

Craft Beer Update

Brewing a Strong Future

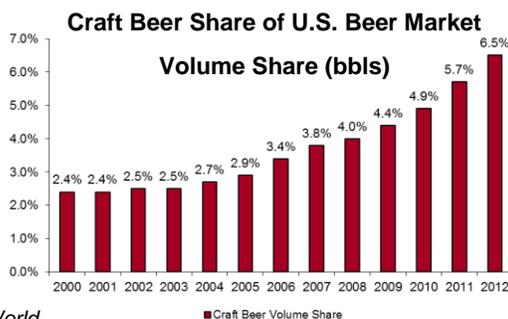
U.S. BEER INDUSTRY AT A GLANCE

The U.S. beer brewing market is big, with an estimated \$28.2 billion in revenues and \$2.9 billion in net profits for 2013.¹ Despite its size, however, the industry reported negative annual growth over the past three years. Much of this negative trend can be attributed to increasingly knowledgeable and health-conscious consumers who are trading up for higher-quality craft beers and other alcoholic beverages. Consumers have therefore shifted away from bulk beer producers like Anheuser-Busch and MolsonCoors, opting for finer products in lesser quantities.²

The future projected performance of the U.S. brewing industry as a whole is somewhat uncertain. Consumer spending is now reaching levels not seen since before the economic downturn in 2008 and 2009, and with this, consumers are beginning to move back toward purchasing premium beverages like wine and liquor. Despite this trend, the craft beer sub-segment of the U.S. brewing industry has fared extremely well over the past several years, and is expected to see significant continued growth in the future.

A CLOSER LOOK AT CRAFT BEER

The Brewers Association defines a craft brewer as any brewery producing six million barrels of beer or less per year. The brewer must be less than 25% owned or controlled by an alcoholic beverage industry member who is not a craft brewer, and must produce a flagship beer that represents the majority (at least 50%) of their total sales. In 2012, 2,347 craft breweries were in operation, representing almost 98% of total breweries in the U.S. That said, the craft brew industry represents a relatively small percentage of the beer industry in terms of sales, with a share of approximately 6.5% by sales volume and 10.2% by sales in dollars for 2012.



August 2013

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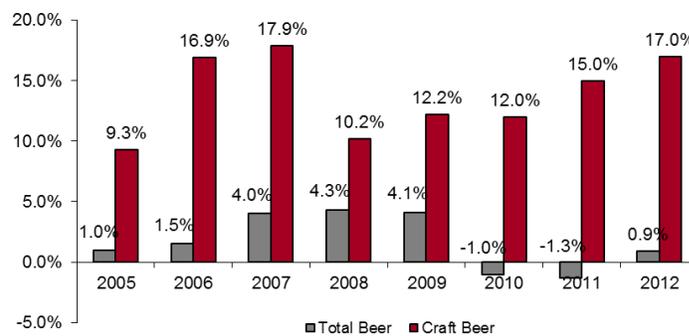
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¹ Brewers Association

² IBISWorld

The craft brew industry has seen major sales growth and development over the past five years, significantly outpacing the sales growth rate of the overall beer industry by almost double. Recent purchasing trends indicate that consumers are willing to pay more for craft beer in order to obtain a higher quality product. Additionally consumers are moving more towards the purchase of local, regionally produced beer, shifting away from the large, low cost, and global presences of companies such as Anheuser-Busch InBev. As a result, from 2007 to 2012, sales in the craft brewing industry grew by almost 50%, from \$2.1 billion in 2007 to \$3.1 billion in 2012. This trend is not expected to stop, either. Sales projections for the craft brew industry over the next five years show an expected growth of another 32%, totaling \$4.1 billion, by 2017.³

U.S. Beer Market Sales Growth Rates



Source: Brewers Association

Each year the Brewer's Association releases a list of the top 50 craft breweries in the U.S. by sales volume. Over the past five years, the top 10 craft brewers have remained, for the most part, unchanged. Boston Beer Company, operating under the Samuel Adams brand name, is far and away the largest craft brewer, with 2012 revenues of almost \$600 million and 2,125,000 barrels sold. Boston Beer accounts for approximately 16.5% of the craft beer market share. The next four largest craft breweries are Sierra Nevada, New Belgium Brewing Company, The Gambrinus Company/Spoetzl Brewery, and Deschutes Brewery, representing an additional 20.1% share. After these few select companies, the playing field opens to a group of thousands of craft brewers fighting for a share of the market.⁴

Top 10 Craft Brewers (volume), 2012 Barrels

Rank	Brewery / Top Brand	Barrels	Share
1	Boston Beer Co. / "Sam Adams"	2,215,000	16.5%
2	Sierra Nevada Brewing Co. / "Sierra Nevada"	966,007	7.5%
3	New Belgium Brewing Co. / "Fat Tire"	764,741	5.9%
4	Gambrinus / "Shiner Bock"	605,896	4.7%
5	Deschutes Brewery / "Deschutes"	255,093	2.0%
6	Lagunitas Brewing Co. / "Lagunitas"	244,420	1.9%
7	Bell's Brewery, Inc. / "Bell's"	216,316	1.7%
8	Matt Brewing Co. / "Saranac"	207,900	1.6%
9	Harpoon Brewery / "Harpoon"	193,000	1.5%
10	Stone Brewing Co. / "Stone"	177,199	1.4%
		5,755,572	44.6%

Source: Brewers Association

³ IBISWorld

⁴ Brewers Association

M&A TRANSACTIONS

The craft brewing industry is growing, and growing quickly. Many brewers are seeking new ways to maximize production volume to keep up with demand, while still keeping their products facing consumers through an increasingly intensifying fight for shelf space. These operating stresses strain the capacity for many craft brewers to grow, and could ultimately lead to a ramp up in industry consolidation over the next several years.

In the past several years, the craft beer industry has seen a steady amount of deal activity, and this trend only stands to grow as more and more craft brewers enter the market. Driven by strategic considerations, notably product diversification and breadth, as well as economies of scale in production, early investments in craft brewing were made by companies like Anheuser-Busch and MolsonCoors as far back as the late 1980s. Indeed, MolsonCoors now has a division, Tenth & Blake, which acts as an incubator for new craft beer brands and products. Alongside these strategic players have recently come new investors, from both international corporations and private equity firms. The following list shows recent deal activity in the craft beer industry:

<u>Closed Date</u>	<u>Target</u>	<u>Total Transaction Value (\$USDmm. Historical rate)</u>	<u>Transaction Type</u>	<u>Buyer</u>
3/25/2013	Utah Brewers Cooperative, LLC	35.0	Private Placement	Fireman Capital Partners,
12/28/2013	New Belgium Brewing Company, Inc. (Kim Jordan)	59% stake	Merger/Acquisition	New Belgium Brewing Company, Inc. (Employees)
12/21/2012	Vermont Hard Cider	305.0	Merger/Acquisition	C&C Group, plc
12/11/2012	North American Breweries, Inc.	388.4	Merger/Acquisition	Cerveceria Costa Rica S.A.
6/15/2012	Associated Microbreweries of America (Karl Strauss)	13.95	Private Placement	-
2/6/2012	Crispin Cider Co. Corp.	NA	Merger/Acquisition	MillerCoors LLC
1/4/2012	The Saint Louis Brewery, Inc. (Schlafly Bottleworks)	60% stake	Merger/Acquisition	Sage Capital, LLC
10/14/2011	Terrapin Beer Company, LLC	NA	Minority Stake	MillerCoors LLC
3/28/2011	Fulton Street Brewery, LLC	39.8	Merger/Acquisition	Anheuser-Busch
4/23/2010	Anchor Brewing Company	NA	Merger/Acquisition	The Griffin Group, LLC
8/11/2010	Independent Brewers United, Inc.	NA	Merger/Acquisition	Craft Brewers Alliance, Inc.
8/3/2010	Kona Brewing Co., Inc.	15.47	Merger/Acquisition	Craft Brewers Alliance Inc. (NasdaqGM: BREW)

Source: Capital IQ

VALUATION ANALYSIS

The majority of craft brewers are private companies, and thus do not disclose their financial information. This provides limited guidance in terms of valuation. However, there are a handful of publicly traded American brewing companies, both craft and otherwise, to lend some insight.

Public Comparables, August 2nd, 2013

Craft Brewers > Publicly Traded Comparables

Company Name		TEV	Market Cap	TEV/LTM Total Rev	TEV/LTM EBITDA
Boston Beer Co. Inc.	NYSE:SAM	2,570.7	2,594.7	3.6x	18.3x
Craft Brew Alliance, Inc.	NasdaqGM:BREW	192.5	181.2	1.1x	20.3x
	Median	1,381.6	1,388.0	2.4x	19.3x

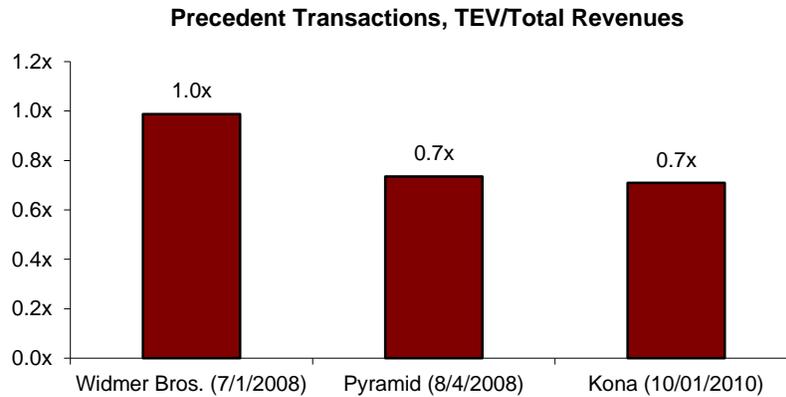
Conglomerate Brewers > Publicly Traded Comparables

Company Name		TEV	Market Cap	TEV/LTM Total Rev	TEV/LTM EBITDA
Anheuser-Busch InBev SA/NV	ENXTBR:ABI	205,347.0	156,572.3	4.9x	12.3x
Carlsberg A/S	CPSE:CARL B	22,628.8	15,263.9	1.9x	9.5x
Heineken Holding NV	ENXTAM:HEIO	44,129.7	18,401.4	1.8x	9.0x
Molson Coors Brewing Company	NYSE:TAP	13,461.9	9,296.4	3.3x	10.4x
SABMiller plc	LSE:SAB	96,990.7	79,431.1	5.5x	14.2x
	Median	44,129.7	18,401.4	3.3x	10.4x

Source: Capital IQ, Tully & Holland analysis

As of the date of this publication, conglomerate brewing companies traded at a median enterprise value to EBITDA multiple of 10.4x, and at a median enterprise value to total revenue multiple of 3.3x. Publicly traded craft brewers traded at a median enterprise value to EBITDA multiple of 19.3x, and a median enterprise value to total revenue multiple of 2.4x. The companies represented here exemplify the most successful and well-established conglomerate and craft brewers in the marketplace, and therefore command relatively high valuations.

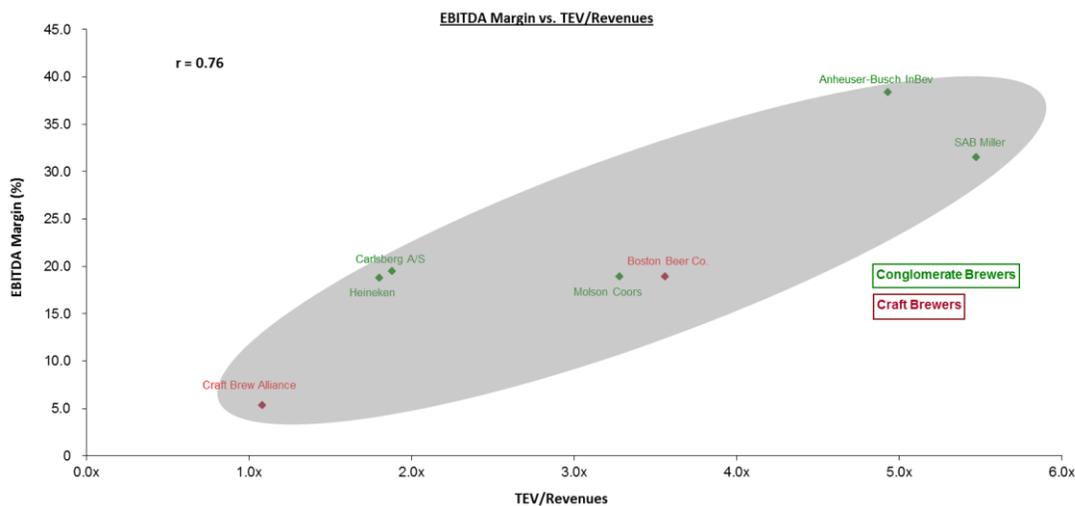
Multiples for the industry’s largest publicly traded companies are likely on the high side of what most privately held craft brewers could expect to realize. Since 2008, there have been three private transactions of established craft breweries. These transactions offer multiples that illustrate a more likely valuation range of 0.7x to 1.0x total revenues.



Source: Capital IQ

Valuation of beer companies, craft or conglomerate, is a function of the strength of cash flows, and not of total revenues. This is exemplified by comparing total enterprise value to total revenue multiples against EBITDA margins of selected publicly traded beer companies. An r-square value of .76 explicitly demonstrates the relation between a healthy EBITDA margin and a high multiple.

As of August 2nd, 2013



Source: Capital IQ, Tully & Holland analysis

T&H CONCLUSIONS

The craft beer industry continues to outpace the growth of the overall beer category, with consistent upward trends in both dollar sales and sales volume. In recent years, there have been several M&A transactions in the craft beer and craft brewing sector. Deal activity is currently steady, and buyers are becoming more and more diverse as the industry continues to grow. These buyers have and will be willing to pay a premium for profitability and growth, especially concerning strategically complimentary targets. Additionally, in the next several years, there will be significant contention amongst craft brewers over shelf space and distribution, which will most likely spur a movement towards industry consolidation.

Tully & Holland advised the majority owner of Independent Brewers United Inc. ("IBU") in the sale of Magic Hat, Pyramid, and MacTarnahan's beers to North American Breweries, Inc. Based in Burlington, VT, IBU's specialty craft beers are sold on both the East and West Coasts. Magic Hat has been one of the fastest growing beers within the craft beer segment.



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