CRAFT SPIRITS DATA PROJECT

park street

American Craft Spirits Association

IWSR drinks market analysis

Annual Craft Spirits Economic Briefing

September 2018

Contents

Key Messages

Key Messages

- The number of active craft distillers* in the U.S. grew by 15.5% over the last year to 1,835 in August 2018.
- The U.S. craft spirits market volume (cases) reached nearly 7.2m cases in retail sales in 2017, growing at an annual growth rate of 23.7%. In value terms, the market reached $3.7 billion in sales, growing at an annual growth rate of 29.9%. The market share of U.S. craft spirits reached 3.2% in volume and 4.6% in value in 2017, up from 1.2% (volume)/1.4% (value) in 2012 and 2.6% (volume)/3.8% (value) in 2017.
- Exports of U.S. craft spirits reached 598,000 cases in 2017, adding more than 7.7% of additional volume to U.S. craft distillers' total sales. Exports grew by 5.7% versus last year.
- The U.S. craft distilling market is fairly concentrated with nearly 2% of the larger producers (between 100,000 and 750,000 proof gallons removed from bond) being responsible for 57.2% of the cases sold. 92.3% of U.S. craft producers are classified as small producers (between 0 and 10,000 proof gallons removed from bond). They are responsible for just 13.1% of the cases sold annually.

*Active craft distillers: licensed US distilled spirits producers, removed 750k proof gallons (or 394,317 9L cases) or less from bond, market themselves as craft, are not openly controlled by a large supplier, and have no proven violation of the ACSA Code of Ethics.

Key Messages (Continued)

- Direct sales at the site of the distilled spirits producer (DSP) are important for all craft distillers but especially important for small producers where these sales make up 40% of total sales. Out of state business is particularly important for large producers, accounting for 62% of the total business.
- Many surveyed retailers and wholesalers see the potential for craft spirits to perform in line or better than craft beer over time. With craft beer market share currently at 12.8% in the U.S., the craft spirits market is expected to continue to grow rapidly.
- Employment in the U.S. craft spirits industry has been on the rise: in 2017 industry employment grew by nearly 4,400 to over 18,300. In 2017 investment by the U.S. craft spirits industry increased by over $190 million reaching over $590 million in total.
- Surveys of craft distillers indicate investments in equipment and staff in the US craft spirits industry are accelerating in 2018 and are expected to continue to accelerate in 2019 due to the impact of the Craft Beverage Modernization and Tax Reform Act which became effective January 1st, 2018.

Craft Spirits Research Definition

Craft Defined for Purposes of the Research

Size:
Not more than 750,000 proof gallons (or 394,317 9L cases) removed from bond by licensed producer (DSP)

Self-proclamation of licensed craft distiller, not openly controlled by a larger supplier:
Distiller claims to be a U.S. craft spirits producer with a valid DSP license and is not openly controlled by a larger supplier

ACSA Code of Ethics:
"We operate in an honest, transparent and non-deceptive fashion. We inform consumers truthfully and accurately about the sources and methods used to make our spirits through our labels, materials and communications. We expect fair dealing and respect amongst members. We obey all federal, state, and local laws."

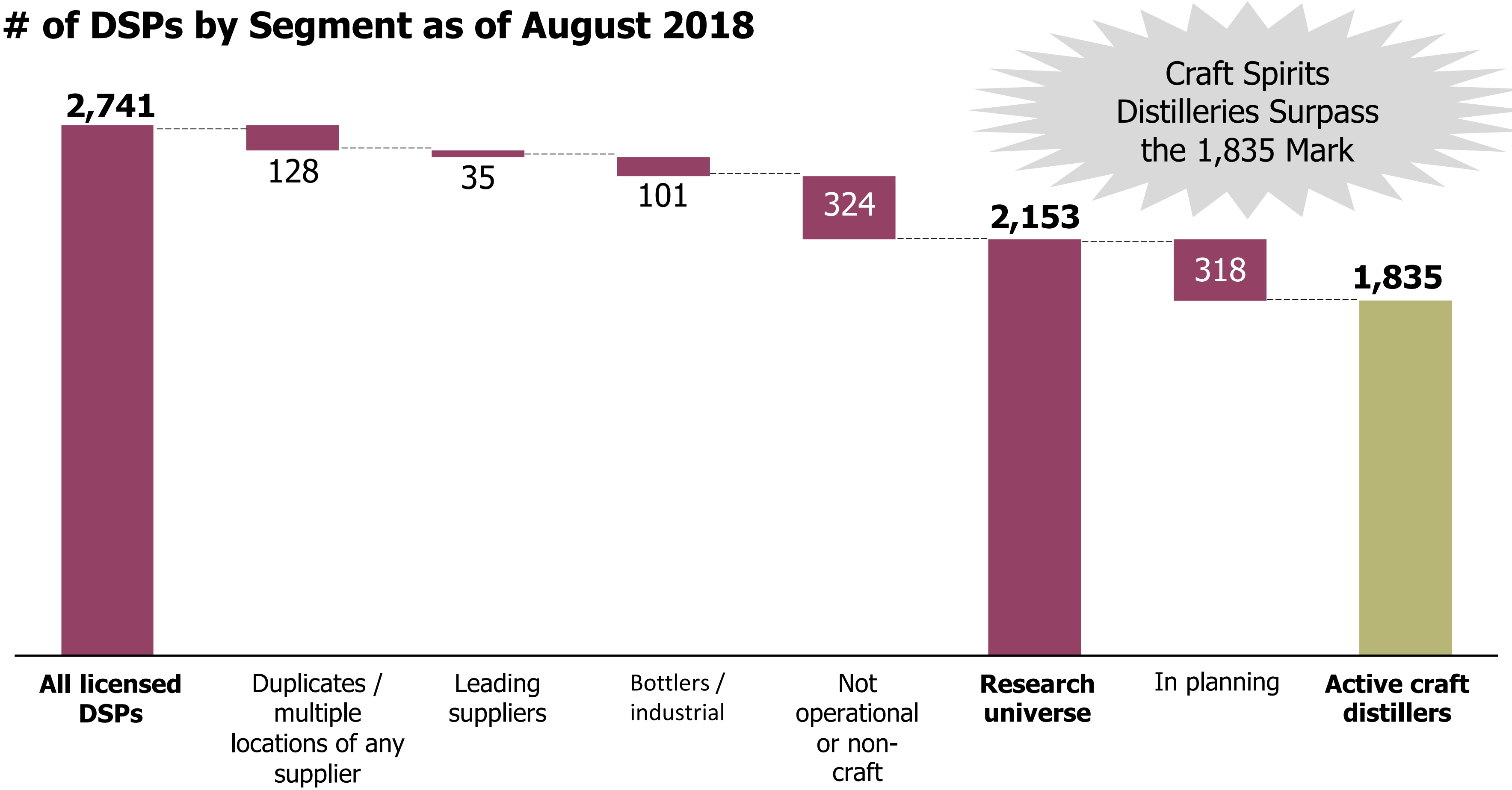
U.S. Craft spirits (for the purposes of this research)

U.S. Craft spirits are distilled spirits that are produced in the U.S. by licensed producers that have not more than 750,000 proof gallons (or 394,317 9L cases) removed from bond, market themselves as craft, are not openly controlled by a large supplier, and have no proven violation of the ACSA Code of Ethics

Craft Spirits Market Data

From DSPs to Active Craft Distillers

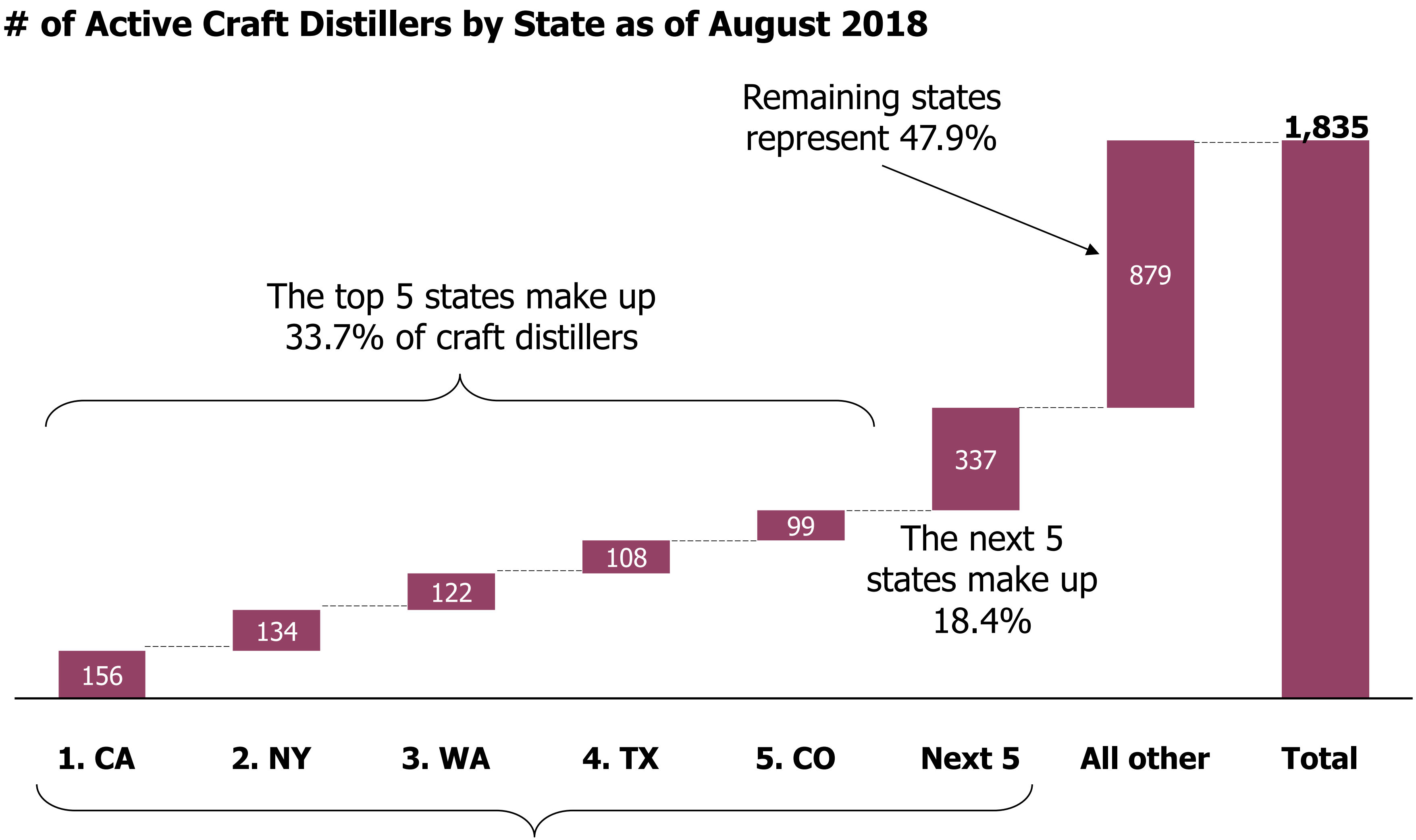
of DSPs by Segment as of August 2018



- The list of DSPs is broken down into segments in order to distinguish the amount of distillers that are not considered craft: duplicates, leading suppliers, bottlers, and/or non-craft/non-operational
- The list of active craft distillers is generated bottoms-up through individual assessment

Sources: TTB, ACSA, ADI, State ABC Boards, State Guilds, Team Analyses

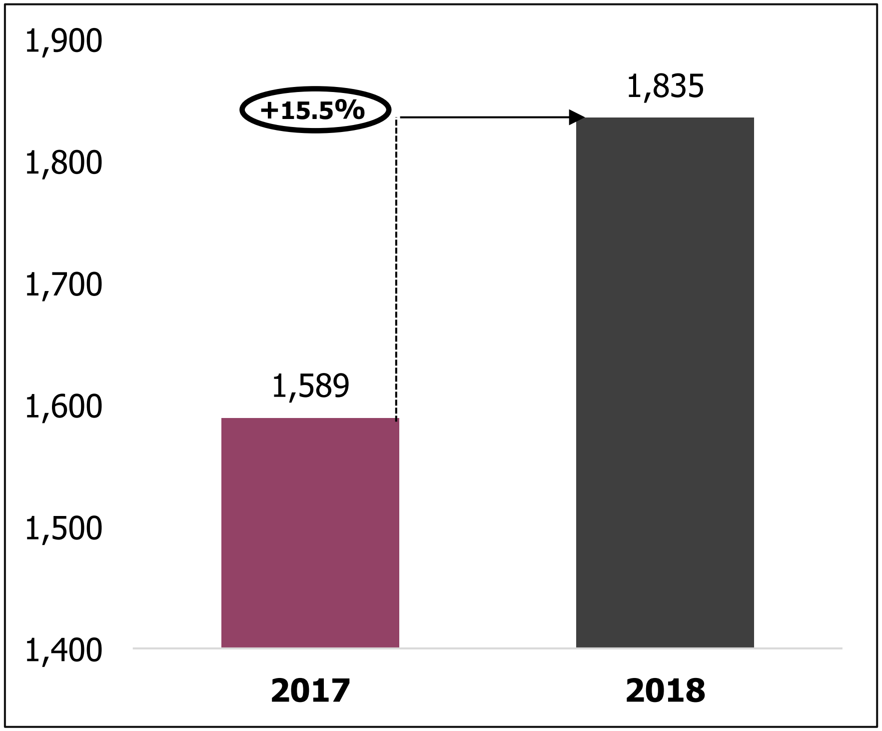
Active Craft Distillers by State

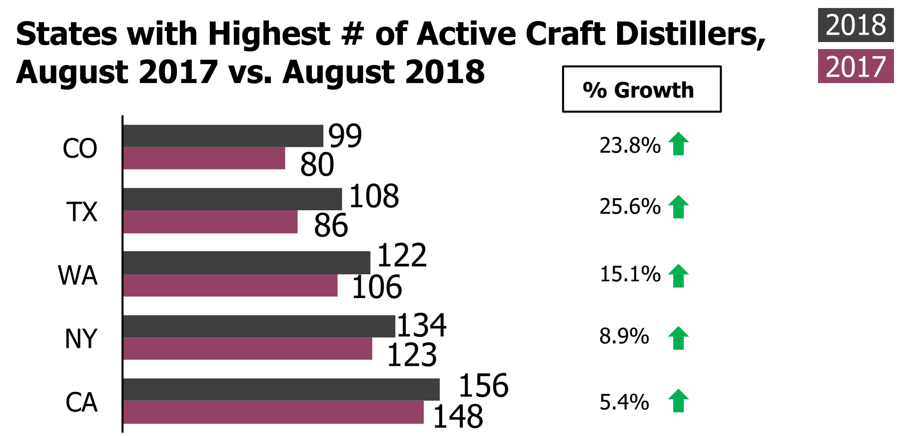


Over half of active U.S. craft distilleries are located in ten states

Number of Active Craft Distillers Has Grown Over 15% Since Last Year

of Active Craft Distillers, August 2017 vs. August 2018



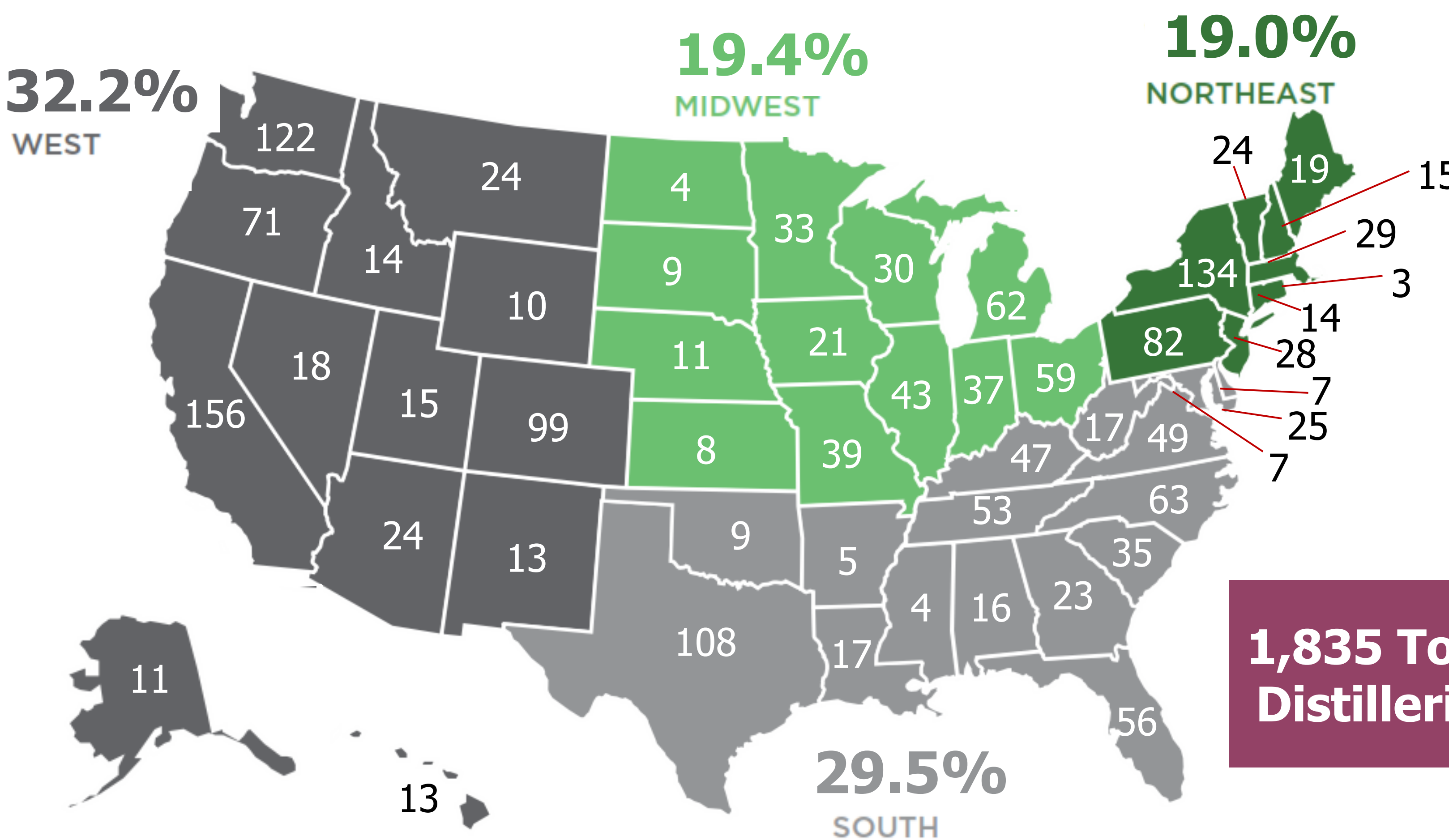


- In August 2018 there were 1,835 craft distillers active in the U.S., up over 15% from 1,589 active distillers in August 2017
- The number of craft distillers in RI, OK and WV grew by 45% collectively

Sources: IWSR, Team Analyses

Active Craft Distillers by State and Region

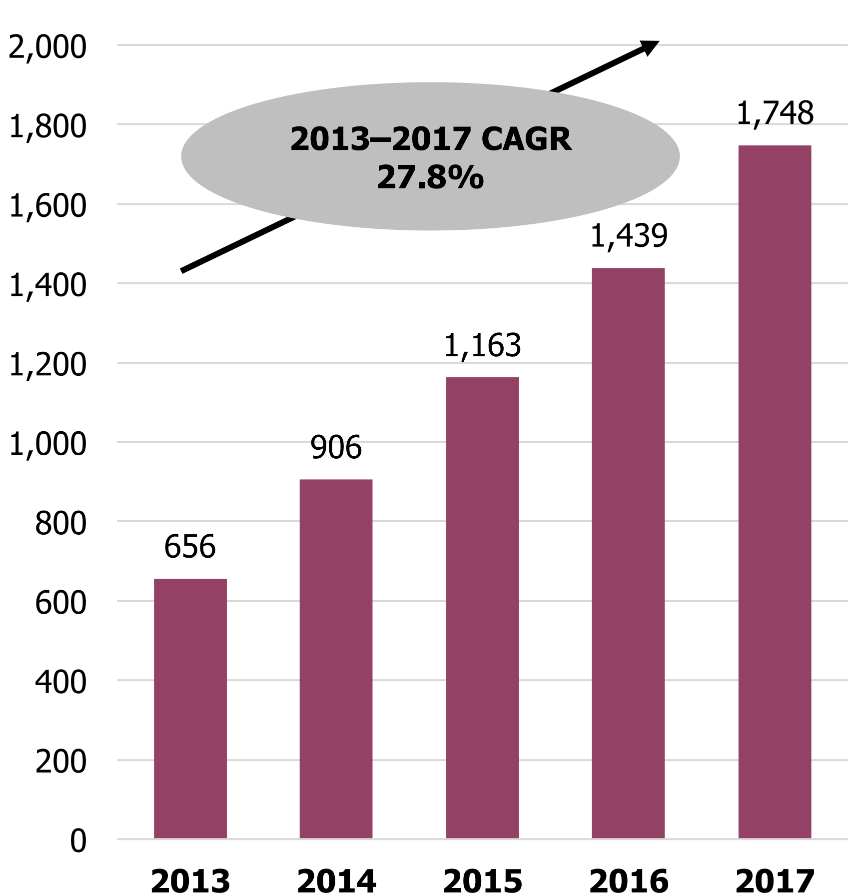
of Active Craft Distillers by State and Region as of August 2018



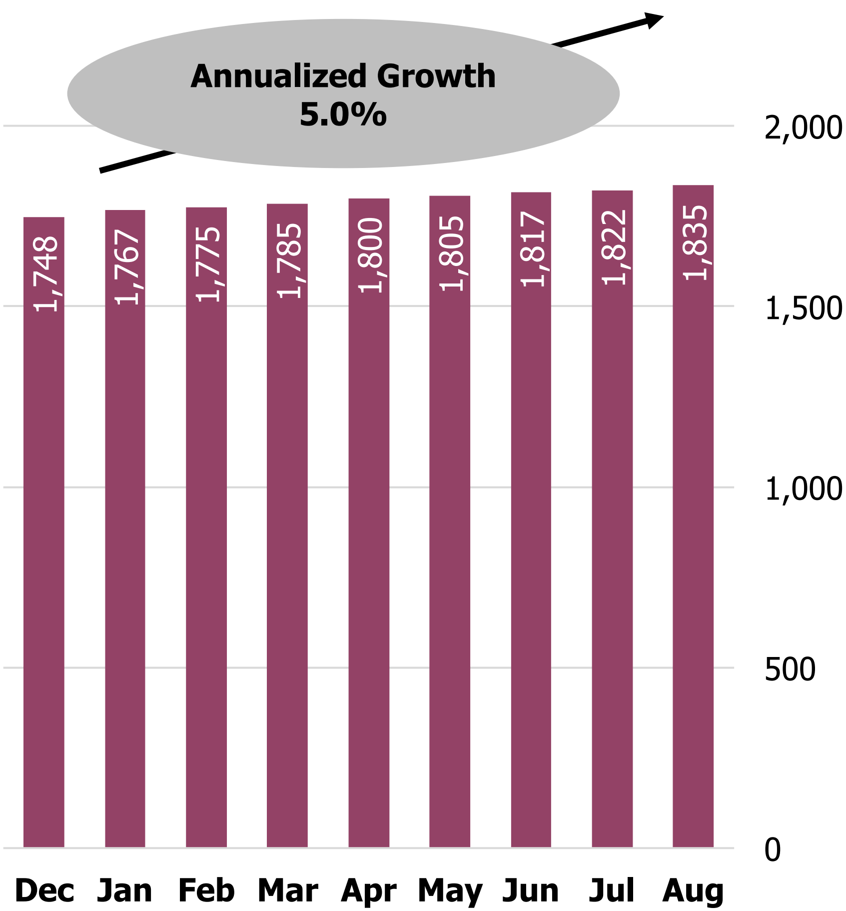
1,835 Total Distilleries

Number of Active Distillers Still Growing Rapidly

of Craft Spirits Producers 2013 – 2017

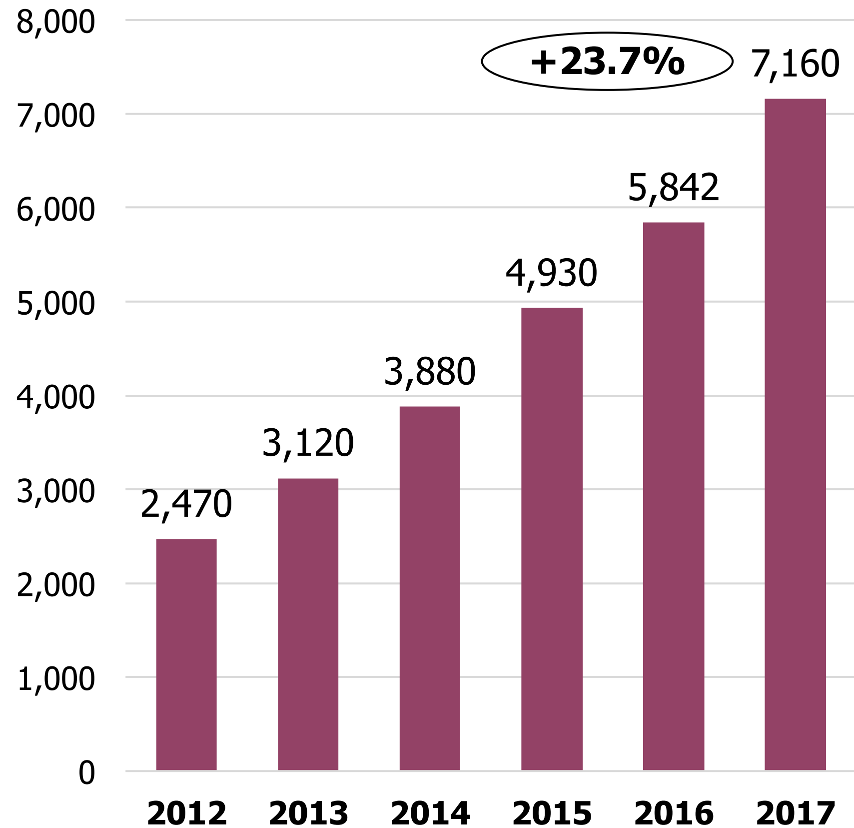


of Craft Spirits Producers December 2017 – August 2018

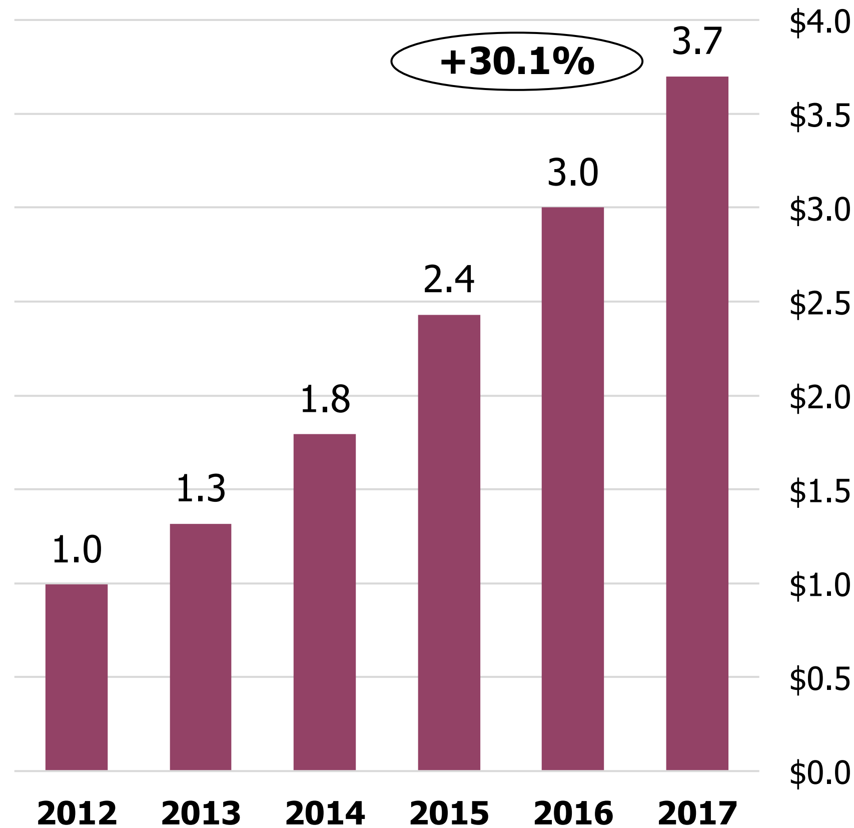


Craft Spirits Sales Are Growing Rapidly by Volume and Value

Craft Spirits Sales by Volume, 2012 – 2017
9L Cases (000)



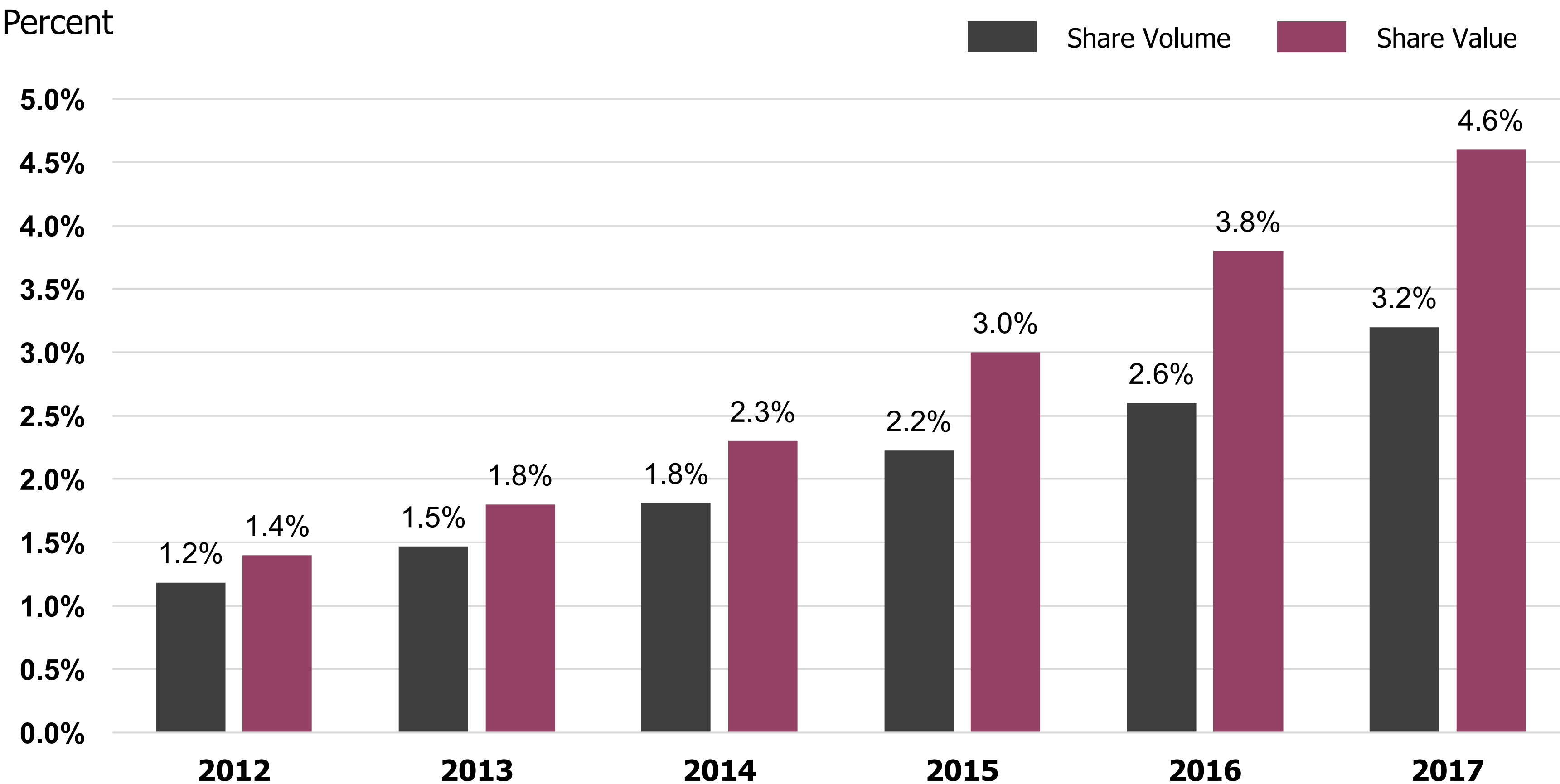
Craft Spirits Retail Sales by Value, 2012 – 2017
$ Billions



Sources: TTB, ACSA, IWSR, State ABC Boards, State Guilds, Team Analyses

Craft Spirits Market Share at 4.6% in Value and 3.2% in Volume

Craft Distiller Sales as a Share of Total U.S. Spirits Volume and Value



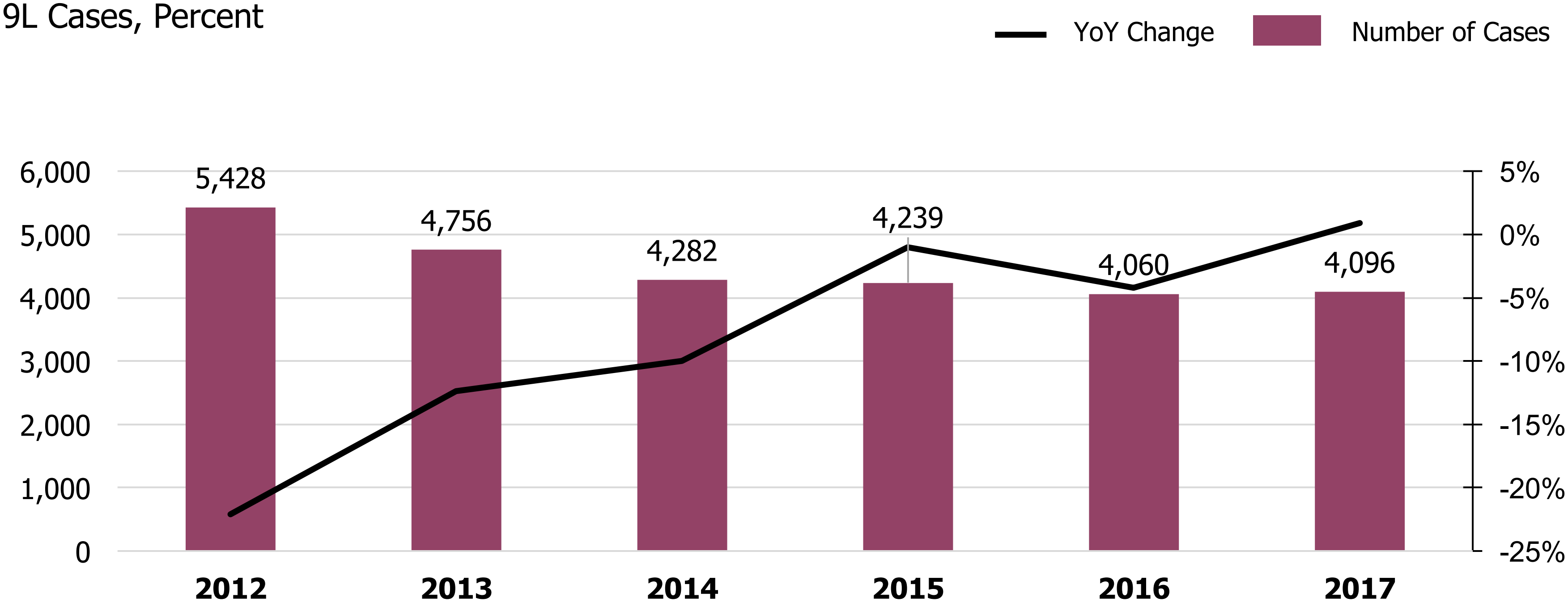
- U.S. craft currently has an estimated market share of 3.2% in cases, up from 1.2% in 2012
- U.S. craft is clearly a contributor to the trend towards premiumization in the U.S. market
- The U.S. craft market share in value is estimated at 4.6%, up from 1.4% in 2012

Sources: TTB, ACSA, IWSR, State ABC Boards, State Guilds, Team Analyses

Inflection Point Has Been Reached - Average Volume Has Started to Increase

of Cases of Average U.S. Craft Distiller 2012 – 2017

9L Cases, Percent

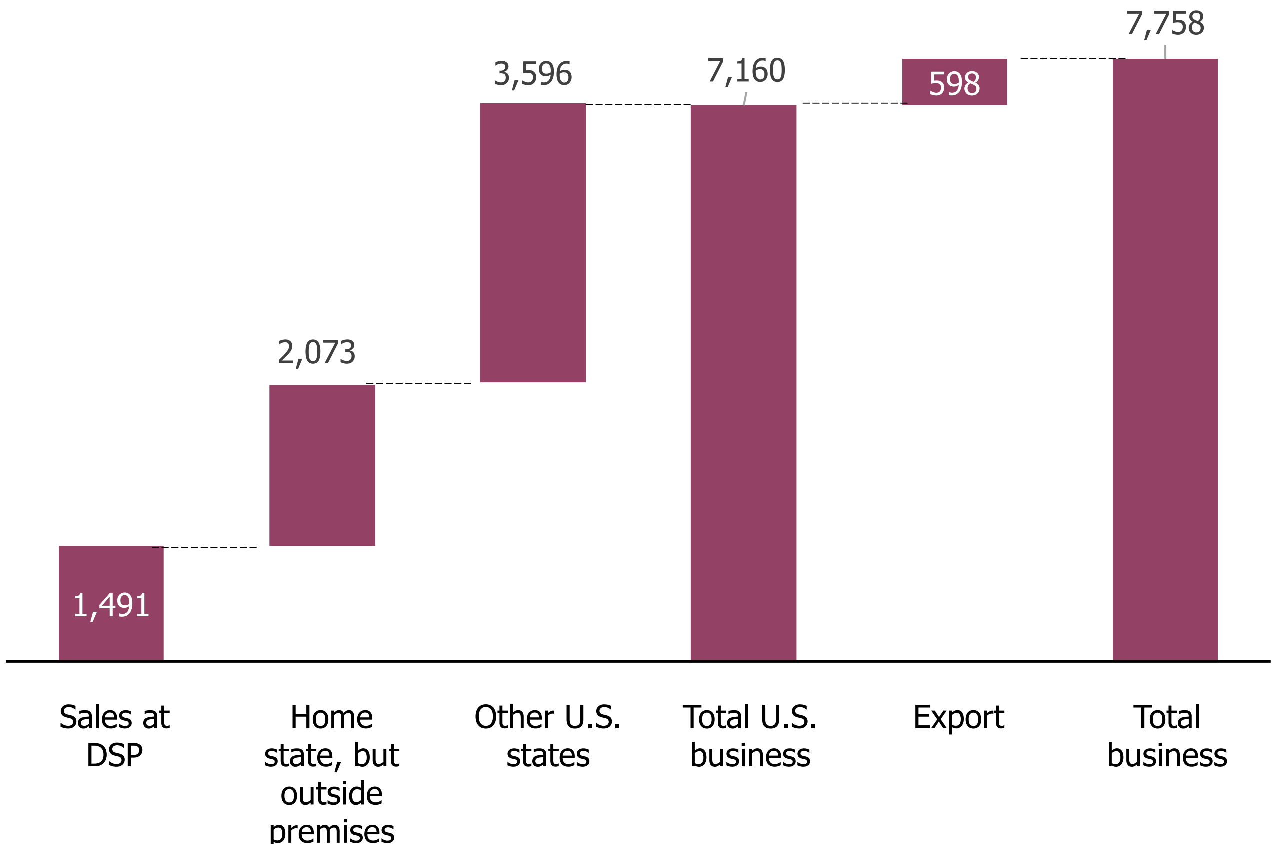


- The market has reached an inflection point at which the volume growth outpaces the growth in number of distillers.
- The volume of the average U.S. craft distiller reached 4,096 cases in 2017, up 0.9% versus 2016.

Nearly 50% of the U.S. Craft Business Takes Place in the Home States

Sources of Case Sales – Total U.S. Craft Spirits Industry, Domestic and Export 2017

9L Cases (000)



% of total U.S. business	Sales at DSP	Home state, but outside premises	Other U.S. states	Total U.S. business	Export	Total business
	20.8%	**29.0%**	**50.2%**	**100.0%**	**7.7%**	**107.7%**

- Nearly 50% of the total U.S. craft business takes place in the home state of the craft distiller
- Exports add nearly 8% to the overall volume of the U.S. business

Sources: TTB, ACSA, ADI, State ABC Boards, State Guilds, Team Analyses

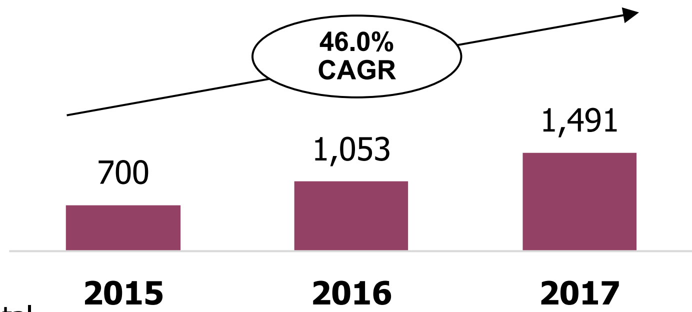
Most of the Growth for Total Craft Spirits has Occurred at the DSP and in Other States

CRAFT SPIRITS DATA PROJECT

Total Craft Spirits Industry, Sources of Case Sales, 2015 – 2017

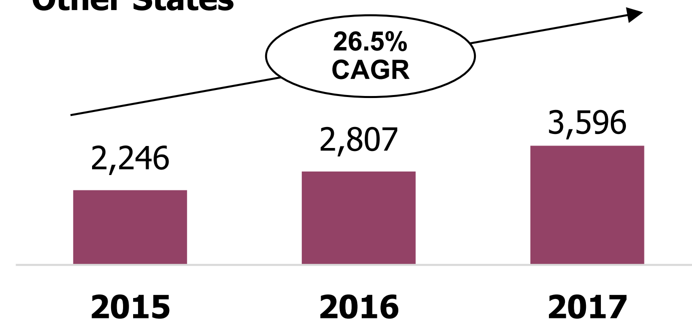
9L Cases (000)

Sales at DSP



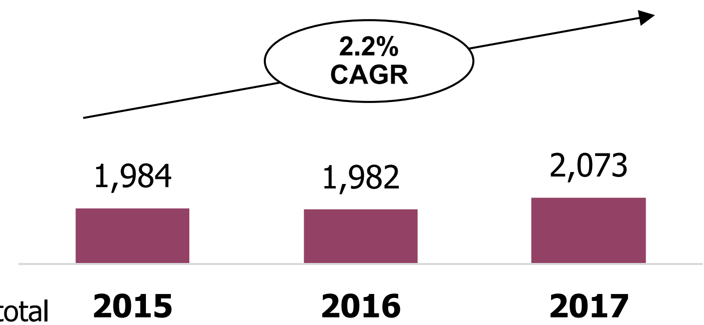
% of total U.S. business	14.0%	18.0%	20.8%	+6.8%

Other States



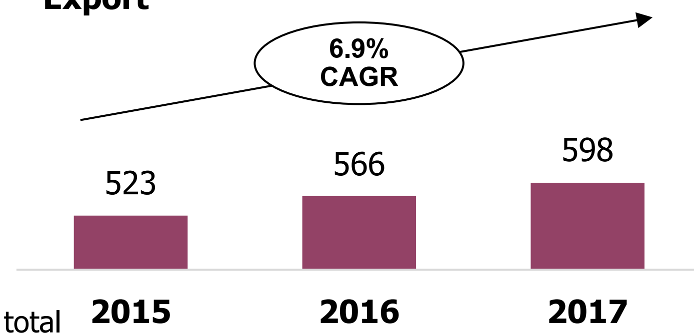
% of total U.S. business	46.0%	48.0%	50.2%	+4.2%

Home State



% of total U.S. business	40.0%	33.9%	29.0%	-11.0%

Export

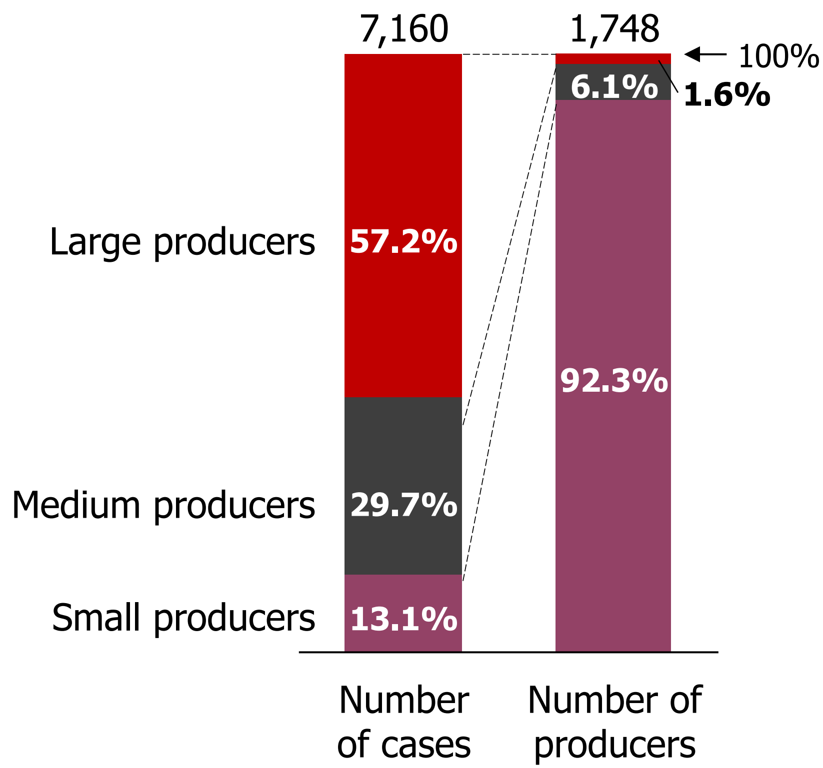


% of total U.S. business	11.0%	8.8%	7.7%	-3.3%

Craft Spirits Market Is Fairly Concentrated

of Craft Distillers and Case Volumes by Producer Size, 2017

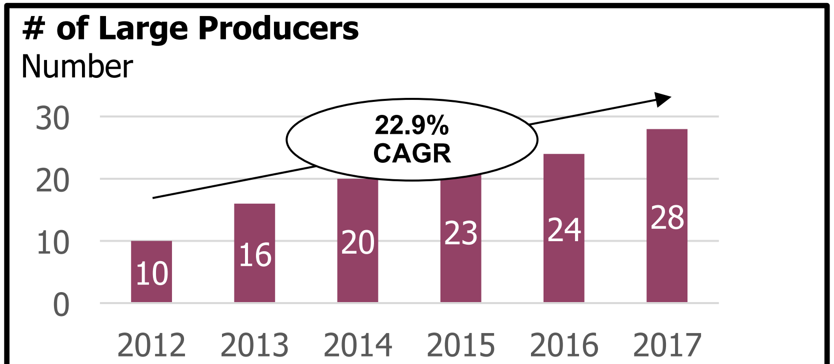
of Producers, 9L Cases (000)

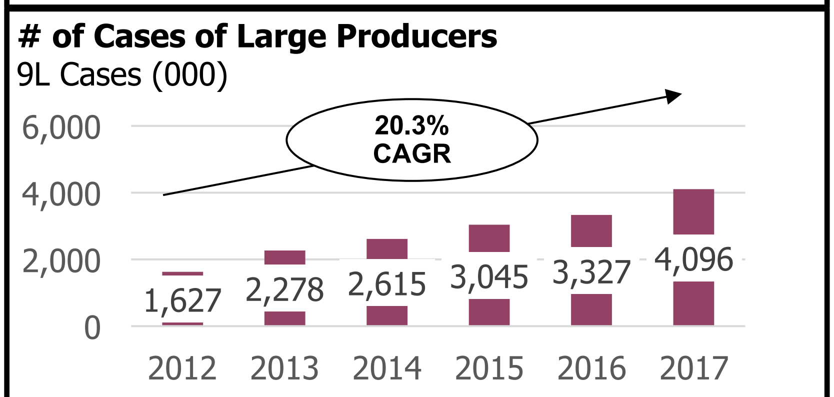


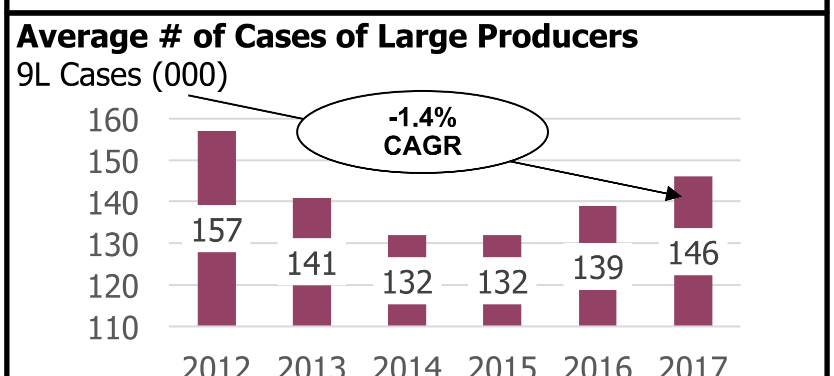
- The U.S. Craft distilling market is fairly concentrated with nearly 2% of the producers being responsible for almost 60% of the cases
- 92.3% producers are classified as small producers. They are responsible for just 13.1% of the cases

Sources: TTB, Distiller Surveys, Team Analyses *Small: 0 - 5,258 9L Cases, Medium: 5,258 - 52,576 9L Cases, Large: 52,576 - 394,317 9L Cases

Average Volume of Large Craft Producers Experienced Growth in 2017







- The number of large craft distillers as well as their number of cases has been growing rapidly
- The number of large craft distillers has grown almost three-fold from 10 in 2012 to 28 in 2017
- The number of cases of large craft distillers has grown from 1.6 million 9L cases in 2012 to over 4.0 million 9L cases in 2017
- The average number of cases of large craft distillers has decreased from 157k 9L cases in 2012 to 146k 9L cases in 2017

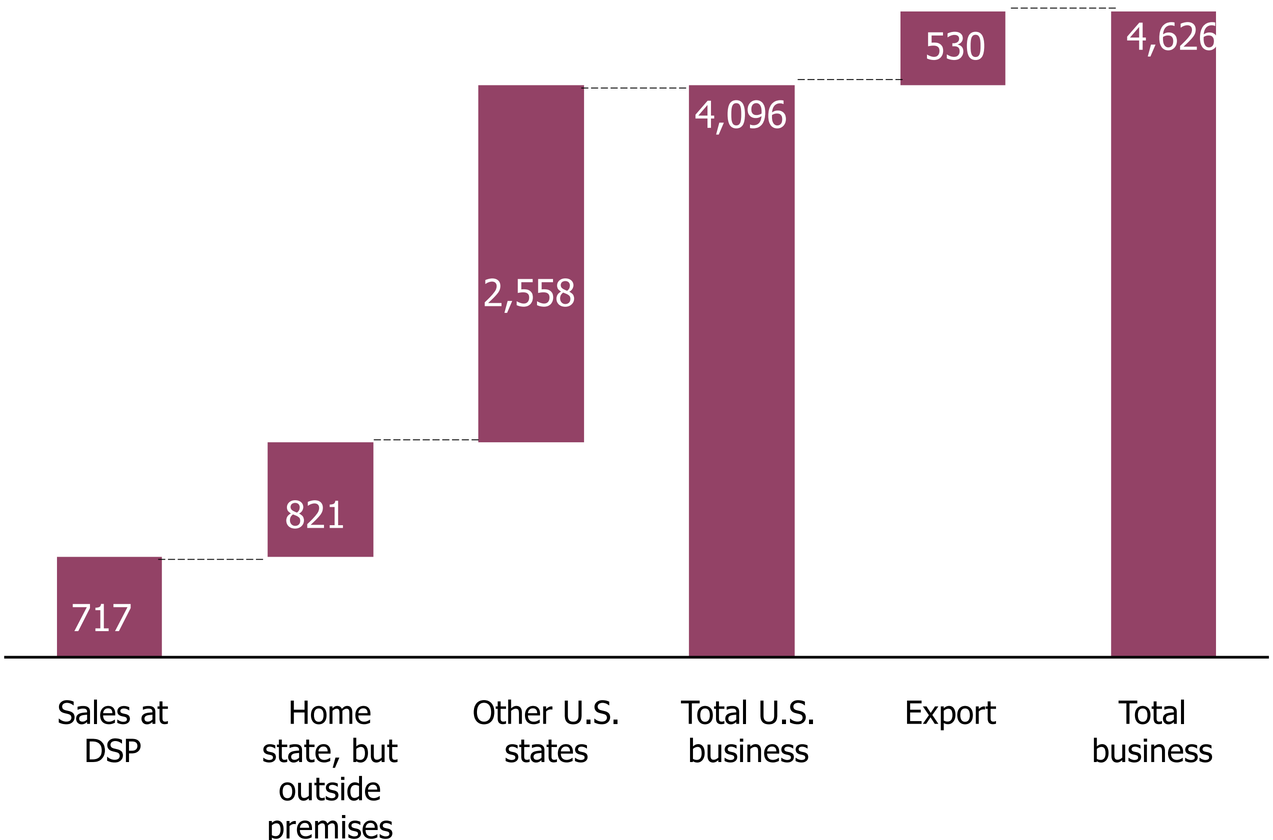
Sources: TTB, Distiller Surveys, Team Analyses

More Than 60% of the Business of Large Craft Producers Takes Place Outside the Home States

CRAFT SPIRITS DATA PROJECT

Sources of Case Sales – Large U.S. Craft Spirits Producers, Domestic and Export 2017

9L Cases (000)



% of total U.S. business	**18%**	**20%**	**62%**	**100%**	**11%**	**111%**

- More than 60% of the total U.S. business of the large U.S. craft producers takes place outside the home state of the craft distiller
- Exports add 11% to the overall volume of the U.S. business

Sources: TTB, ACSA, ADI, State ABC Boards, State Guilds, Team Analyses

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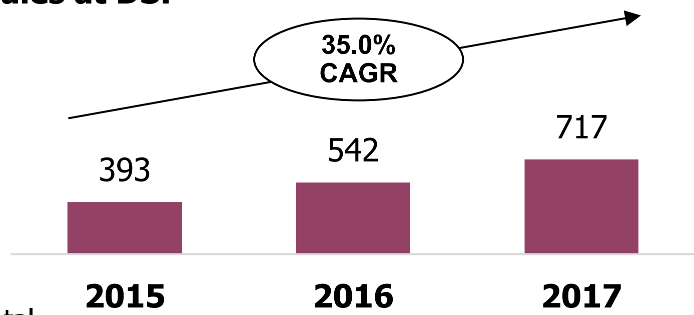
While Large Craft Producer Sales Are Growing, Home State Sales Continue to Decline

Large Craft Spirits Producers, Sources of Case Sales, 2015 - 2017

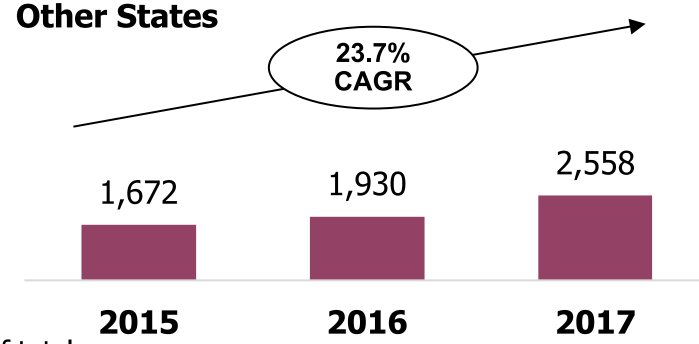
9L Cases (000)

Sales at DSP



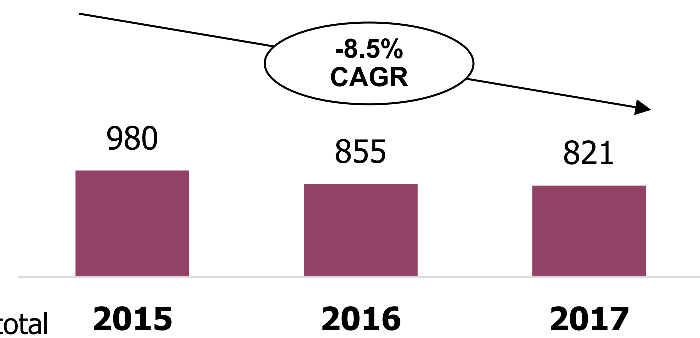
% of total U.S. business 13.0% 16.0% 17.5% **+4.5%**

Other States



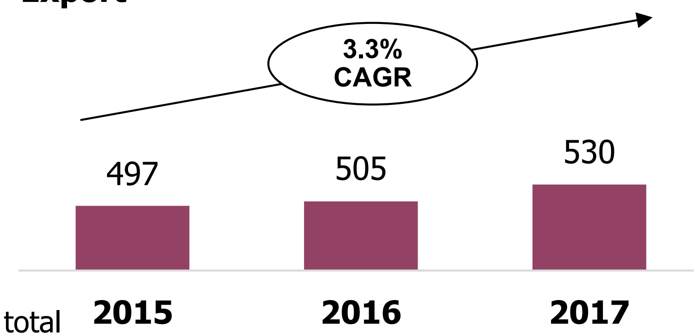
% of total U.S. business 55.0% 58.0% 62.5% **+7.5%**

Home State



% of total U.S. business 32.0% 26.0% 20.0% **-12.0%**

Export

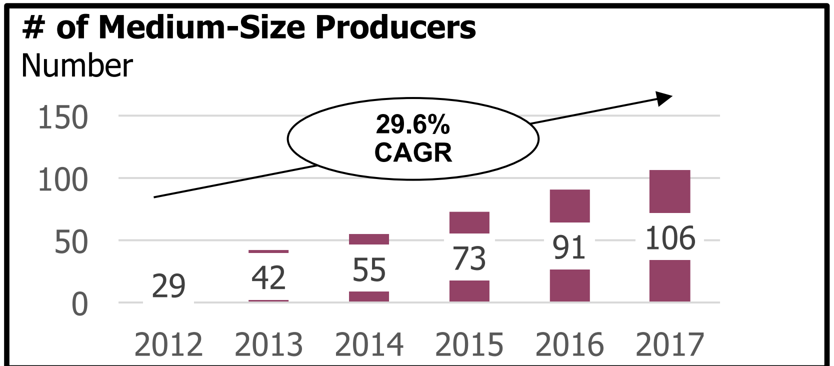


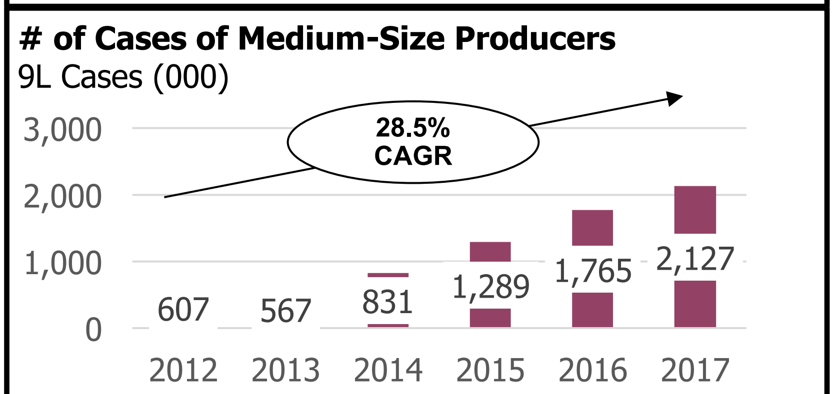
% of total U.S. business 16.0% 13.2% 11.5% **-4.5%**

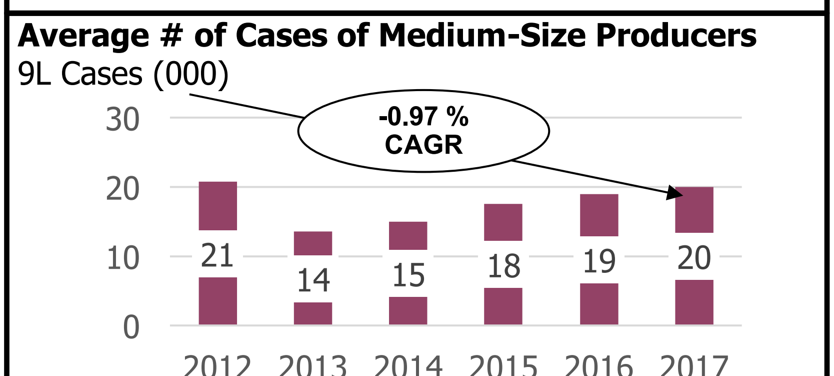
Sources: TTB, ACSA, ADI, State ABC Boards, State Guilds, Team Analyses

Medium-Size Craft Producers Have Been Growing Well

CRAFT SPIRITS DATA PROJECT







- The number of medium craft distillers as well as their number of cases has been growing rapidly
- The number of medium craft distillers has grown almost six-fold from 29 in 2012 to 106 in 2017
- The number of cases of medium craft distillers has grown from 607k 9L cases in 2012 to over 2.1 million 9L cases in 2017
- The average number of cases of medium craft distillers has decreased from 21k 9L cases in 2012 to 20k 9L cases in 2017
- Medium-sized craft producers have had positive average case growth year over year since 2013

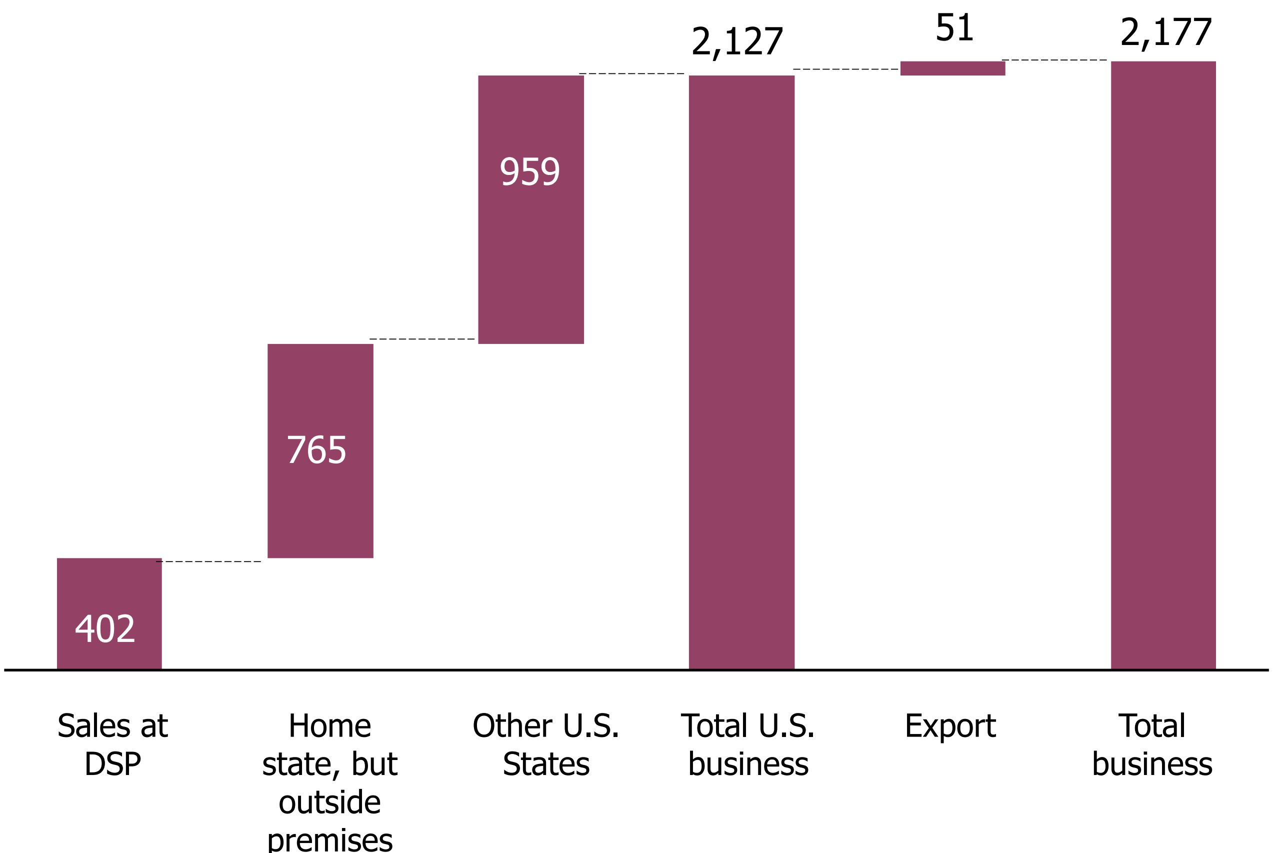
Sources: TTB, Distiller Surveys, Team Analyses

More Than 50% of the Business of Medium Craft Producers Takes Place in the Home States

CRAFT SPIRITS DATA PROJECT

Sources of Case Sales – Medium U.S. Craft Spirits Producers, Domestic and Export 2017

9L Cases (000)



% of total U.S. business	19%	36%	45%	100%	2%	102%

- 55% of the total U.S. business of the medium U.S. craft producers takes place in the home state of the craft distiller
- Exports add only about 2% to the overall volume of the U.S. business

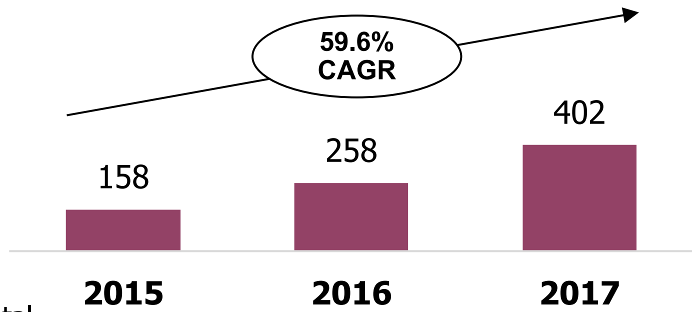
Sources: TTB, ACSA, ADI, State ABC Boards, State Guilds, Team Analyses

Medium Craft Producer Sales Have Grown Strongly Across All Sources

Medium Craft Spirits Producers, Sources of Case Sales, 2015 – 2017

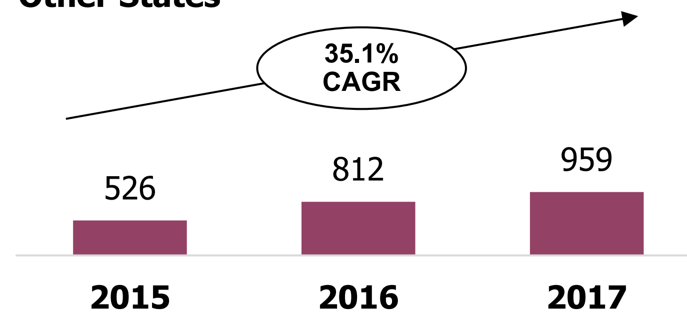
9L Cases (000)

Sales at DSP



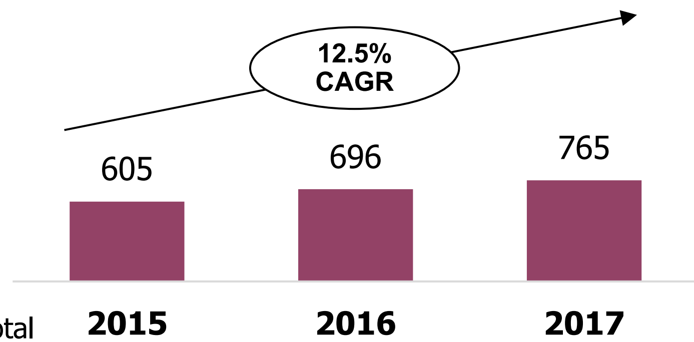
% of total U.S. business	12.0%	14.6%	18.9%	**+6.9%**

Other States



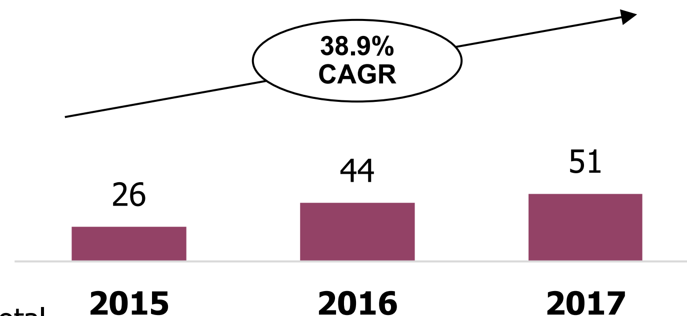
% of total U.S. business	41.0%	46.0%	45.1%	**+4.1%**

Home State



% of total U.S. business	47.0%	39.0%	36.0%	**-11.0%**

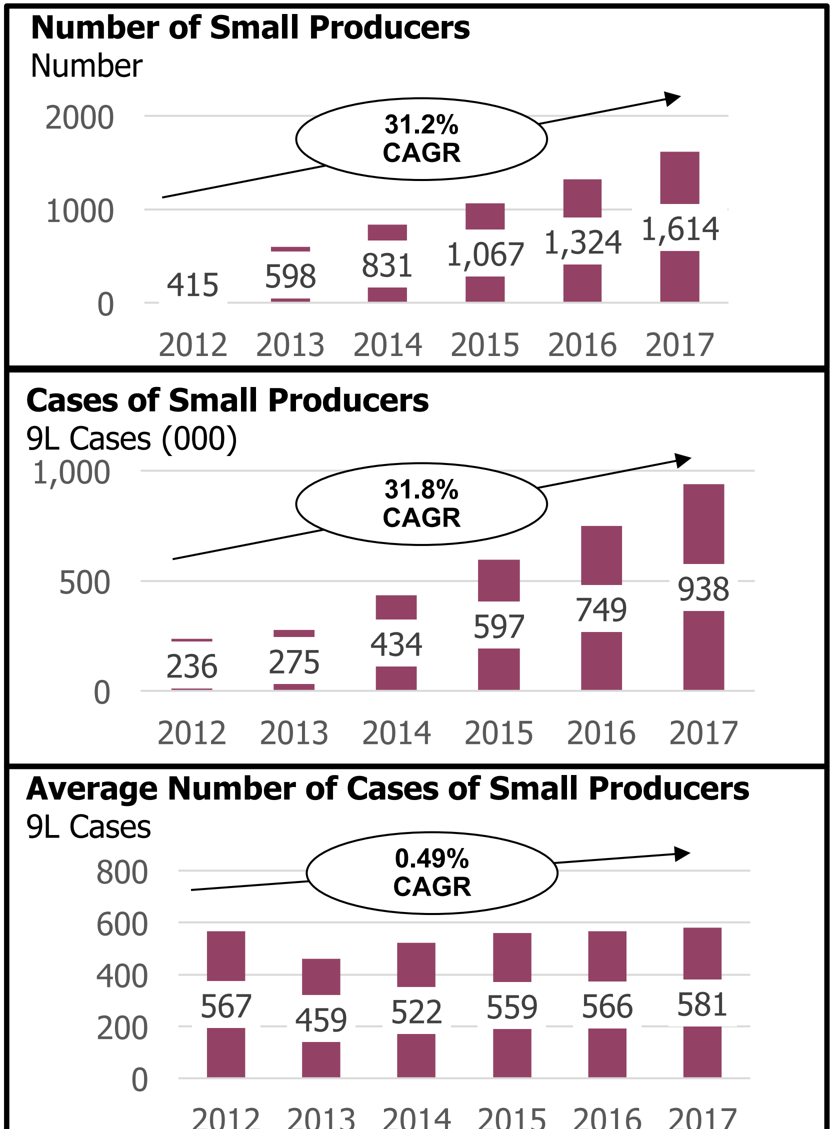
Export



% of total U.S. business	2.0%	2.4%	2.3%	**+0.3%**

Sources: TTB, ACSA, ADI, State ABC Boards, State Guilds, Team Analyses

Small Craft Producers Have Been Growing Well



- The number of small craft distillers as well as their number of cases has been growing rapidly
- The number of small craft distillers has grown almost six-fold from 415 in 2013 to 1,614 in 2017
- The number of cases of small craft distillers has grown from 236k 9L cases in 2012 to 938k 9L cases in 2017
- The average number of cases of small craft distillers has slightly increased from 567 9L cases in 2012 to 581 9L cases in 2017

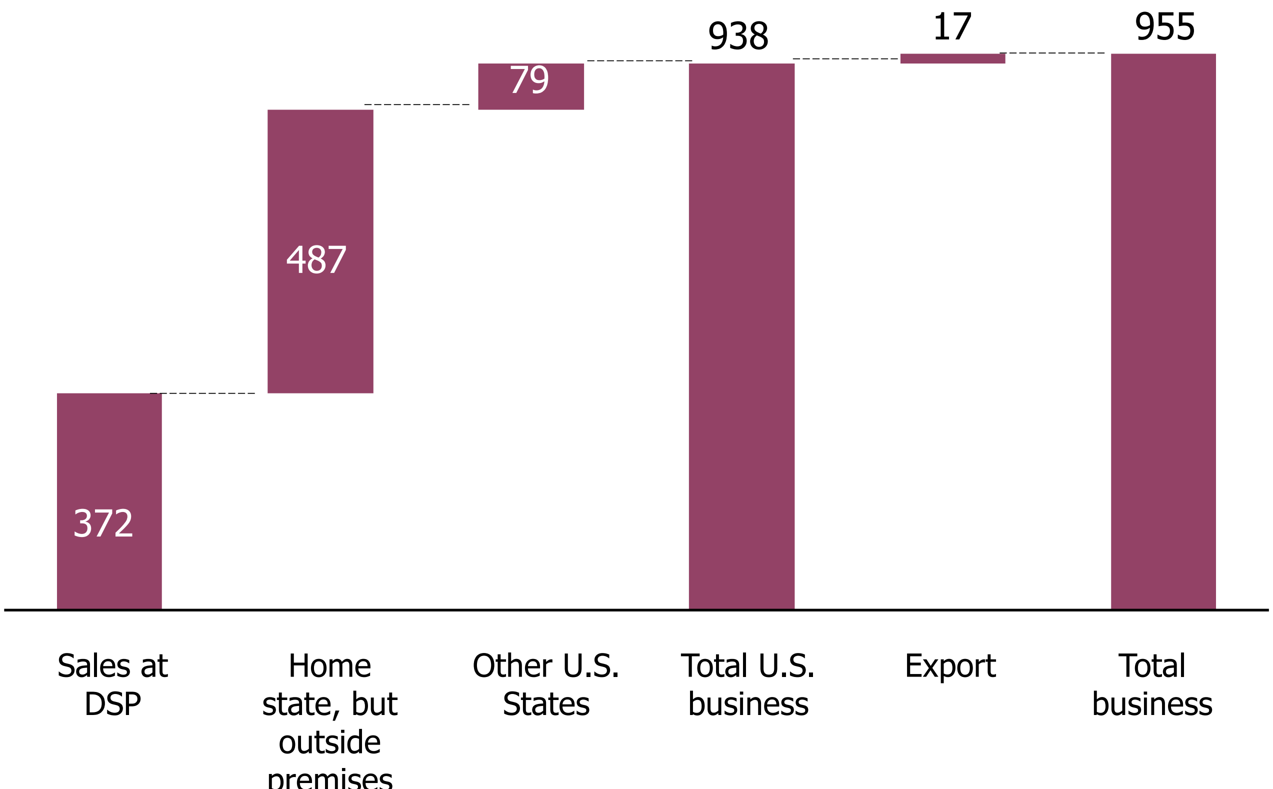
Sources: TTB, Distiller Surveys, Team Analyses

92% of the Business of Small Craft Producers Takes Place in the Home States

CRAFT SPIRITS DATA PROJECT

Sources of Case Sales – Small U.S. Craft Spirits Producers, Domestic and Export 2017

9L Cases (000)



% of total U.S. business	40%	52%	8%	100%	2%	102%

- 40% of the total business of small craft producers comes from sales at the DSP
- Less than 10% of the total business comes from sales outside the home state

Sources: TTB, ACSA, ADI, State ABC Boards, State Guilds, Team Analyses

American Craft Spirits Association

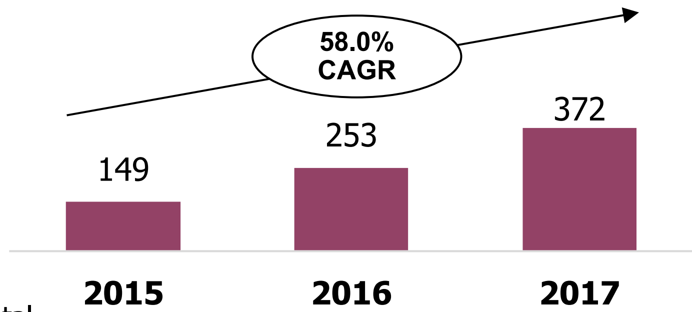
IWSR drinks market analysis

Small Craft Producer Sales Are Slowly Growing Outside of Their Home States

Small Craft Spirits Producers, Sources of Case Sales, 2015 – 2017

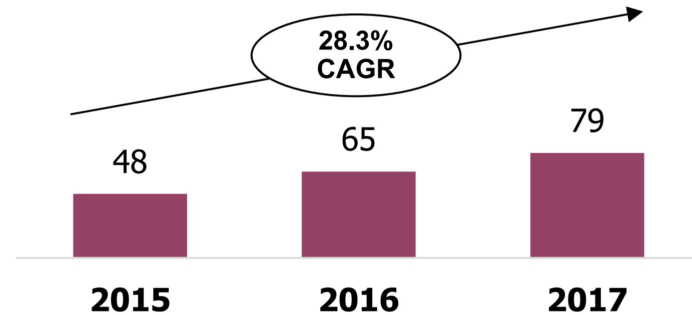
9L Cases (000)

Sales at DSP



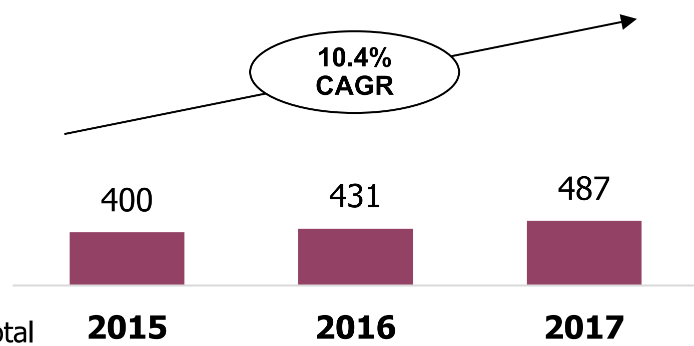
% of total U.S. business: 25.0% | 33.8% | 39.7% | **+14.7%**

Other States



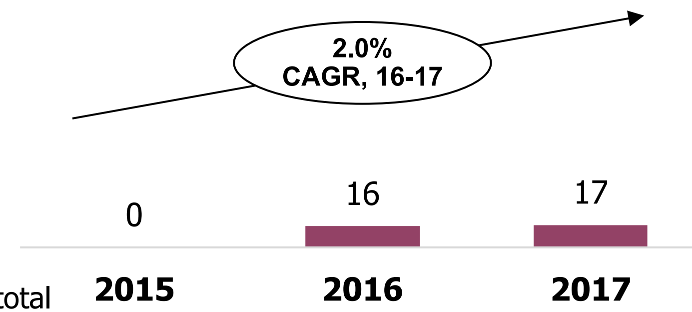
% of total U.S. business: 8.0% | 8.7% | 8.4% | **+0.4%**

Home State



% of total U.S. business: 67.0% | 57.5% | 51.9% | **-15.1%**

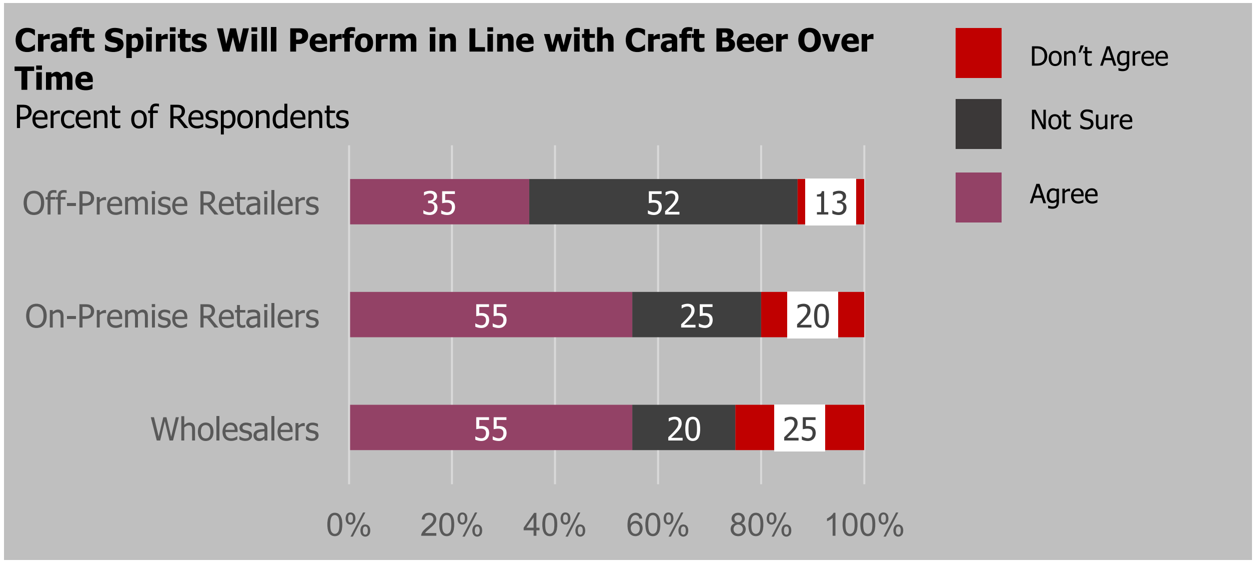
Export

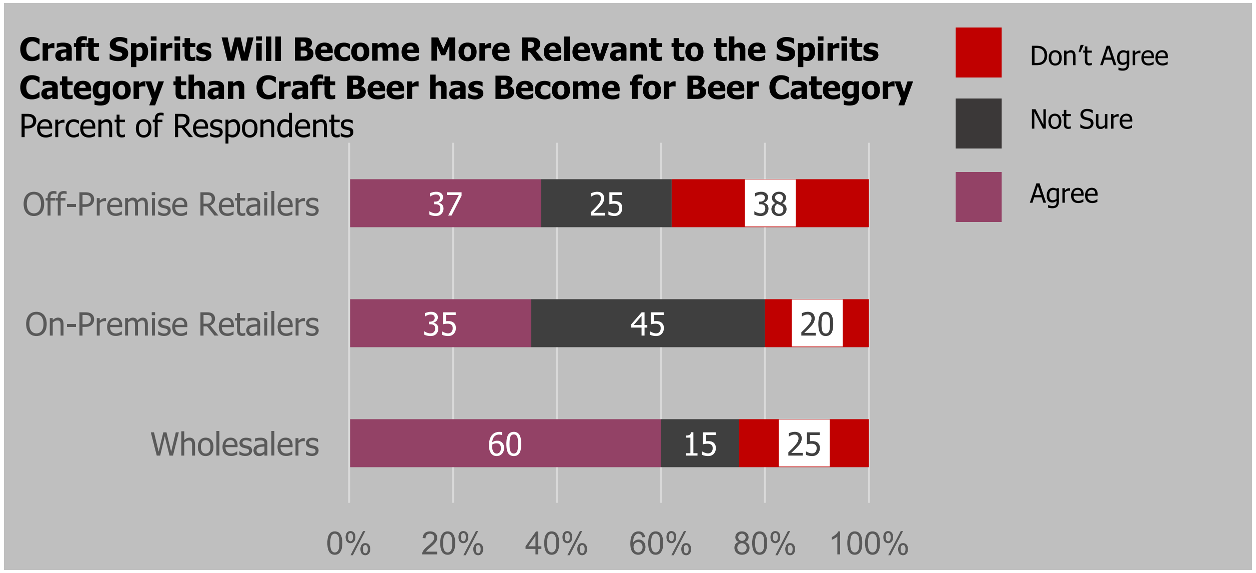


% of total U.S. business: 0.0% | 2.2% | 1.8% | **+1.8%**

Sources: TTB, ACSA, ADI, State ABC Boards, State Guilds, Team Analyses

Many Retailers and Wholesalers See Potential for Craft Spirits to Perform in Line or Better than Craft Beer



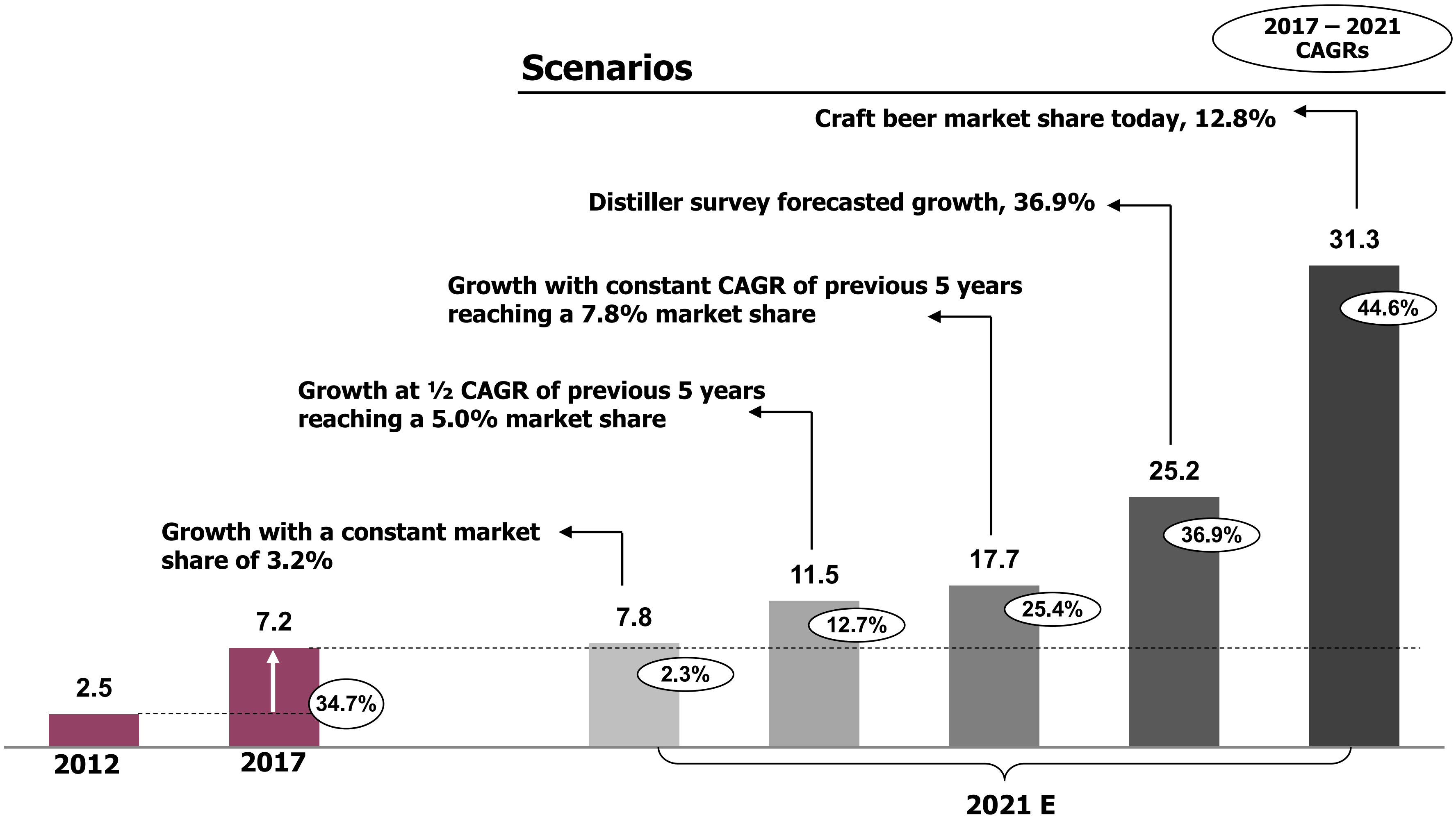


- Many retailers and wholesalers see the potential for craft spirits to perform in line or better than craft beer
- With craft beer market share currently at 12.8% in the U.S., the craft spirits market is expected to continue to grow rapidly

Craft is Still Small but Could See Much Further Growth in Future Years

U.S. Market Size Scenarios for 2021

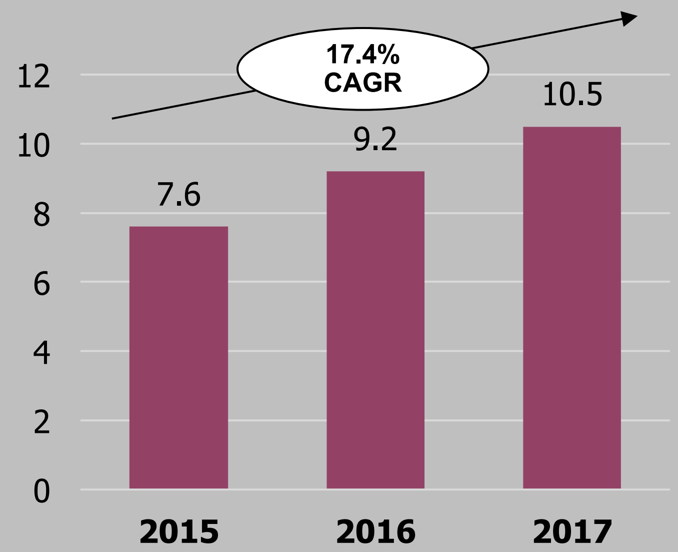
9L Cases (millions)



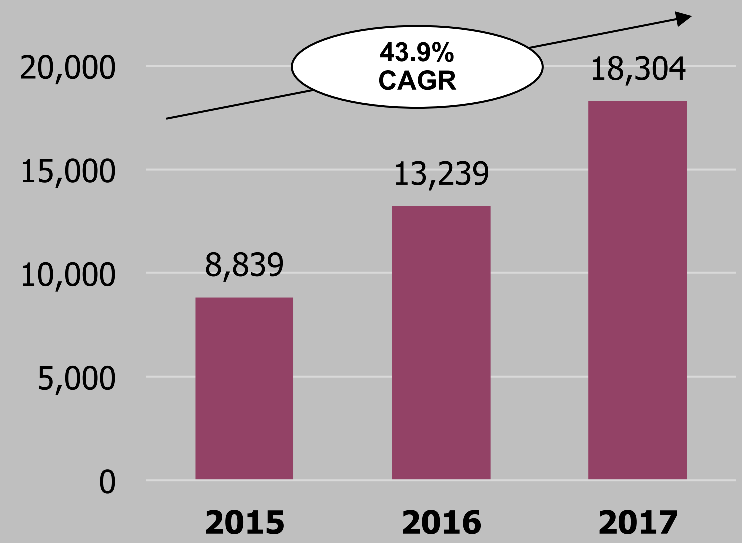
Sources: IWSR, Team Analyses

Employment in the U.S. Craft Industry Has Been on the Rise

Average Full-Time Domestic Employees of U.S. Craft Spirits Producers, 2015 – 2017
FTEs

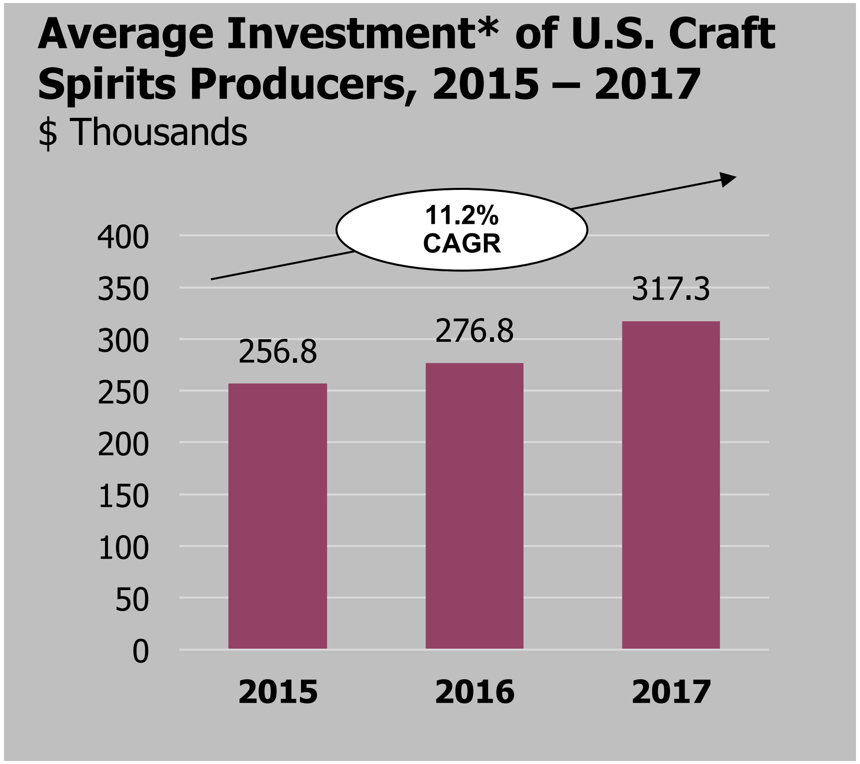


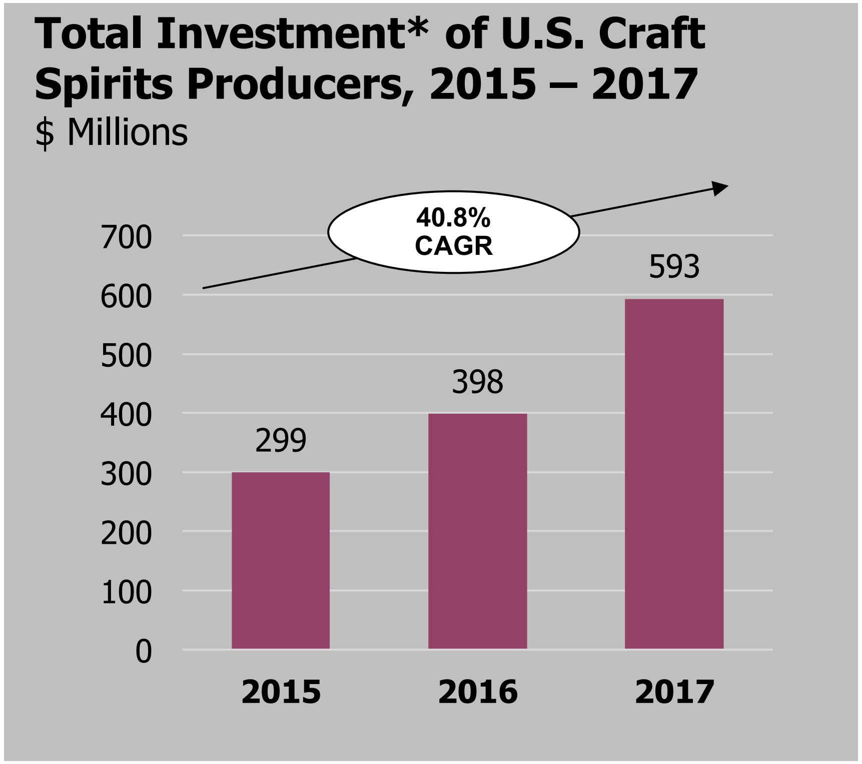
# of Full-Time Domestic Employees of U.S. Craft Spirits Producers, 2015 – 2017
FTEs



- Number of average FTEs has increased by 38.2% between 2015 and 2017
- Total employment has surpassed the 18,300 mark in 2017 with a strong CAGR of 43.9% since 2015

Investment in the U.S. Craft Industry Has Been on the Rise

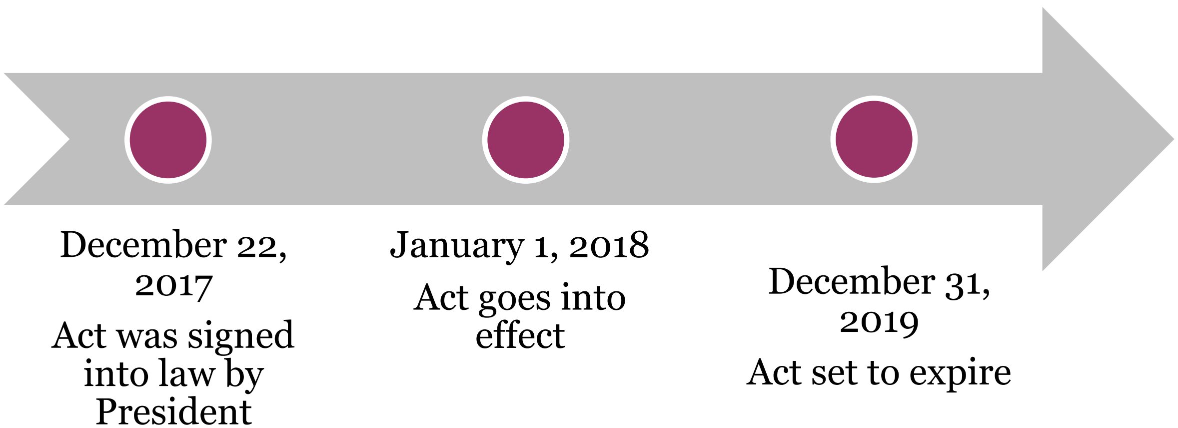




- The average investment of a U.S. craft producer has increased by 14.6% from $276.8k in 2016 to $317.3k in 2017
- Total investment has increased by 48.9% from $398m in 2016 to $593m in 2017

Sources: Distiller Surveys, TTB, Team Analyses. *Investments for expansions.

Overview and Update on the Craft Beverage Modernization and Tax Reform Act



The Act provides for reduced tax rates on distilled spirits, wine, and beer for the 2018 and 2019 calendar years

There are two reduced tiers for Distilled Spirits

- The first 100,000 proof gallons will be charged at $2.70 per proof gallon
- Over 100,000 proof gallons up to 22,230,000 proof gallons will be charged $13.34 per proof gallon

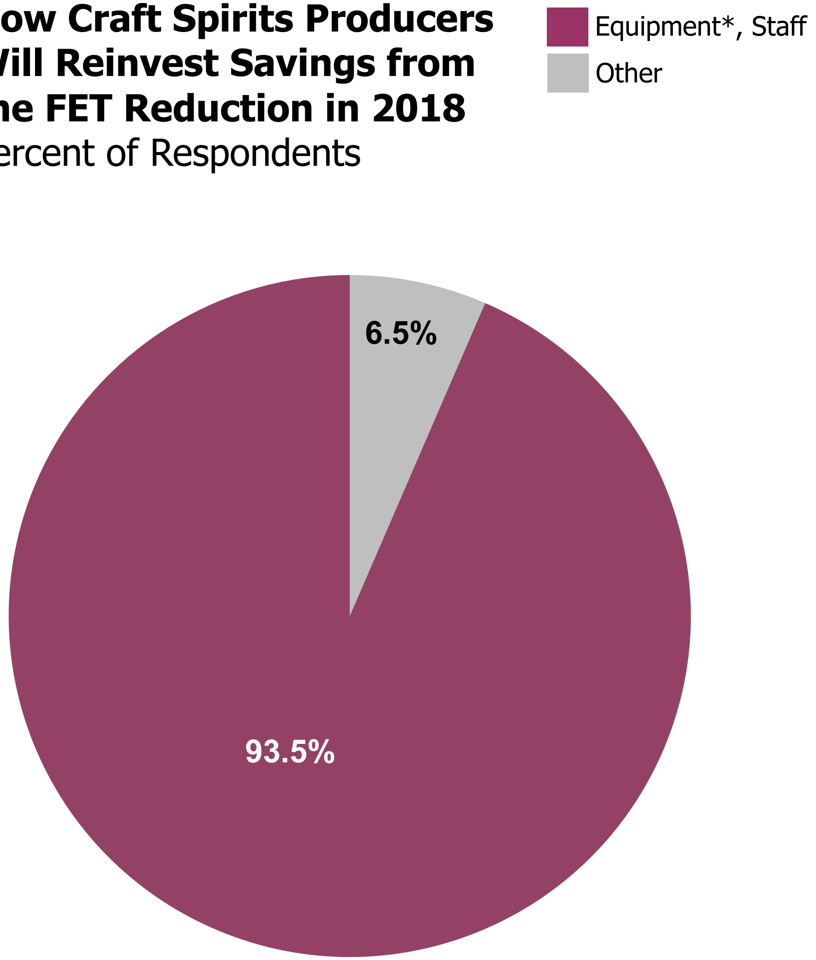
The tax reduction is set to expire at the end of 2019

Sources: TTB, ACSA, Team Analyses

Craft Spirits Producers Plan on Reinvesting Most of Their FET Savings in Equipment and Staff

CRAFT SPIRITS DATA PROJECT

How Craft Spirits Producers Will Reinvest Savings from the FET Reduction in 2018
Percent of Respondents



"We plan on using our FET savings towards purchasing a second still, designing and building a tasting room, and hiring 2 sales reps."
-Distiller 1

"With our FET savings we hope to build a barrel warehouse, hire more staff, reduce water usage and increase production."
-Distiller 2

"Our FET savings will give us the opportunity to build a new barrelhouse and distillery, and increase our production staff."
-Distiller 3

Sources: Distiller Surveys, Team Analyses. *Equipment (e.g., production, tasting room, etc.).

Contact Information

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Appendix

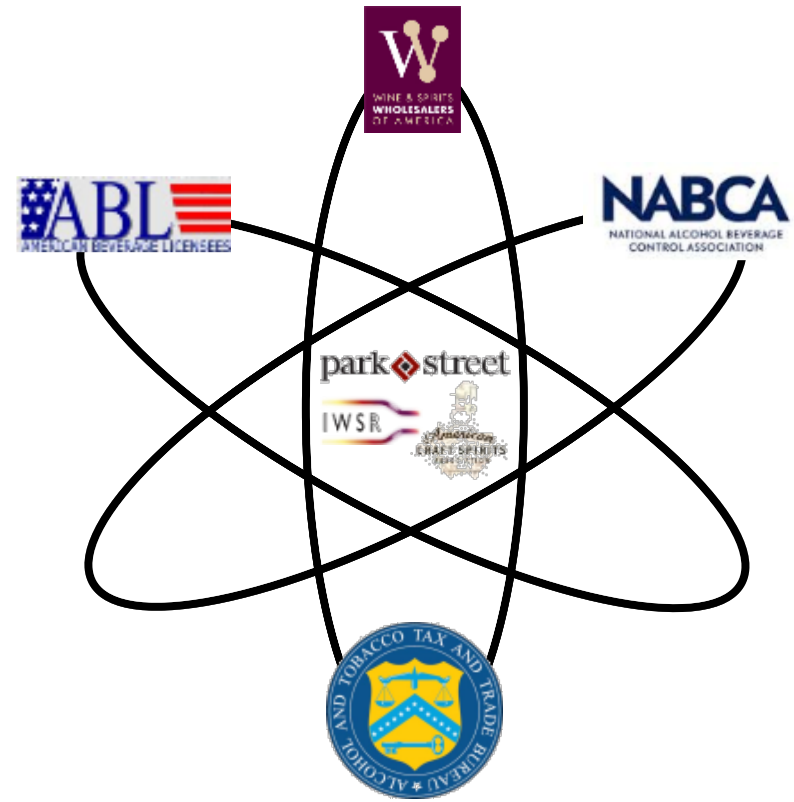
Project Background and Craft Spirits Definition

Craft Spirits Data Project - Industry Wide Collaboration

Teaming up for a common cause

The American Craft Spirits Association, International Wine and Spirits Research, and Park Street teamed up in 2015 to launch the Craft Spirits Data Project (the "Project"), a research initiative with the goal of providing a solid and reliable fact base for evaluating performance and trends in the U.S. craft spirits industry

- Major industry stakeholders such as the TTB, NABCA, WSWA, and ABL have committed resources to help the Project
- The fact base helps all stakeholders to make their respective investment cases and vastly improve an understanding of the full impact at the local, regional, and federal level
- The Project is set-up to provide a consistent fact base for all stakeholders on an ongoing basis. Update reports will be published annually



Project Background and Research Methodology

- **The project serves to:**
  - Quantify the number, size, and impact of craft spirits producers in the U.S.
  - Create a deeper understanding of the U.S. craft spirits landscape among four key groups: DSPs, wholesalers, retailers, and consumers
  - Provide findings on craft supplier best practices and success factors
- **The following information was collected** (all information was collected with the assurances of full confidentiality):
  - Data on craft distiller production size and patterns, sources of revenue, and the category's overall economic impact within the spirits industry
  - Data on craft spirits business size, patterns, and outlook on the wholesaler and retail levels (both on- and off-premise)
  - Input on craft spirits brand perceptions
- **Things to remember**:
  - When estimating the number of producers behind the U.S. craft spirits production, the Project team relied on a combination of official data released by regulatory authorities, survey data, other industry data sources both national (e.g., NABCA, ACSA) and regional (e.g., guilds), as well as interviews and team assessments using the craft distiller definition
  - In the accompanying data sets, the team assumes independent ownership as having equal or more than a 75% equity stake and/or operational control of the DSP. The team has set up a process that asks industry members to notify the ACSA of all ownership or strategy changes away from craft so the changes can be reflected accordingly in the database

Project Organizer: American Craft Spirits Association (ACSA)

Craft Spirits Data Project

The American Craft Spirits Association (ACSA) is the only registered non-profit trade association representing the U.S. craft spirits industry. Its mission is to elevate and advocate for the community of craft spirits producers. Membership in ACSA is open to anyone.

ACSA is governed by a Board of Directors elected by the eligible voting members of the Association. Voting members must be independent, licensed distillers (DSPs) annually removing fewer than 750,000 proof gallons from bond (the amount on which a federal excise tax is paid.)

ACSA was founded in 2013 by 23 founding craft distillers.

Project Partners: IWSR and Park Street

the Source for Wine & Spirits Analysis

The IWSR is the leading source of data and analysis on the beverage alcohol market. IWSR is the longest-running research company specializing exclusively in global alcoholic drinks. The IWSR's comprehensive database quantifies the global and local market of wine, spirits, beer, cider and prepared cocktails by volume and value, and provides insight into short- and long-term trends

Park Street delivers productivity-enhancing and cost-saving back-office solutions, advisory services, and working capital to more than 4,500 alcoholic beverage brands from the U.S. and around the world. Established in 2003, the company provides a fast and reliable conduit to the U.S. and E.U. markets and a cost-effective operating platform. Park Street works with suppliers at all stages of growth and its clients range from entrepreneurial craft distillers to multi-brand global portfolios

Project Supporters: Broad Industry Collaboration

TTB: Provided Beverage Spirits Producers and Bottlers by Average Taxable Removals; agreed to change annual reporting moving forward to enable consistent fact basis

WSWA: Assisted in wholesaler survey design and execution with members

ABL: Assisted in on- and off-premise retailer survey design and execution with members

NABCA: Provided in-depth view of craft distillers using control state data

What Constitutes a Craft Spirit?

- There is no universally accepted definition of craft spirits in the industry, and the expression "craft spirit" is not protected in any way
- Given the positive trends for craft spirits from a consumer perspective (e.g., premium to other spirits, rising demand), there is a natural incentive for brands to utilize craft spirits cues and position themselves as a craft spirit
- The industry has responded with different definition attempts based on criteria for the producer of the craft spirit including production steps at the location, ownership and operational control of the distillery, subscription to an ethics code based on honesty and transparency, production methodology, and size of production
- Many of the criteria used or suggested by industry members would require a formal certification or peer approval process in order to be used as a universal base for quantification purposes
- As long as a universally accepted craft spirits certification or approval that could be used as an industry wide criteria remains unavailable, the quantification has to rely on certain verifiable quantitative metrics which are complemented by estimates to bridge gaps
- Looking at the manufacturer, size of production, ownership/control, and production specifics are criteria that could possibly be measurable and verifiable. However, the consistent collection of the data is not without barriers and could be very cumbersome, which suggests the potential use of a pragmatic approach

- U.S. craft spirits, as defined pragmatically for the purposes of the research, are distilled spirits that are produced in the U.S. by licensed producers that have not more than 750,000 proof gallons (or 394,317 9L cases) removed from bond, market themselves as craft, are not openly controlled by a large supplier, and have no proven violation of the ACSA Code of Ethics

Craft Distillers by Size – Classification Definition

	Range of gallons removed from bond annually*	Range of 9L cases removed from bonds annually*	Characteristics
Large craft distiller	100,001 – 750,000	52,577 - 394,317	▪ Often nationally distributed ▪ If negative cash flow, then by choice in favor of investment
Medium-size craft distiller	10,001-100,000	5,259 – 52,576	▪ Often regionally distributed ▪ Often still cash flow negative
Small craft distiller	1- 10,000	1 - 5,258	▪ Often only locally distributed ▪ If no on-premise business, typically cash flow negative

Sources: TTB, Team Analyses' *Assuming on average 80 proof alcohol content; for purposes of the analysis removed from bond equals sales