The Apple Doesn’t Fall Far from the Tree…

CRAFT INDUSTRY UPDATE, SPRING 2019

CALIFORNIA CRAFT BREWERS ASSOCIATION

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Newton's Three Laws

for the rudimentary physicist

(or craft brewer)

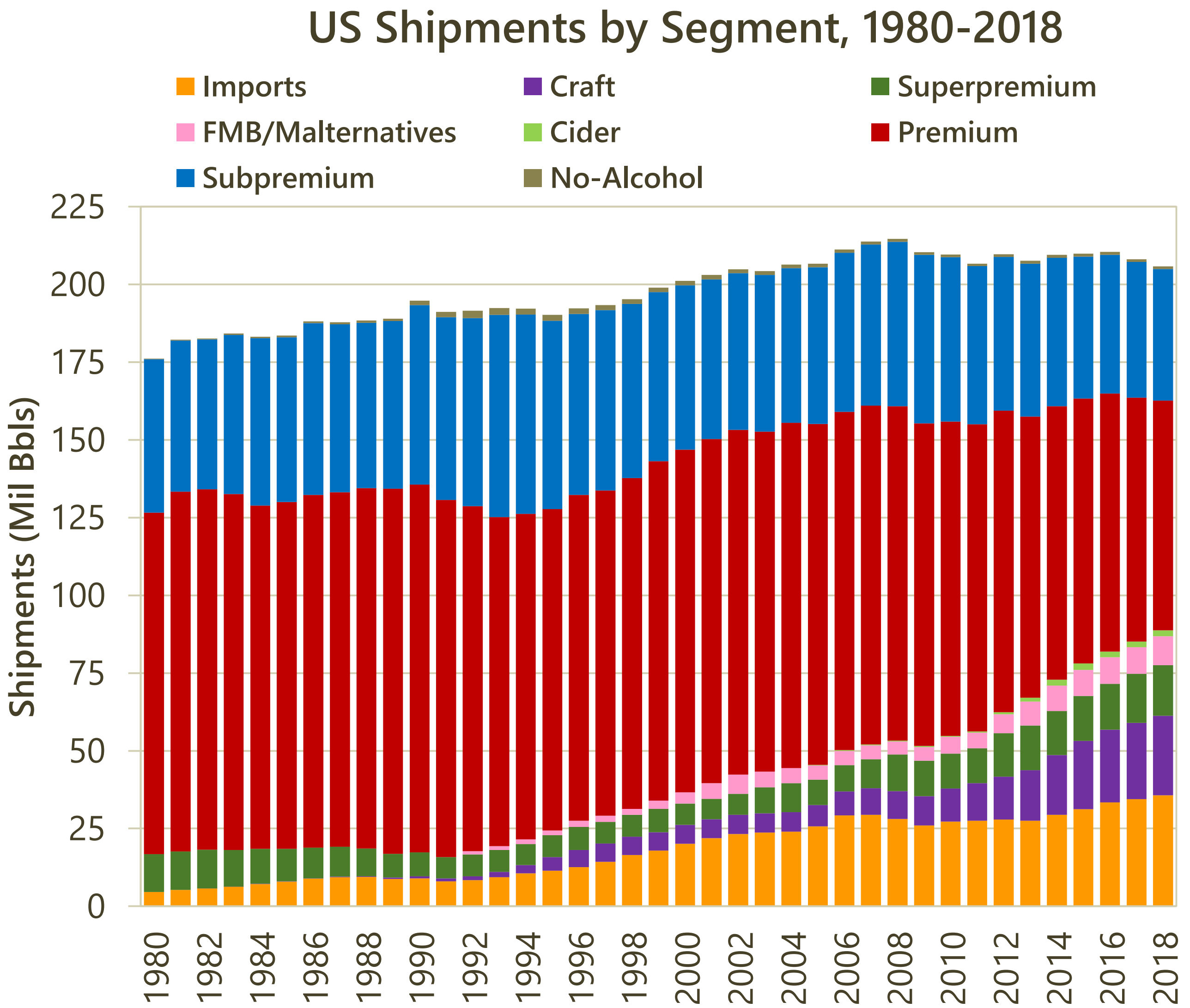
1 | "…an object in motion stays in motion…"

Long-term beer trends: premiumization & fragmentation

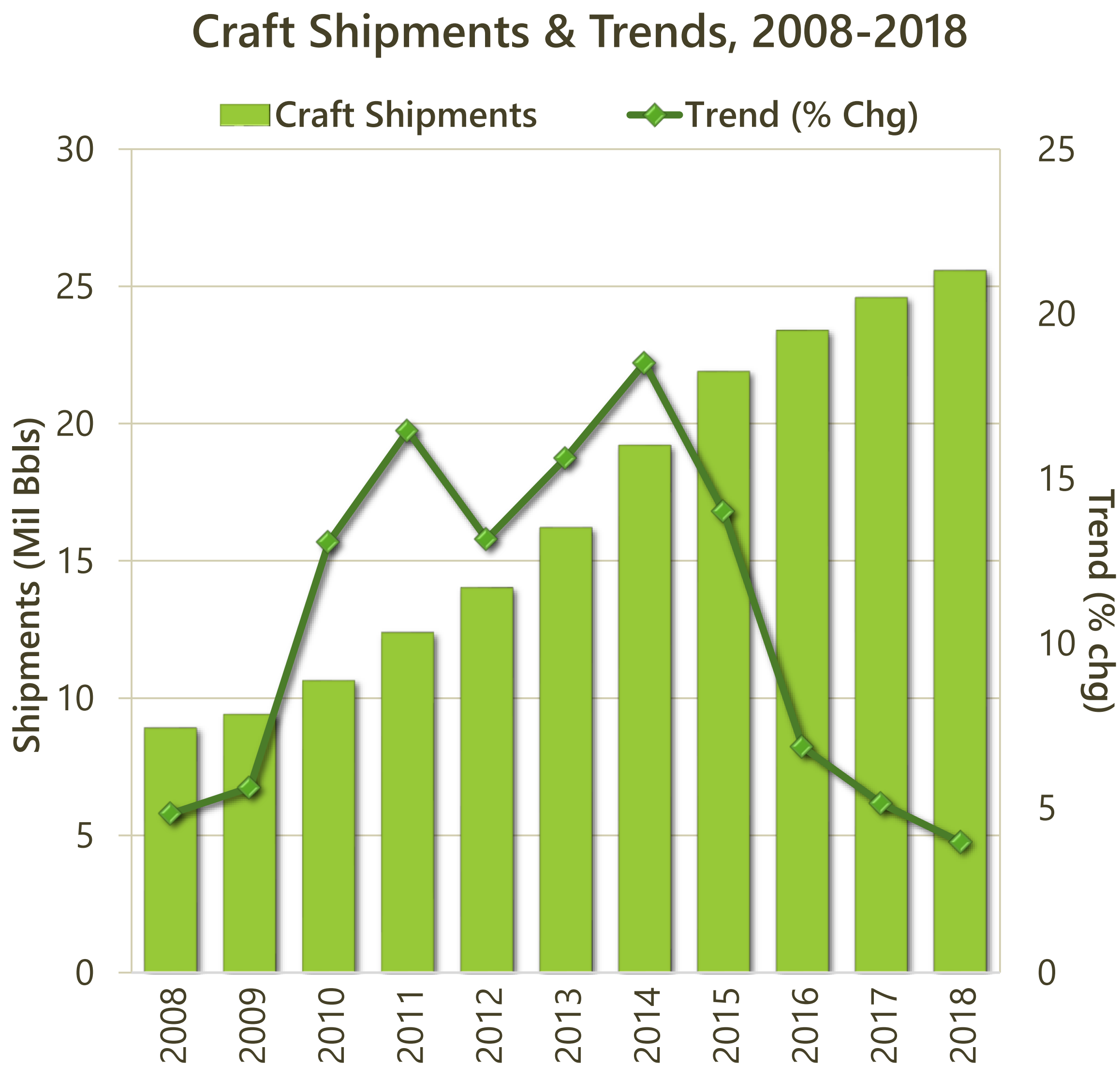
Premiumization in US beer biz tracks back to early 1990s:

In 1990, all above-premium segments totaled less than 20 million barrels, just over 10 share of US beer volume.

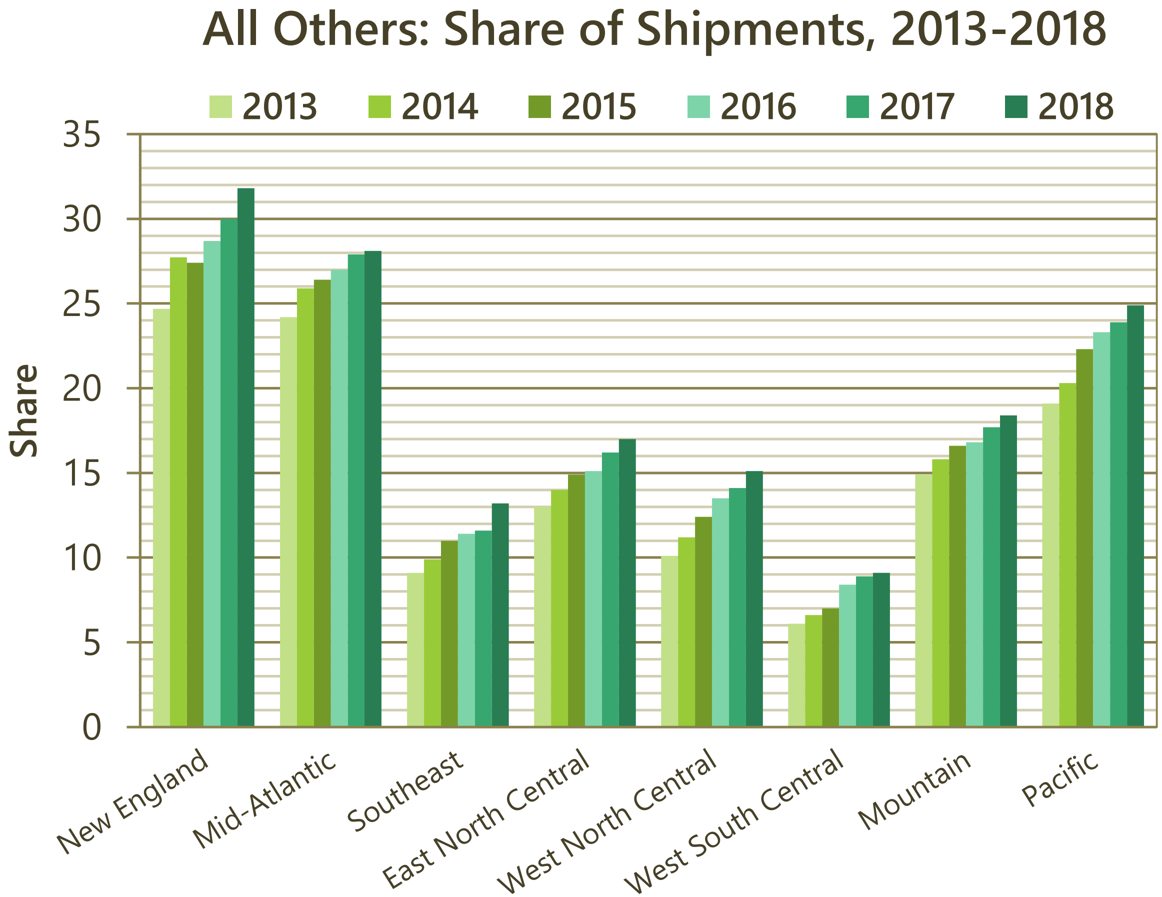
In 2018, the high end of the beer industry topped 43 share and neared 90 million barrels, larger than the premium segment.



Craft contributed to that shift, drove high-end growth since 2008:



- Craft volume nearly tripled in 10 years, +16.7 mil bbls 2008-2018
- In 2008, the average 21+ US adult consumed just over one 12oz serving of craft per month. Now it's closer to 3.
- Over 10 years, mainstream beer lost 40 million bbls, down by almost ¼.
- Craft growth slowed over last 3 years, gained just under 1 million bbls in 2018, +4%, we estimate.



Fragmentation:

"All Others" = all US brewers, importers & malt bev suppliers below the top-5 (AB, MC, Constellation, Heineken USA, Pabst)

All Others hit 19.8 share of US shipments in 2018, +0.9 share in 1 yr, +4.9 share in 5 yrs.

Small suppliers gained share in each of the last 5 yrs in all regions, save one.

Craft Consumption in Major Metro Markets

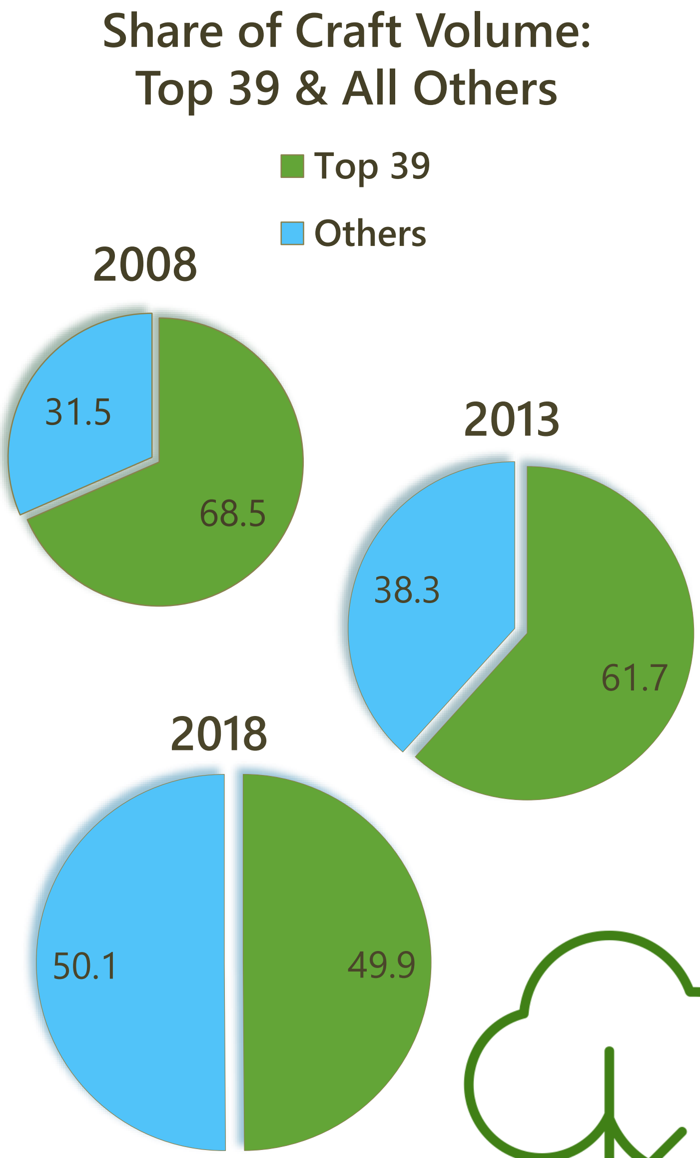
(% of 21+ adults who had "any" craft or microbrew in last 30 days)

	2012-2013	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	*5-Yr Chg*
SF	24.0	17.2	25.7	26.0	23.8	25.9	*1.9*
LA	14.3	14.1	12.1	16.0	13.7	14.0	*-0.3*
Top 10 US Metros	14.5	15.2	16.3	16.7	17	18.4	*3.9*

Source: Scarborough Research

Fragmentation reaches into craft too:

- In 2018, 39 US craft players shipped over 100K bbls, collectively shipping just over 13 million bbls.
  - Over half of them flat or down
  - Collectively down for 2nd yr
- Over 5,700 breweries opened in the US in the last 10 yrs and ¾ of those opened in the last 5 yrs.
- Larger craft brewers dominated the segment in 2008 with near 70 share. But brewers over 100K bbls lost 7 share between 2008 and 2013 and then slipped below 50 share for the 1st time last yr.
- Smaller brewers got all of craft growth in 2018, collectively doubled in 5 yrs and expanded by 4.5X, 10.3 mil bbls in 10 yrs.



To seltzer and beyond!

Flavor experimentation (epitomized by craft) fragments the beer biz further.

Seltzer = 2 mil bbls in 2018
Mike's (White Claw) + Boston (Truly) = 75-80 share

Both co's expect seltzer to double+ in 2019 (tripling so far). If they hold share, that's still 400-500K bbls up for grabs. Many craft brewers see this oppy.

What's next? AB throwing lots at the wall; entrepreneurs from non-alc goin' hard; from kombucha and lighter teas to coconut water. Oh, right: cannabis bevs too.

Consumers "not running to seltzer…running from sugar."
-Ben Weiss (Crook & Marker)

They're runnin' alright…

"...an object in motion..."

FMBs tend to be more developed in markets where craft is *also* more developed.

Last yr, FMBs (driven by seltzers) gained the most in mkts with above-average craft share high craft share.

Volume Trends in 11 Markets, Calendar 2018 (IRI)				
	Craft	Super-premium	FMB	Craft Share
Portland, OR*	-2.3%	10.1%	18.1%	30.5
Seattle/Tacoma, WA*	-2.5%	15.6%	25.8%	27.6
San Fran/Oakland, CA	-4.2%	4.2%	3.3%	19.2
San Diego, CA	1.7%	11.0%	12.0%	17.2
Chicago, IL	-3.2%	26.1%	18.2%	10.2
Ohio	1.3%	19.6%	16.4%	8.1
Los Angeles, CA	1.8%	16.9%	9.0%	7.5
North Carolina	7.3%	15.5%	12.4%	7.1
Houston, TX	-4.2%	20.1%	8.1%	6.1
Dallas/Ft. Worth, TX	-1.3%	14.3%	7.0%	5.8
Florida	1.0%	9.4%	11.9%	4.9

IRI Multi-outlet + convenience; except Portland, Seattle, no convenience

This yr, craft distribution (TDPs) is down low single-digits in Nielsen all outlet off-premise data, as FMBs and superpremiums get more space and attention.

Beer was "at rest" til craft took off, and now look, a wise man told us last summer.

From a consumer perspective, they started moving and continue to.

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(or craft brewer)

1 | "…an object in motion stays in motion…"

2 | FORCE = MASS x ACCELERATION

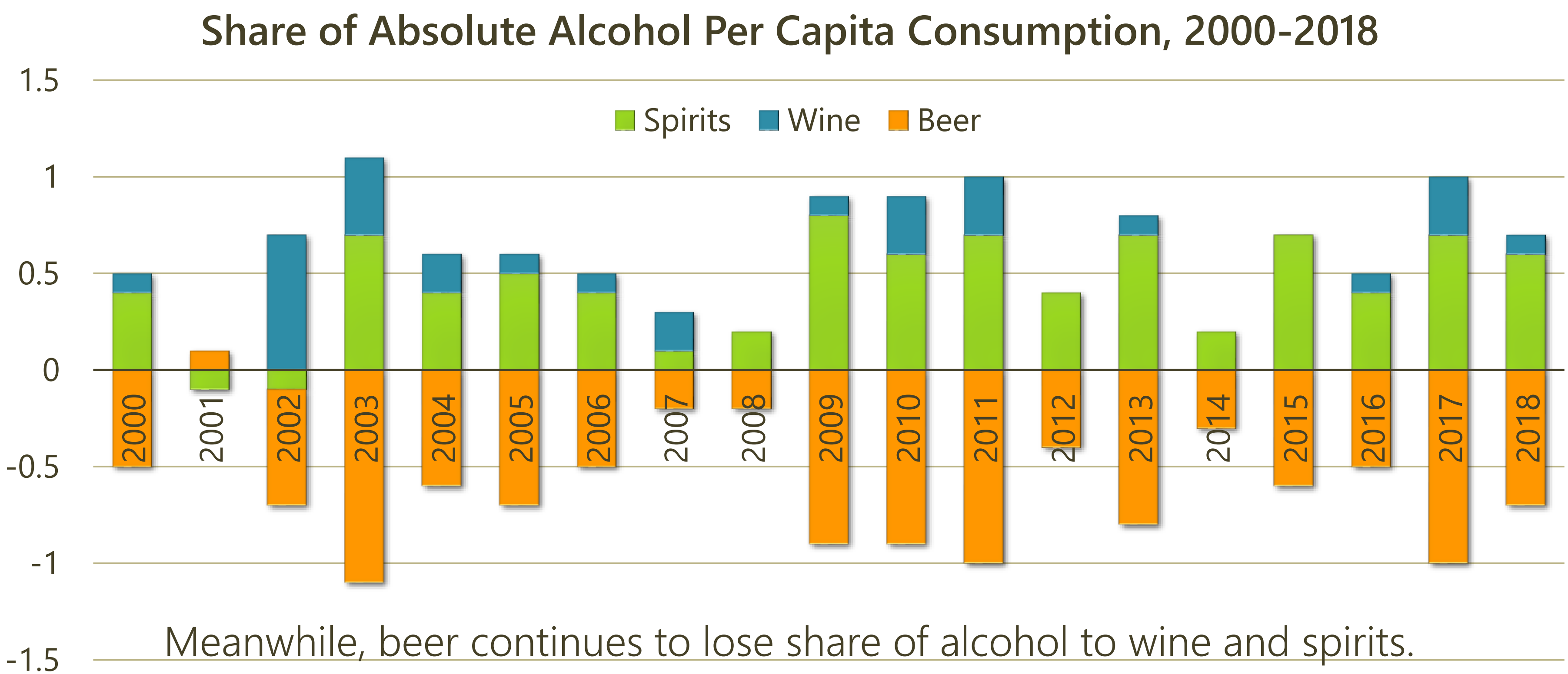
Big things need strong forces to move…

Absolute alcohol consumption per capita barely budges

On average, about 2/3 of American adults say they drink. On a total 21+ population basis, per capita consumption has been flattish for decades.

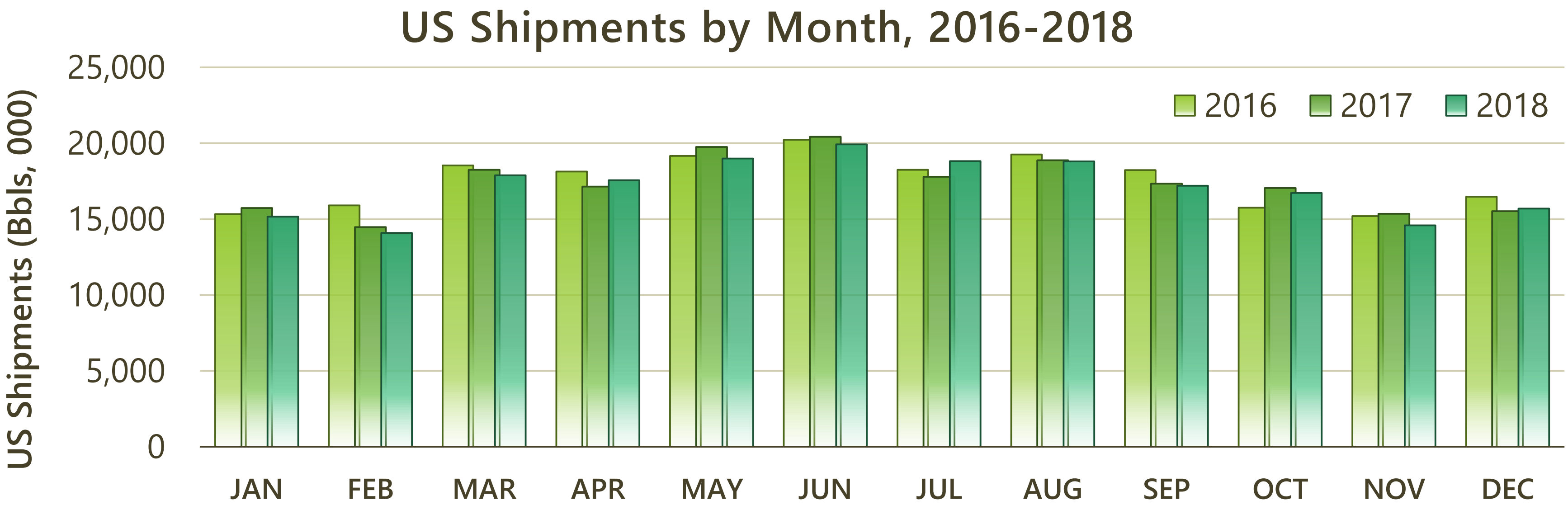
Concerns about Generation Z walking away from alcohol may be overblown: tho underage drinking is way down, drinking rates still rising to standard levels once 21. Are more folks moderating?

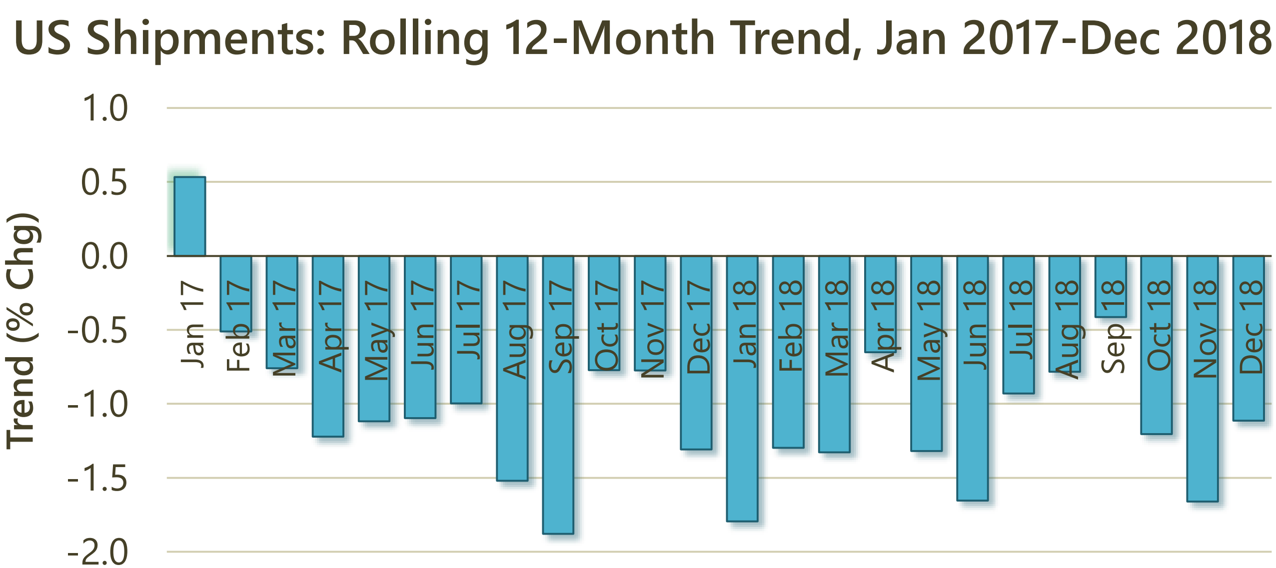
Will cannabis eventually move this needle in a meaningful way?



Meanwhile, beer continues to lose share of alcohol to wine and spirits.

Total US beer volumes remain soft:





Domestic Taxpaids

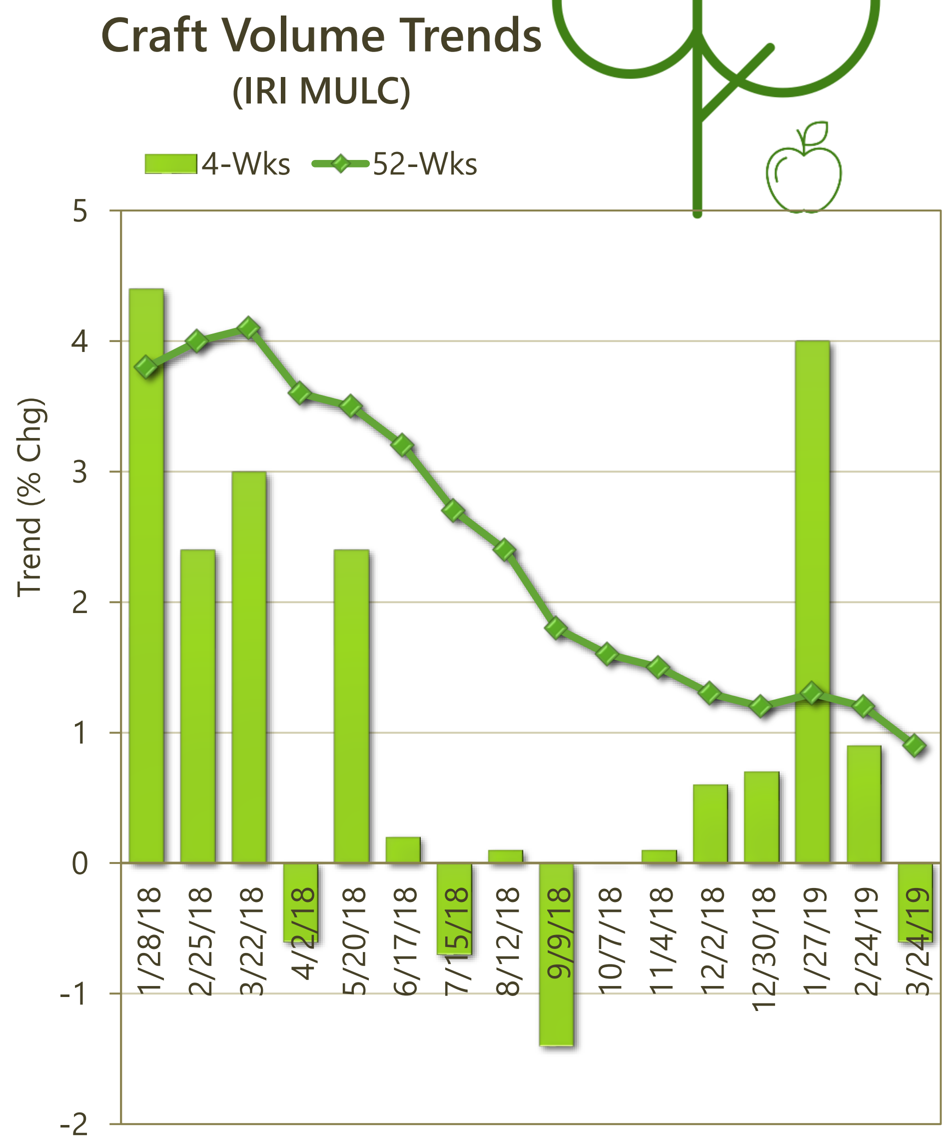
Jan: +1.2%
Feb: +0.4%
Mar: -2.0%
Q1: -0.5%

Imports much softer:
-7% Jan-Feb

Known shipments:
-567K bbls

Craft, too, has slowed considerably:

- Craft's absolute bbl gains have diminished considerably over the last few years:
  - 2013: +2,190,000 bbls
  - 2014: +3,000,000 bbls
  - 2015: +2,690,000 bbls
  - 2016: +1,500,000 bbls
  - 2017: +1,200,000 bbls
  - 2018: +975,000 bbls
- Smaller growth is split more ways: a million bbls split 7,500 ways is just 133 bbls per brewer.
- Much of that growth is going thru on-site sales in brewery taprooms, as craft is barely growing in tracked off-premise channels.



As in beer, so in craft as largest players largely sluggish:

Top Craft Players	Bbls (000)	Trend (%Chg)
Boston Beer (beer)*	1,800	-7.7
Sierra Nevada	1,070	+1.2
Lagunitas*	1,025	+4.6
New Belgium	850	-11.0
Craft Brew Alliance	719	-1.6
Founders	563	+20.6
Goose Island*	540	-6.9
Spoetzl (Shiner)	526	-1.3
Bell's	478	+2.8
Firestone Walker	454	+12.1
Stone	400	+3.1
Deschutes	314	-7.4
Brooklyn	282	-3.8
Dogfish Head	275	0.0
Ballast Point	275	-12.9

*BMI estimate

Select Craft Portfolios

Anheuser Busch*

Total Acquired: <1.5 mil bbls, +10%

Goose Island	-7%
Elysian	+34%
Golden Road	+74%
Karbach	+28%
10 Barrel	+13%

Shock Top: 425K bbls, -19%

MillerCoors

Total Acquired: 265K bbls, +17%

Blue Moon: 2.055 mil bbls, -3.1%

Leinenkugel: 805K bbls, -15%

CANarchy 421K bbls +23%*

(+Deep Ellum, Three Weavers)

ABV 311K bbls +23%*

(+Sixpoint)

As the largest state by far, California drives national trends:

Since 2013:
Total shipments in CA flattish

AB lost 7 share, MC lost 5 share, STZ gained 9

"All Others" +1.2 mil bbls in 5 yrs, but -0.3% last yr

In-State California Brewers: Preliminary 2018 Totals by Production

	Count**	Production	In-State	% In-State	Share of In-State
>100K Bbls	5	2,442,929	1,334,357	54.6	46.0
50K-100K Bbls	7	482,538	311,969	64.7	10.8
20K-50K Bbls	15	501,856	441,140	87.9	15.2
10K-20K Bbls	14	181,657	164,255	90.4	5.7
5K-10K Bbls	19	132,194	129,760	98.2	4.5
2K-5K Bbls	57	191,822	184,836	96.4	6.4
1K-2K Bbls	63	89,491	88,048	98.4	3.0
500-1K Bbls	78	56,761	56,651	99.8	2.0
100-500 Bbls	125	31,417	31,399	99.9	1.1
0-100 Bbls	160	4,425	4,425	100.0	0.2
Known Subtotal*	**543**	**4,115,090**	**2,746,840**	**66.8**	
*In-State Craft**			*2,950,000*	*+1-2%*	

**Subtotal only includes monthly and quarterly filers; Annual filers estimated for in-state totals*
***Count may be slightly inflated, not all companies with multiple licenses consolidated*
Source: CA Board of Equalization

Top Craft Suppliers & Brands in Top CA Markets (Volume, IRI MULC, Calendar 2018)

SAN DIEGO			LOS ANGELES			SAN FRANCISCO		
Supplier	Trend	Craft Share	Supplier	Trend	Craft Share	Supplier	Trend	Craft Share
Stone	12.1	12.9	AB Craft	14.7	13.9	Lagunitas	-3.7	20.1
Constellation Craft	-9.5	10.7	Firestone Walker	11.8	13.6	Sierra Nevada	-5.0	17.3
Lagunitas	-4.6	9.3	MC Craft	-3.9	13.6	MC Craft	-10.2	8.7
MC Craft	-5.2	8.0	Lagunitas	2.1	12.3	Firestone Walker	17.8	6.8
Sierra Nevada	-5.4	8.0	Stone	10.2	7.7	AB Craft	4.8	5.0
AB Craft	9.2	6.8	Sierra Nevada	-8.7	7.7	Craft Brew Alliance	-18.7	4.7
Craft Brew Alliance	-14.0	5.5	Craft Brew Alliance	-13.4	6.6	21st Amendment	18.9	4.4
Firestone Walker	19.8	5.0	New Belgium	0.6	4.5	Anchor	-20.2	3.4
New Belgium	-10.1	3.3	Constellation Craft	6.0	4.4	Bear Republic	-15.8	3.3
Port	32.2	2.8	Sam Adams	-16.3	4.2	New Belgium	-13.8	3.0
Top-10	**-0.4**	**72.2**	**Top-10**	**1.5**	**88.5**	**Top-10**	**-4.7**	**76.8**
All Other	**7.6**	**27.8**	**All Others**	**4.0**	**11.5**	**All Others**	**-2.5**	**23.2**
Craft	**1.7**		**Craft**	**1.8**		**Craft**	**-4.2**	
Total Beer	**-1.0**		**Total Beer**	**0.5**		**Total Beer**	**-2.8**	

Brand	Trend	Craft Share	Brand	Trend	Craft Share	Brand	Trend	Craft Share
Lagunitas IPA	-13.4	5.1	Firestone 805	12.0	11.9	Lagunitas IPA	-12.2	9.3
Firestone 805	22.4	4.0	Blue Moon Belg White	-10.5	8.7	Sierra Nevada Pale Ale	-13.4	8.0
Blue Moon Belg White	-8.7	3.8	Lagunitas IPA	-9.4	7.3	Blue Moon Belg White	-11.6	6.3
Stone IPA	-10.2	3.7	Shock Top Belg White	-11.1	4.5	Firestone 805 Blonde	21.4	5.9
Sierra Nevada Pale Ale	-6.9	3.6	Sierra Nevada Pale Ale	-9.4	3.8	Lagunitas Little Sumpin	-10.6	3.2
Stone Delicious IPA	40.0	3.5	Stone IPA	-9.0	2.4	Bear Republic Racer 5	-14.2	3.0
Ballast Point Sculpin	-9.0	2.9	Lagunitas Little Sumpin	9.9	1.8	Sierra Nevada Torpedo	-17.3	2.7
Shock Top Belg White	-7.2	2.5	Elysian Space Dust IPA	92.0	1.7	Sierra Nevada Seasonal	-1.7	2.1
Sierra Torpedo IPA	-15.2	2.0	Golden Road Wolf Pup	60.3	1.7	Shock Top Belg White	-13.3	1.9
Ballast Grapefrt Sculpin	-2.6	1.6	Kona Big Wave Golden	5.8	1.7	Anchor Steam Beer	-16.2	1.8
Top-10	**-3.0**	**32.8**	**Top-10**	**0.1**	**45.5**	**Top-10**	**-9.1**	**44.2**
All Other	**4.2**	**67.2**	**All Others**	**3.3**	**54.5**	**All Others**	**0.1**	**55.8**

**Constellation Craft is Ballast Point; AB Craft is mostly Shock Top, Golden Road, 10 Barrel, Elysian; MC Craft is mostly Blue Moon, Saint Archer, Hop Valley; Craft Brew Alliance is mostly Kona, Widmer, Redhook*

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1 | "…an object in motion stays in motion…"

2 | FORCE = MASS x ACCELERATION

3 | For every action,
an equal and opposite reaction

Push & pull, zig & zag

Style trends in craft often zig & zag as brewers react:

17 of top-25 new craft brands in off-premise scans are IPAs; among others, most are lagers

Lager

IPA

Mainstream Beer

Hazy

Brut

IPA still dominates growth in off premise scans, 40 share of craft $$ and counting, +14%

Innovation a major contributor

Non-Beer Bevs

Golden Ales +12%
Other Pale Lagers +13%
Pilsner +4%
Craft "Light" +10%
(IRI MULC, YTD to 3/24)

Two opposing ways to find new craft drinkers:
exploring experimental niches/crossover bevs
& craft takes on mainstream beer styles

Legislative push & pull, reactions & responses:

Growth of taprooms → retailer & distributor pushback

Traditional resistance to small brewer license privileges from 3-tier advocates still ramps up in some places as compromise prevails elsewhere:

- NC: yrs of discord → messy lawsuit → 2019 compromise
- MD: Guinness-driven carve out → raised cap with controversial "buyback" provision → taproom cap raised, no buybacks
- CT: attempt to raise off-premise limits → pushback/gov't support → discussions, working toward compromise
- TX: 2015 compromise, no to-go sales at production breweries → lawsuit → brewers/1 distrib org compromise, but other distrib org opposed → committee hearings blocked → amendment passed…

Some believe this is "just the beginning" of taproom pushback from the retail tier.

How far does it go? Where will it be successful? Can concerns be allayed?

Is franchise law reform back on the table?

Small brewer carve-outs to state franchise laws pass in a couple states and being considered in others:

- MD: quickly, unanimously passed carve out for brewers <20 bbls
- CT proposal dropped as part of off-premise sales negotiation
- Back again in MA; ME discussions; GA bill
- Why? A conflux of potential changes in 3 major participants:
    - Brewers: maturing organizations; clout?
    - Distributors: willingness, benefits to compromise?
    - Legislators: encouraging compromise? Changeover?

What will happen in California following Constellation's wholesaler consolidation (plus other middle-tier movement)?

Small distrib frustration → ← AB/Reyes biggest players

↑

CCBA

Narrative & logic; or this → that:

- Fragmentation → consolidation
- Consolidation → heightened competition
- Heightened competition + consumer "localism" → digging deeper at home
- Digging deeper at home → finding new audiences or, redefining what "growth" or "success" is

On the consumer side:

fragmentation → confusion → dependability?

(not in the data yet, but some consumers clearly here)

Slower beer growth → new avenues:

Cannabis investments can be seen in this context.

Do Newton's laws apply to this movement too?

1| cannabis deregulation has been a slow build; "inevitable" perhaps?

2| government/science move slowly, but state markets moving very rapidly (watch-out!)

3| CA's "gray" mkt → less than smooth rollout; lack of equity in adult use states → social justice issues at the fore in NY, NJ, local-focus in ME

So far, no clear, discernable impact on alcohol or beer sales in the available data. But we know these substances don't operate in vacuum: the interactions, the touchpoints are too varied to ID one clear read one way or another. So we wait…

Recap:

1| Momentum is powerful, but so is rest, stillness & stasis;
beneficiaries vary and momentum can shift

2| Big things need ever bigger actions just to keep moving

3| Constant give & take, push & pull:
acknowledging, accepting and working successfully inside of flux requires:

→ clarity → empathy

→ humility → curiosity

Thanks!

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