.5%. This gives us the confidence to once again raise guidance for our beer business this fiscal year lifting the low end of our growth outlook. We now expect to achieve 9% to 10% net sales growth and 4% to 5% operating income growth for fiscal '23.

Moving on to Wine & Spirits. Our Wine & Spirits business continues to advance its vision to be the high-end market leader. As noted earlier, our largest higher-end brands delivered strong performance relative to their categories in the third quarter. In our Aspira portfolio, which includes our fine wine and craft spirits brands, over the third quarter in track channels, The Prisoner brands grew dollar sales by 4.3%, while the fine wine segment contracted by 5.7%. And High West grew dollar sales by 22%, while high-end spirits segment grew by only 3.4% In our premium and mainstream Wine & Spirits portfolio, which we refer to as Ignite, both Meiomi and Kim Crawford gained share in the U.S. wine category.

Depletions for our Wine & Spirits business declined by 5.5% in the third quarter, mainly driven by continued headwinds based across our mainstream brands. However, our Aspira portfolio delivered strong performance with 8.5% depletion growth in the quarter. And in fiscal '23 year-to-date, our Aspira portfolio has now achieved an overall 6.3% increase in depletions supported by strong double-digit depletion growth for The Prisoner and High West.

Among Ignite brands, Meiomi and Kim Crawford have also delivered solid depletion growth in fiscal '23 year-to-date, supporting an overall 2.3% increase in depletions for our premium line portfolio. Our Wine & Spirits business also continued to expand its global omnichannel footprint, advancing its growth in direct-to-consumer, 3-tier e-commerce channels as well as international markets. Wine & Spirits DTC net sales grew 23% in the third quarter, and we continue to perform particularly well in 3-tier e-commerce which delivered dollar sales growth 9 points above the competition.

These results were underpinned by our strategic DTC investments in both hospitality through facility upgrades and talent development and our own e-commerce website platforms as well as our continued leadership in 3-tier e-commerce through marketing innovations like launching video ads on Instacart. And a strategic focus on major omnichannel national accounts, third-party marketplaces and digitally native retailers like Amazon, where we were the #1 overall supplier and #1 gross supplier in higher-end wine in the third quarter.

International markets accounted for 9% of the total net sales in the Wine & Spirits business in the third quarter as our strategically focused approach continued to target select metropolitan markets, including London, Tokyo, Seoul, Sydney, Mexico City, Zurich and Toronto with some of our most renowned premium and fine wine brands like The Prisoner, the Schrader as well as more recently acquired brands like Lingua Franca and My Favorite Neighbor.

And with our craft spirits portfolio, which includes brands like Casa Noble and the CAMPO high-end tequilas, that delivered international shipments 5x greater than the third quarter of the prior year. We are also pleased that our efforts to establish a leading global higher-end Wine & Spirits portfolio are gaining recognition with several of our brands receiving remarkable accolades including Schrader Cellars winning its 37th 100-point score and its Double Diamond brand being recognized by The Wine Spectator as its #1 wine of 2022.

Our To Kalon Vineyard was being recognized again as the top vineyard in North America for the fourth consecutive year among top vineyards in the world. And I'm pleased to report that our To Kalon Vineyard has now also is certified as organic, expanding the appeal of its lines to a broader set of consumers and adding to its differentiation. And in our spirits portfolio, our recently launched Nelson Brothers Bourbon Reserve was ranked among Whiskey Advocate's top 10 most exciting whiskeys of 2022. So all in, our Wine & Spirits business continues to make meaningful progress on its transformation.

And while net sales and operating margins, net of recent divestiture, were slightly lower relative to the third quarter of last fiscal year due to volume shifts from shipment timing only being partially offset by mix and pricing benefits we did see a significant sequential uplift in operating margins of 55 basis points relative to the second quarter of this fiscal year. This gives us confidence to reaffirm our fiscal ’23 guidance for our Wine & Spirits business of stable to 2% lower net sales and 3% to 5% operating income growth, which we are providing against the fiscal ’22 baseline adjusted for the recent divestiture.

Looking further ahead, we are also confident that over the medium term, both our beer business and our Wine & Spirits business remain well placed to deliver strong growth and best-in-class operating margins. That said, given continued inflationary pressures and the potential impact of recessionary environment, we remain mindful of balancing the momentum of our brands against near-term cost challenges.

To that end, based on our current expectations of the pressures that the consumer will continue to face in the near term, we are giving even more careful consideration to our pricing actions for fiscal ’24. In particular, we currently expect pricing actions for our beer business to be more muted in fiscal ’24 as our pricing actions in the current fiscal year were ultimately above our medium-term algorithm. While input costs remain at historically elevated prices we strongly believe that additional consideration in our approach to pricing in fiscal ’24 is warranted to sustain healthy growth for our brands.

In addition, while some input costs are below the peaks from earlier this fiscal year, we now anticipate inflation to remain above historical trends in the high-end single-digit range for fiscal ’24. As always, we will continue with our disciplined approach to manage these evolving conditions through cost-saving initiatives. But these persistent inflationary headwinds will be compounding on the double-digit cost uplift we have faced in fiscal ’23. As such, we now expect operating margins for our beer business in fiscal ’24 to be more in line with our anticipated margin structure for this fiscal year, and therefore, below our stated 39% to 40% medium-term range. We are still refining our outlook for ’24 and will provide more detailed guidance at our next earnings call, but we wanted to share some context today now that our annual planning process is underway.

With all that said, let me be clear. Our beer business continues to have best-in-class operating margins and our Wine & Spirits business continues to make progress toward achieving that same differentiation. We are also confident that over the medium term, our beer business remains well positioned to deliver leading operating margins, supported by the sustained momentum of our core Modelo Especial and Corona Extra brands, the significant opportunity being captured by our Pacifico, Modelo Chelada brands.

The incremental upside from our broader existing portfolio and the continued development of our innovation lineup particularly from exciting imminent additions like dell' Ornellaia and we continue to expect our Wine & Spirits business to make progress on its operating margins supported by continuing to pursue the exciting runway for growth of our higher-end brands and ensuring these brands represent an even greater portion of our mix over time, enhancing the performance of our mainstream portfolio through a greater focus on brands and initiatives with higher returns, including through relevant and innovative products and growing our omni-channel and international leadership particularly as an incremental opportunity for higher-end growth.

Now before I conclude, I wish to quickly touch on Canopy. We remain supporter of Canopy sellers to create an exchangeable share structure designed to support the consolidation of all its U.S. cannabis assets into a single avenue. And to that end, our intention continues to be to transition our existing common share ownership interest in Canopy Growth into new exchangeable shares once its shareholders approve this transaction. We believe that the conversion of our ownership interest will maintain our ability to realize the potential upside of our investment in Canopy.

At the same time this transaction and the surrender of our warrants are expected to eliminate the impact to our equity and earnings, mitigate risk to our organization and further reinforce our intent to not deploy additional investment in Canopy in line with our capital allocation priorities. In closing, I'd like to reiterate 3 main takeaways today. First, nearly 4 years ago we committed to a series of strategic initiatives aimed at delivering profitable growth and shareholder value. And I'm pleased to say that we are delivering against those initiatives and in many cases even exceeding the goals we set out to achieve.

Second, our third quarter results demonstrate that we continue to execute against these strategic initiatives and that our company remains in a strong position to deliver best-in-class results. Despite the headwinds in the quarter due to macroeconomic pressures and tough comps versus prior year, the strong performance of our beer business has put it on track to deliver better-than-expected results in fiscal '23. And the transformation of our Wine & Spirits business is also yielding results.

And third, we remain confident we will continue to build on our track record of solid growth and value creation through our strategic initiatives. And with that, I turn the call over to Garth.

Garth Hankinson

Thank you, Bill, and good morning, everyone. As Bill mentioned, we delivered another set of solid results in the third quarter and continue to make progress against our operating plans and strategic initiatives. Our beer business achieved high single-digit net sales growth and continue to deliver best-in-class operating margins. Our Wine & Spirits business made additional progress against its strategy with an even more premiumized portfolio further aligned with consumer trends following our recently completed divestiture. Additionally, we generated strong cash flow results and with yesterday's declared dividend to be paid in February, we are on track to exceed our stated $5 billion goal of returning cash to shareholders in the form of dividends and share repurchases between fiscal '20 and fiscal '23.

I will now review our Q3 performance and full year outlook in more detail, where I will generally focus on comparable basis financial results. Starting with our beer business. Net sales increased 8%, primarily driven by higher average price increases and solid demand across our portfolio. Q3 shipment volumes were up 3% reflecting a difficult buying lap given the focus of replenishing product inventories in the same period last year. From a depletions perspective, we achieved growth in the quarter of approximately 6%, driven by the demand of our Modelo family of products, including the Modelo Especial and Modelo Chelada brand as well as double-digit growth from Pacifico.

As Bill noted, depletions decelerated sequentially from Q2 to Q3. This was primarily due to: number one, incremental fall pricing that, as expected, will put us above our targeted annual average increase. Notably the impact of our fall increases has been heightened by additional pricing actions across the value chain. That said, we expect the impact of incremental pricing will settle over the coming months as we have seen in prior similar circumstances.

Number two, relatively lower distribution growth in Q3 versus Q2, where we lapped a softer prior year period when we were managing supply constraints. And while we are seeing distribution growth return to normalized levels, it remains aligned with our full year expectations. Importantly, it is worth noting that Q3 distribution growth remained well above the levels we achieved in Q4 last year and Q1 of this year.

And number three, as Bill also referenced in the third quarter, particularly in the month of November, we lapped multiple tailwinds from last year such as double-digit depletion growth rates in key regions like California, which benefited from periods of warmer weather and a stronger macroeconomic environment. All of that said, we expect depletion trends to continue to normalize as we move into fiscal 2024, and we remain confident in our fiscal year expectations. Selling days in the quarter were flat year-over-year, but please note that in Q4, there will be 1 less selling day. Operating income for the beer business decreased 2% and operating margins declined by 380 basis points to 38%.

As expected, operating income and operating margins were negatively affected by on-going inflationary pressures across raw materials and packaging, particularly as more favorable hedges rolled off. Increased logistics expenses related to higher fuel and freight costs, incremental operating costs and increased depreciation as a result of our brewery capacity expansions, and increased marketing spend, particularly from our media investments in sports sponsorships with NFL and TAA Football, Major League Baseball, the NBA and the NHL. Marketing as a percent of net sales increased 160 basis points to 9.6% in Q3. For fiscal '23, we continue to expect that marketing as a percent of net sales will be in the 9% to 10%. More broadly, given the strong top line growth of our beer business year-to-date, we now anticipate it will grow net sales between 9% to 10% and operating income between 4% to 5% for the full fiscal year.

This still implies an operating margin of approximately 38% for fiscal 2023. As expected benefits from our 2% to 3% average pricing increase for the full year and our cost-saving efforts will be more than offset by the same headwinds that have affected our margins year-to-date. I'd like to take a moment to reiterate some of the points Bill made earlier regarding fiscal '24. As mentioned, we are anticipating our beer business margins to be more in line with our anticipated margin for this fiscal year, and therefore, below our stated medium-term target range of 39% to 40%. This is driven by the fact that input costs remain at historically elevated levels due to ongoing inflationary pressures.

As we have shared in some of our prior calls, we hedged about 10% of our beer business costs to help reduce volatility in the P&L. However, our commodity hedging program is managed on a multiyear rolling basis. So we currently do not anticipate our blended hedge rates to capture the favorability of recent declines in certain commodity prices until the second half of next fiscal year. In addition while prices have declined from their peaks earlier this year for commodities like aluminum and natural gas, which are part of our can and glass cost, they still remain above pre-pandemic levels.

Beyond our hedging program, most of our beer business input costs have a greater exposure to inflationary pressures, including raw materials, such as wood pallets, steel crowns and cartons. The majority of these input costs are subject to contractual agreements that tend to reflect negotiated prices that are based on existing inflationary conditions. So as we move forward with our annual planning and supplier cost determination process, we will develop a clearer view of these contractual prices and on the resulting margin expectations. Against that backdrop, with these processes now underway, we have greater visibility into the high single-digit cost segments that will continue to build off the double digit unfavorable cost outlook that our beer business faced in fiscal ’23.

In addition, we continue to see ongoing macroeconomic pressures on the consumer, which are leading us to plan to take more subdued pricing actions across our beer portfolio in fiscal ’24. That said, we expect a number of tailwinds that will partially offset some of these elements, including the continued momentum of our core brands, capitalizing on opportunities with emerging brands such as Pacifico and Modelo Chelada’s, winning with new and future innovation such as Modelo or Modelo Oro and through our consistent and disciplined cost savings actions, nevertheless, as Bill mentioned, we will continue to refine our outlook for next year, and we will provide detailed guidance during our Q4 earnings call.

That said, it is important to reiterate that our expected fiscal ’23 and fiscal ’24 operating margins remained best in class. And in fact, when considering our fiscal ’20 through our currently anticipated fiscal ’24 margins, we expect the average operating margin for that

5-year period to remain within our medium-term algorithm of 39% to 40%.

Now shifting to Wine & Spirits. As a reminder, during our recently concluded third quarter, we divested a series of brands from our Wine portfolio. As such, third quarter of fiscal ’22, included approximately $17 million of net sales and $11 million of gross profit less marketing, that are no longer part of the Wine & Spirits segment results. When presenting today’s results, I will be discussing our top line results on an organic basis, excluding the contribution from those divested brands in the preceding periods.

Starting with organic net sales. The Wine & Spirits business decreased 1%, primarily driven by a 13% increase in shipments, partially offset by a favorable product mix, which both related to consumer-led premiumization and mix improvements of our portfolio. From a depletions perspective, while the Wine & Spirits business saw a decline of approximately 6% on an organic basis in Q3 as Bill noted earlier, our higher-end brand delivered strong performance with our Aspira portfolio, which includes our fine wine and craft spirits brands, delivering depletion growth of 9%, driven by growth in our Prisoner Wine and High West brands.

Meanwhile, our Ignite portfolio, which includes our mainstream and premium Wine & Spirits brands primarily faced headwinds from our mainstream brands, which was down 8%. That said, in tracked channels, our largest higher-end brands continue to outperform their corresponding segments, and our peak premium brands portfolio actually gained share in the category with particularly strong performance from Meiomi and Kim Crawford in both volume and dollar sales growth.

Moving on to Wine & Spirits operating income and operating margins. Wine & Spirits operating income declined by 7%, partly as a result of the divestiture and operating margin decreased 60 basis points to 24.8%. The decrease in operating margins was driven by higher transportation costs, including ocean freight shipping, unfavorable costs from higher drivers largely due to inflation and increased general and administrative expenses due to higher compensation and benefits primarily related to higher headcount from our continued strategic focus on expanding into direct-to-consumer channels and higher-end brands in our Aspira portfolio.

For full year fiscal '23, we remain confident in our previously stated outlook for our Wine & Spirits Experience business. We expect fiscal '23 organic net sales decline of 0% to 2% and operating income to increase 3% to 5% implying a full year operating margin of about 24%. Looking ahead to fiscal '24, we expect our Wine & Spirits business to continue to make progress on its operating margin. We believe our Wine & Spirits business is positioned to further improve its operating margins through growth of our higher-end brands, bolster performance from our mainstream portfolio through high-return brand initiatives such as innovation, and expansion of our omnichannel and international footprint.

As I mentioned earlier, we are currently working through our annual planning process and we'll provide a more detailed fiscal '24 outlook during our Q4 earnings call. Now let's proceed with the rest of the P&L. Corporate expenses came in at approximately $75 million, up 70% versus Q3 last year. This increase in corporate expense was primarily impacted by costs associated with increased compensation and benefits, primarily related to a third quarter fiscal '22 reversal of stock-based compensation and third-party services related to our ongoing investments in our digital business acceleration initiative.

We now expect our total corporate spend to be between $290 million and $300 million for the full year, mainly driven by the incremental costs in Q3. Interest expense for the quarter was up 12%. Also, as we noted in our release, following the completion of the reclassification of our Class B common stock, we now expect interest expense for fiscal '23 to be between $390 million and $400 million. This includes the interest expense associated with the funding of the $1.5 billion cash consideration which is expected to be $80 million to $90 million on an annual basis based on current market rates. Our Q3 comparable basis effective tax rate, excluding Canopy equity and earnings, came in at 18.8% versus 14% in Q3 last year.

The effective tax rate increased mostly due to the change in stock-based compensation benefits. As a result of these updates to our outlook, the increased interest expense due to the reclassification bonds, adjustments relating to our most recent divestiture in our Wine & Spirits business and increased corporate expenses that were only partially offset by the increased expectations for our beer business. We now expect comparable EPS guidance to be in the $11 to $11.20 range, which represents a $0.20 decrease to the bottom end and a $0.40 decrease at the top end of our prior guidance range.

Moving to free cash flow, which we define as net cash provided by operating activities less CapEx. We generated free cash flow of $1.6 billion for the 9 months of fiscal '23 reflecting strong operating cash flow partially offset by a 14% increase in CapEx investments as we continue to support the growth of our beer business through our brewery capacity expansion plans. And on that note, to echo Bill, we are excited by the progress we have made with our new sites in Veracruz in which we recently broke ground. Our fiscal '23 free cash flow is now expected to be in the range of $1.5 billion to $1.6 billion and CapEx is now expected to be between $1.1 billion and $1.2 billion. Operating cash flow for fiscal '23 remains unchanged and is expected to be between $2.6 billion and $2.8 billion.

Related to our uses of these cash flows, as we recently noted in December, our capital allocation priorities moving forward following the reclassification remain fundamentally aligned with the priorities we introduced in fiscal '20. To achieve a disciplined and balanced and thoughtful approach to support growth and value creation. Our recently updated capital allocation priorities are as follows: first, we remain committed to our investment-grade rating and to targeting dividend growth in line with earnings as key elements of a disciplined financial foundation.

We ended the third quarter with a net leverage ratio of approximately 3.5x when factoring in the financing for the cash payment associated with our recent transition to a single-class stock structure and excluding Canopy equity earnings. That said, we have set a target net leverage ratio on that same basis of approximately 3x, which we are confident we can return to.

Another important element of our commitment to a disciplined financial foundation is targeting an approximately 30% dividend and payout ratio. Second, we will continue to balance investments to support the growth of our business and deliver additional returns to shareholders through share repurchases. As we look ahead, we continue to expect adding another 25 million to 30 million hectoliters of brewing capacity between fiscal 2023 and fiscal 2026. This will be supported by $5 billion to $5.5 billion of investment over that same period. We are developing this capacity through a series of expansion ways which is consistent with the modular approach we have adopted to maintain capital expenditure discipline and flexibility.

We remain committed to executing share repurchases targeted to at least cover dilution. While we also have approximately $1.2 billion of our repurchase capacity still under our current board authorization and plan to remain opportunistic, particularly since we achieved incremental cash flow flexibility. And third, we may deploy excess cash to smaller acquisitions. Again, we intend to remain disciplined in our pursuit of any M&A opportunities and we'll continue to pursue transactions that we believe fulfill one or more of the following characteristics: are consumer led, they deliver growth momentum, providing compelling returns, fill portfolio gaps, and offer synergistic benefits.

Lastly, on Canopy. As it announced in October, Canopy plans to consolidate all of its U.S. cannabis assets into a single entity, Canopy USA. This U.S. holding company and new exchangeable share structure is designed to enable Canopy USA to trigger full ownership of Canopy's U.S. cannabis investments and capitalize on the U.S. cannabis market opportunities. Assuming the completion of this transaction and approval by Canopy shareholders of a charter amendment we intend to transition our existing common share ownership interest in Canopy into new exchangeable shares, which is intended to protect Constellation shareholder value while retaining an interest in Canopy through nonvoting and nonparticipating shares.

This share ownership transition and the surrender of our Canopy warrants is aligned with our focus on core beer and Wine & Spirits businesses and capital allocation priorities. As a reminder, until this transaction is completed and we convert our holdings into exchangeable shares, Canopy will still be reported within our P&L consistent with past quarters.

In closing, we continue to demonstrate strong execution in growing our core business and investments to enhance our portfolio of industry-leading brands. As we approach the end of the fiscal year, we remain committed to delivering against our stated goals to drive sustainable and profitable growth and build shareholder value. And with that, Bill and I are happy to take your questions.

Question and Answer

Operator
— Operator Instructions —

Our first question comes from the line of Lauren Lieberman with Barclays.

Lauren Lieberman
When you walk through the drivers of the change in trend for depletions that you saw towards the end of the quarter, one sort of mention was a comparison on macroeconomic trend versus the prior year and then also your comments on taking sort of more muted

pricing as you look into ’24. So I’d love if you could just spend a little bit more time talking about what you’re seeing from your various kind of core consumer groups, it feels like I know you pointed out some share gain continues. But when we look at some of your brands relative to other high-end brands, core beer brands, not Seltzer, it does look like there’s underperformance, it’s specific to your brands. So just any further diagnostic you may have done would be really helpful to hear about? And then also, I wasn’t entirely clear on why the slower CapEx spend, I know you just went through it across at the very end of your comments, but I was hoping you could just reframe that because I admittedly missed why is it $200 million lower this year?

William Newlands

Sure. So relative, Lauren, to the depletion trend scenario, we’re still seeing in our – all of our assessment and research suggests that we continue to have very strong support for our brands among our core Hispanic base as well as growing trends amongst the non-Hispanic community. I think a great example of that shows itself in that we actually had an increase in our share gain quarter-on-quarter from last year which reflects very well. Certainly, some of what we saw at the latter part of this quarter was driven by a couple of things. One is many businesses, including ours, took additional pricing over what we had planned. And that caused an overall softness in the market, particularly in the state of California. It wasn’t limited to us. And frankly, that’s not an unusual reaction. We’ve seen that many times before.

Frankly, what we were very pleased about as we then look into December and to see if this thing is beginning to go back to some normalcy, we see that it has been, we saw a 7.5% swing to the upside in dollars versus where it was in November and that compares to a category swing of 4.5%.

So again, we saw a significant improvement in the market that was primarily the cause of a bit of deceleration in our depletion performance as we got into December, and we continue to gain share in that overall mix of swing. So we're not – we – this is not an unusual event. It happens virtually every time you see significant pricing action taken and the fact that we continue to gain share at the clip that we are gives us great confidence going forward and the strength of the brands overall. Garth, anything you want to say.

Garth Hankinson

Yes, Lauren, just on the CapEx, it's important to note that we continue to progress with our expansion as planned. As we stated in the remarks, we've added 11 million hectoliters of capacity over the last several years, $9 million in growth, sort of $2 million through productivity initiatives. We are on track with our expansions at both Nava and Obregon. And as we mentioned, we've recently broken ground in Veracruz. So the reduction in CapEx for this year is not necessarily abnormal as we move through the year. It really has more to reflect the timing of when payments will be made and less to do with progress.

Operator

Our next question comes from the line of Nik Modi with RBC Capital Markets. .

Nik Modi

Bill, I was hoping maybe you could talk about what's actually happening with some of the pricing as it goes through the supply chain? Certainly, we've picked up some commentary within the trade that pricing was taken on top of what you actually took in the market. And I'm just curious what the state of that is, if it's starting to get unwound? And have you seen any implication of that in some of the more recent weeks?

William Newlands

Yes. You bet, Nik. You're absolutely right. One of the things that we saw that occurred after our pricing increase is that other players within the chain took more price on top of what our pricing increase was. And frankly, this often happens. Well it tends to happen, and we've already started to see it in certain some markets is that, that moderates over time as well because an attempt is made to see what the consumer is ready to accept. And if we find a spot that's a bit more than they are ready to accept you see some moderation in that increase. You've already started to see that with some critical change in the state of California, which probably relates to my answer to Lauren a moment ago, which is why you saw the trends in December change quite a bit.

So you're correct there was a lot more and it piled on, if you will, once it was out of us and into further down the chain, more was taken and as we often see that goes higher early and then moderates over time.

Operator

Our next question is from Nadine Sarwat with Bernstein.

Nadine Sarwat

I just want to stick with depletions here. I know you gave those explanations in your prepared remarks, but I have 2 follow-ups. So the first is that the reported depletion still meaningfully lag the trends in the Nielsen track channels, which I would have assumed would reflect a number of the factors that you called out, so could you help us understand this gap? And then the second question is, I know you've mentioned that you have confidence that your depletions would return to those normal levels. But we are still seeing weakness in the December Nielsen trends. So could you provide some color as to what gives you that confidence? And what are your quarter-to-date depletions at the moment?

William Newlands

Sure. So let's start with the question of track channels. One of the things that we have historically found is that you're in the roughly – there's roughly 3-point delta, we use IRI, I realize you just said Nielsen, we use IRI. There's roughly a 3-point delta historically between the growth that you see in the tracked channels and the depletion rates. Interestingly, that got massively bigger when you're in the middle of the pandemic because the percentage of business that went through the off-premise trade increased substantially. That has now come back to somewhat of a more normalized level as you get to a little bit better positioned in the on-premise, not quite back to where it was, but it's directionally.

So that is some of what you are seeing is you're back to a more traditional split between those individual things. Relative to – and I quoted to the California, some other states are seeing a bit different. Texas on the other was also a market that was somewhat softer post price increase, and that one has not rebounded just yet. But that, again, is not unusual either. It's a little bit of a different channel mix than what you see in the state of California where you often see a more faster response to whatever impact pricing increases take. So this, in our judgment is all part of a normal process of when pricing actions are taken.

It takes a few months for it to all work its way through the system. Relative to the depletes, we don't have the final numbers in. As you would expect, we're only in day 5 of the new year and obviously, it included the new year, which makes the reporting a little bit behind. What I would say is that we're comfortable with where we think the summer is going to land. Otherwise, we wouldn't have raised our guidance.

Operator

Our next question is from Kaumil Gajrawala with Credit Suisse.

Kaumil Gajrawala

Not to belabor the pricing conversation, but when you mentioned 2024 pricing to be more muted, could you maybe just talk a little bit more about what that means? And then Garth, when we think about the share price, not just the movement today but perhaps more recently and perhaps even the fact that it's been – the share has been flat for a period of time. Does that change how you're thinking about share recalls?

William Newlands

So relative to 2024 pricing, as we stated in the last quarterly call, we were going to go above what our expectations had been. And that reflects, obviously, in the October increase that has taken us above our traditional 1% to 2% guidelines. What we're suggesting relative to 2024 is that it's going to be much more in line with what our historical trend has been, which is 1% to 2%. We would not expect it to go beyond the top end of the range as we did in this particular year and late in this fiscal year.

Garth Hankinson

Yes, Kaumil on the share repurchase, I just want to make sure it's clear that we haven't necessarily deprioritized share repurchase activity. As we mentioned, we have $1.2 billion worth of capacity under our current board authorization. In the near term, we think that it's more important to focus on getting our leverage ratio back down close to 3%. That being said, we do have the flexibility to be able to – to take advantage of weakness in the marketplace, as we said in our prepared remarks and be opportunistic. So it's absolutely something that we have the flexibility and optionality to execute against.

Operator

Our next question is from Bonnie Herzog with Goldman Sachs.

Bonnie Herzog

Just maybe first, a quick clarification on your pricing. I'm wondering if you're still expecting to be in your 2% to 3% pricing guidance range for the full year since I guess that would imply only around 1% pricing in Q4? And then, I guess, a question on your guidance, just in terms of your beer guidance, you raised your full year sales and op income growth, but it does imply shipments will be down maybe as much as high single digits in Q4. So I'm aware you're lapping the distributor inventory build from last year, but just trying to reconcile this with some of the key initiatives you have out such as the rollout of Modelo

Oro that's shipping now. So maybe if you could touch on that? And then just finally, I wanted to clarify if you expect your full year shipments and depletions to be broadly in line with each other?

William Newlands

Sure. We do expect to be slightly above our 2% to 3% that we quoted in the last quarter, when all is said and done for the year. We also – you should also recognize that mix is going to be higher and in large part because of the significant increase in the Chelada business, which is mix accretive in the overall portfolio. Garth, do you want to touch on the other piece?

Garth Hankinson

Yes. Just in Q4, right? I mean as a reminder Bonnie, as we said throughout the year, you need to focus on sort of full year performance as that we're going to – it was going to be sort of uneven or choppy results throughout the year, given the fact that we had the difficult overlaps as we were in the first half of last year dealing with some production-related issues in the second half of the year, we were building back inventories. So Q4 will certainly be muted this year versus what it was last year as last year was sort of artificially high due to that, those rebuilding efforts.

Operator

Our next question is from Dara Mohsenian with Morgan Stanley.

Dara Mohsenian

So I know we spent a lot of time on depletions already, but just a couple more specific follow-ups to drive a finer point on it. A, just as we think about the deceleration we've seen in nontrack channels, the untracked channels the last couple of quarters here. I wanted to get a little more detail on your perspective on what's occurring there. Is it more just look, there's less momentum from an on-premise recovery post-COVID as you cycle the more normalized post-COVID comps, might there be more of a macro slowdown on the untracked off-premise channels as theoretically volume shift to track channels in areas like Bodegas, et cetera, just sort of break down that nontracked channel mix a bit in terms of talking about on-premise versus the untracked off-premise so sort of extended a bit beyond the answer and maybe into the question?

And then Modelo does look like it's disproportionately slowed. Just to check on that, it seems like your mindset is more that it's related to some of the weakness in California, some of the pricing impact, less sort of more temporary factors. Is any of that sort of related to more longer-term factors? Maybe it's at a much larger base and you're having – you're not going to see as much growth? How do you sort of think about the Modelo brand and its performance recently?

And then last, sorry for the multipart question, but price/mix was obviously very strong in the quarter. Some of that is higher year-over-year pricing. But presumably, some of that is mix also. So are you seeing a big shift to smaller packages, might that also be part of the reason for some of the depletion weakness. So I just wanted to get a little more clarity on those points as it related to depletions?

William Newlands

Sure. Let's try to tackle those one at a time. Relative to Modelo, well, importantly, we are still seeing share gains in our 5 biggest markets. I think that's really important. But we're seeing several times those gains in the other markets with track channels, which we see as we've said many times before, a tremendous upside opportunity, this brand is still under shared, if you will, in terms of its household penetration compared to Corona Extra as an example. So there's just a lot of runway for growth for Modelo, and we remain very, very comfortable and confident in that brand's ability to continue to accelerate.

Relative to the nontracked channels, we have continued to see on-premise get closer to where it had been, but it's still not quite to where it was before the pandemic, one. Two, it always takes a bit more time in some of the smaller Bodega style nontrack channels for pricing actions to work their way through. We've seen that happen before. And obviously, when you include and talk about the state of California, which is our single biggest share market, I'll remind you that Modelo Especial is bigger than Coors Light, Miller Light, Bud Light combined.

When you see some of that happen it has a disproportionate impact in the short term until the pricing scenario plays itself through. So we don't believe this is any long-term trend issues. And our confidence in that is bolstered by the fact that as I stated earlier to one of the earlier questions, that we saw a very strong rebound in the State of California during December.

Relative to price mix, a piece of that – by the way, I should also mention, the #1 share gainer in the State of California in the last 4 weeks happen to be Pacifico. I think that also speaks to the strength of our portfolio. Our portfolio is not a one-trick pony. We have a very strong place in the Corona brand, and the Modelo brand as well as Pacifico, all of which I think is very positive. Relative to the price mix question, right? We are seeing mix benefits.

Some of that, as I stated just a moment ago is related to Chelada, given how big and important Chelada has gotten to be, that is mix accretive to our overall business. And therefore, the 40-plus percent growth profile that you see from that particular subsegment of Modelo does add significantly to the mix benefit that you observed.

Operator

Our next question is from Kevin Grundy with Jefferies.

Kevin Grundy

So my question relates to trade down in the category over the next 12 months, given the sort of obvious element in the room with the macro factors. And I wanted to tie that in your level of confidence on – in your beer segment. So we are seeing trade down like we see it in the Nielsen data for economy beers, which, of course, have been donating share for a long period of time.

So Bill, how concerning is that when we look at trade down behavior and we've seen it in past recessions as well. I just want to see how that's sort of in forming the view. And I think relatedly, just given some of the concern that's out there in the market today, I think folks would be very keen on hearing your level of confidence, I guess, in your intermediate term, high single-digit growth outlook for the beer business. The color you guys gave on margins was certainly helpful. And it looks like you're taking a conservative tack there. Is it reasonable to take a sort of similarly conservative tack in your outlook for top line growth in the beer segment looking out to next year as well?

William Newlands

Sure. I'll go backwards there on that. Hopefully, I won't miss anything. We maintain our continuing expectation of our medium-term guidance that we've said before, we don't think there's any radical change to where that has been. And as you know, we've often beaten that in the past. Relative to trade down, we'd obviously watch this carefully. We are very fortunate in the alcohol beverage business that we tend to be recession-resistant, doesn't mean that there's no impact that we are – it is certainly resistant.

The interesting thing that's occurred at this particular time is we've seen variable trade down at our price points. It doesn't mean – you're correct, there has been trade down, but it has tended to be from price points below us going even lower rather than trade down from our brands which I think speaks very strongly to this year's strength of those brands. We have seen some trading around within our brands.

I know – as I said a moment ago, the Pacifico scenario in the state of California is spectacular. And I think is reflective of the growth potential for that business but it also reflected some trading around within our portfolio that occurred. So we are less concerned. We also keep our eye on it. We are less concerned about trade down from our price points. And remember, we are continuing to market these brands in the same way that we have historically. Our share of voice at the consumer level has never been higher. And I think that's important as well. We continue to invest behind our brands to support those in the eye and the mind of the consumer. And I think that's going to be critically important during a time when there could be some trade down lower in the category.

Operator

Our next question is from Andrew Strelzik with BMO.

Andrew Strelzik

First, I'll follow up quickly and then another question. The follow-up is on pricing again. I'm just curious, obviously recognizing that you're making some of the commentary about '24 being a bit more muted, while you're seeing some volatility in the depletion trends. So can you just talk about how you'll be approaching that or what you'll be watching as you move through the year potential flexibility there, things maybe holding a little bit better? And then the other question is just on product innovation, which you mentioned all the growth that's been driven by product innovation in the last several years. How does the innovation pipeline look now versus the last several years? Are you – where are you seeing kind of the biggest opportunities or where is the focus? And is that more or less relevant in this consumer environment?

William Newlands

So relative to pricing, Andrew, we believe we're going to be more – we took more price now in October which will inherently have some rollover benefit within the P&L. But relative to new pricing taken in next fiscal year, we expect them to be back in that 1% to 2% range that we have consistently delivered. We think that's important, especially in an environment where the consumer is overly sensitive to pricing actions.

We're in an inflationary environment across all areas in the consumer space. And our view is we need to be careful in balancing our growth profile with our pricing profile. And we're going to continue that thought and approach going forward because we think it's in the best long-term interest of our brands.

Innovation is going to continue to be an important part of what we do. As you know, we're very excited about the launch here in March of Modelo Oro. Certainly, the Chelada business continues to be one of our great growth drivers. And many of those things, as I noted in my prepared remarks, are products that are relatively new. As you probably know, this fiscal year, we added a 12 pack, we added 12 ounce. We're putting a variety pack in. That's been very successful also. So we're reaching more consumers and more consumer occasions than what we have done. And therefore, we continue to expect innovation to be an ongoing part of our success, same through the wine business.

You saw that with things like Unshackled with things like our Red Blend in Meiomi. You saw that with Illuminate, with Kim Crawford. We're – and innovation has been a strength of our companies and that we can put outstanding liquids in the bottle or can as the case may be and continue to do so, and we think that's going to be an important part together with our core organic growth of our growth profile going forward.

Operator

Our next question is from Chris Carey with Wells Fargo.

Christopher Carey

So I'm just trying to get a little bit more comfort with the outlook on beer operating margins for next year. If I just take this concept of muted pricing and high single-digit inflation, I'm coming up with a little bit of operating margin compression, right, and maybe modest operating income growth in beer next year.

And so I'm just wondering if that logic is sound or whether there are other things going on here like incremental savings programs for less spending elsewhere, which gets you to, I think, what you're implying is operating margins are flat, and if not, I just wonder if there's a more important revision of estimates that's required here, so thanks for any clarification on that? And any help you can provide on the bridge math.

Garth Hankinson

Yes, Chris, thanks for the question. Look I think it's important to note that we will continue to deliver best-in-class operating margins, both this year and next year. As we said during the call, we're in the process right now of going through our annual planning review. And so we'll have a lot more detail to share on this with our Q4 earnings release and outlook for FY 2024. That being said, we did want to use today to acknowledge that next year's margin profile is going to be more in line with this year's margin profile for all the reasons that we discussed. Certainly, inflation continues to be enduring, and it's lasted longer than anyone had expected.

And as we noted, many of our costs are contractual in nature, and those contracts when they get renegotiated, they get renegotiated at sort of the then inflation rate, not necessarily what the outlook for the year is. And we're going through that process again right now. So we'll have more clarity around where we land on those as we go through the next several weeks and months. We've talked about hedges in commodities, and commodities coming off their highs, but certainly, they certainly haven't reverted yet to where they were pre-pandemic, so they will continue to be a bit of a headwind for us next year.

Depreciation will also be a bit of a headwind next year for us as we lay around the incremental CapEx that I referenced to Lauren's question, we will – we do expect to go live with our ABA capacity expansion at Nava as well as that incremental capacity at Obregon. What's the impact to that depreciation on, again, we'll know better about that in the next few months because that's all dependent upon when assets are put into service.

And then as you know, pricing will be a bit more muted. Again, we're still going to be within our 1% to 2% algorithm. We just won't be above 2%, like we have been not just this fiscal year but last fiscal year as well. And so those will be some of the headwinds. And again, we always have tailwinds for as well. The continued momentum of the brands, right? We'll continue to – the brands will continue to grow and drive efficiencies, and we always have a robust set of cost savings initiatives that we will avail ourselves up. And again, we'll have more detail around what – how each of those impact margins for FY '24 as we release our FY '23 annual results, but we wanted to acknowledge that on this call.

Operator

Our next question is from Bryan Spillane with Bank of America.

Bryan Spillane

Just one quick one for me. Garth, I guess while we're talking about '24 there's a $26 million, I guess, gross contribution after marketing hit from the Wine & Spirits divestitures that affected fiscal '23. So does any of that spill into fiscal '24? Or are there still I guess drags from divestitures that we should be thinking about as we're just polishing up our '24 model today?

Garth Hankinson

There won't be any more necessarily more drags per se from that, as the cost will come out. I won't say that the impact that you'll have is that there will just be a comparability issued for the first sort of 3 quarters of the year, but no further drag as we move into the year.

Operator

And our final question comes from Vivien Azer with Cowen and Company.

Vivien Azer

I was hoping we could pivot to the wine segment, given the conversations around down trading in beer Bill, I was hoping to get some perspective on what you guys think you're seeing in wine, the Nielsen data would suggest that there is down trading there? And if you could just remind us, given all of the divestitures that you guys have done, what percentage of your wine revenues are coming from $20 and above?

William Newlands

Sure, you bet Vivien. We have seen some more trading down in the wine business in the fact that private label has been tending to outpace branded sales by roughly 2.1 points in the last 12 weeks. So that has had some impact. What's interesting is you get a bit of a, I would say, a buying model scenario, meaning you're seeing some trade down at sort of mid- to lower price points. And then you're doing fine if you get into higher price points and a little bit in the middle has been a little shaky is some of what we're seeing. So – which is a little different than what you have seen historically in these particular environments. As I said in my prepared remarks, there's been a pretty radical change in the amount of our business in the premium sector.

I would – I didn't categorize it as $20. But we're well over 60% of our total business now occurring in the premium and fine wine sector, which was 34% just a few years ago. So we're seeing a pretty radical move within our business as we thought what if we reshape the portfolio because over the long term that's where the consumer is going. And we believe that's not only where there's better profitability but there's better growth as well. So we believe the work that we've done is bearing fruit, and I think it plays itself out in terms of the growth profile of some of our higher end and critical brands.

Operator

We have reached the end of the question-and-answer session. I'd now like to turn the call back over to Bill Newlands for closing remarks.

William Newlands

Thank you, Rob. Despite the ongoing inflationary headwinds affecting the concern in our business over the last 3 quarters, we're on track to deliver another strong year of growth and remain well placed to further build on the solid track record we have established against advancing our long-term strategic initiatives for nearly 4 years now.

Our beer business continues to lead in share gains, growth and margins and we're confident in our ability to capture the significant opportunities we still see for our core and our next wave brands.

Our Wine & Spirits premiumization strategy continues to gain momentum as well advancing our higher-end brands, DTC channels and international footprint, all yielding noticeable results. Lastly, the performance of our businesses, coupled with our disciplined and balanced capital allocation priorities has allowed us to maintain our investment-grade rating, surpass our cash returns goal, grow our beer production capacity and execute small growth accretive M&A.

With all that said, let me reiterate, looking ahead, we remain committed and believe we now have an even stronger foundation to deliver sustainable growth and value creation for our shareholders. Thanks for everyone for joining the call, and I wish you a happy, safe and healthy new year.

Operator

This concludes today's conference. You may disconnect your lines at this time, and we thank you for your participation.