Wine Australia

Craft Cider Export – USA

November 2019

Wine Australia

IWSR drinks market analysis

USA Craft Cider

Executive Summary & Recommendations

Wine Australia

IWSR drinks market analysis

USA – Executive Summary

- The US craft cider market must be seen firmly in the **context of three other well-developing craft markets**:
  - Craft beer
  - Craft RTD mixed drinks
  - Craft spirits
- Especially the craft beer and RTD mixed drink (and here particularly the booming hard seltzer market) have **high relevance to/impact on the craft cider market** in terms of:
  - Market participation (many brewers/RTD companies may branch out to ciders)
  - Interchangeability of categories in sales accounts
  - Category blur
  - Positioning as natural refreshment

USA – Executive Summary

- While cider overall has fluctuated in recent years, **craft cider has been gaining in strength** against big cider brands, and some of the former regional craft brands are starting to branch out to way beyond their former geographical sphere of influence.
- In cider, as in the wider Beverage Alcohol market, 'craft' is performing well and at least theoretically **should provide good proving ground for Australian imports**. This must, however, be seen within the context of very strong domestic competition, both from highly local/regional brands and the beginnings of larger craft brands who are expanding state-by-state.
- As always in the case of the US beverage alcohol market the following points need to be borne in mind when attempting to export
    - the post-prohibition era three-tier distribution system
    - the presence of numerous state-controlled states
    - non-unified taxation issues between individual states, forcing a state-by-state approach
    - a restricted, essentially false ecommerce environment hampered by legislative issues and having to operate within the confines of the three-tier system

USA – Executive Summary

- Perhaps with the exception of Angry Orchard/Boston Beer Co the corporate part of the cider market has been struggling over recent years. By contrast, **the most buoyant part of the US cider category is accounted for by smaller domestic producers** of below 50,000 HL output.

- Most of these smaller producers are **primarily active in their own regional markets** and do not attempt to distribute nationwide. In the most important apple-growing areas – New York State and the Pacific Northwest – they have forged **industry associations** for pooling of resources in terms of lobbying, generic advertising, trade events and - increasingly – joint market research. The latter – Northwest Cider Association – indeed straddles national borders by including producers in neighbouring British Columbia (Canada).

- The domestic cider industry is **increasingly organised**, with regional trade bodies supplemented by a national cider association, USACM. Funding of these bodies reportedly remains an issue. The smallest members – of which there are many - have reported outputs of well below 400HL per year.

USA – Executive Summary

- **Imports of cider have suffered in recent years**, accounting for around 13% of volumes in 2018. More than 90% of imports consist of three MNC brands – Stella Cidre, Strongbow and Magners. With the further exception of Rekorderlig, Blackthorn (another C&C brand) and Samuel Smith, no imported brand is achieving more than 700 HL of annual volume, with availability of individual brands fluctuating strongly.
- **Craft cider** has a relatively strong on-premise footprint, more so than big cider brands. Some of the larger craft cider brands estimate their on-premise footprint to be as much as one third of sales volumes, and in geographical pockets even higher. Craft cider on draft is becoming increasingly popular, bringing with it its own distribution issues.

USA – Executive Summary

Pros:

Working **for** Australian craft cider exports are the following trends:

- The USA beverage alcohol market in general has **high acceptance of niche/craft brands** with public opinion especially among more affluent consumers veering away from Big Business with regard to beverage alcohol
- Relevant **buzzwords** that work for cider in the US in general are particularly applicable to craft brands – "gluten-free", "coeliac-friendly", "natural" etc.
- There is a strong consumer trend **towards natural ingredients**
- Australian craft cider appears to have **duty free access** to the USA, licences permitting, under the AUSFTA provisions
- A new generation of cider consumers typically connect with cider through trending products, creating marketing opportunities that may utilise brands' 'Australian-ness'.

USA – Executive Summary

Cons:

Working **against** Australian craft cider exports are the following trends:

- A trend towards ‘craft’ products in beer, RTD mixed drinks and increasingly cider itself also means a high degree of fragmentation. Retailers are increasingly complaining about the **allocation of scarce shelf space** to yet more ‘craft’ brands being offered to them
- Many domestic craft cider producers operate on the back of their own **small-scale orchards** (emphasising provenance and the link to domestic/regional fruit)
- Even among smaller/craft brands there is a tendency to **veer away from pure apple products towards rose offerings**, not the forte of Australian craft producers
- The recent boom in Hard Seltzers at least in part is due to a **strong consumer trend towards real or perceived low-calorie beverage alcohol products**, with cider potentially seen as the antithesis given its fruit base
- The US geographical area most easily served from Australia – the **West Coast** – is also home to one of the most vibrant domestic craft cider scenes (in Washington and Oregon) which filters down into California. Competition from smaller domestic producers will, therefore, be strongest – 80% of whom also operate tasting rooms, tap houses or other on-premise outlets as part of their domestic/local appeal. West Coast cider makers – in addition to defending themselves from both Big Cider and imports – are actually preparing for an **exporting drive** (particularly to Europe).

USA – Recommendations

Australian ciders should have a reasonable chance to gain some traction in the USA's thriving craft scene. The following points need to be watched:

- Competition from domestic companies **working in exactly the same space** is steep, with local companies obviously having an advantage despite Australia's duty-free access
- It is recommended that the '**Australian-ness**' of product is highlighted in order to gain some edge over domestic offerings
- The US cider market in general is **veering away from pure apple products** towards rose and flavoured products. Part of the appeal of US craft cider is adventurous play with flavours.
- Products that may have **'light' credentials or are hybrids** should do particularly well within the current low-calorie (or perceived low-calorie) beverage alcohol boom
- A **state-by-state approach** is crucial to attempting exports to the USA. Distributor partnerships are proscribed, **with direct sales to retail outlets, on-premise outlets or ecommerce platforms not an option.**

USA – Recommendations (cont'd)

- The latter point of course **restricts opportunities for the smaller producers among Cider Australia's clientele** as a direct sale approach to outlets or chains (as would be possible for the UK) is essentially ruled out, with firm structures needing to be in place.
- Similarly, Cider Australia – and of course potentially Wine Australia – are **less able to provide market entry opportunity** for the same reason. Nevertheless, assisted trade fair participation, sponsorship of Australia produce weeks in supermarket chains or sponsorship of Australia-heavy sports events could be ways of gaining consumer (and channel) interest – as long as potential suppliers are clear that appointing distribution partners is compulsory.
- In summary, whereas Australian exporters may have various ways of approaching the UK market, there is really only one market entry mode/route to market available for the USA – a state-by-state distributor approach.

USA Cider

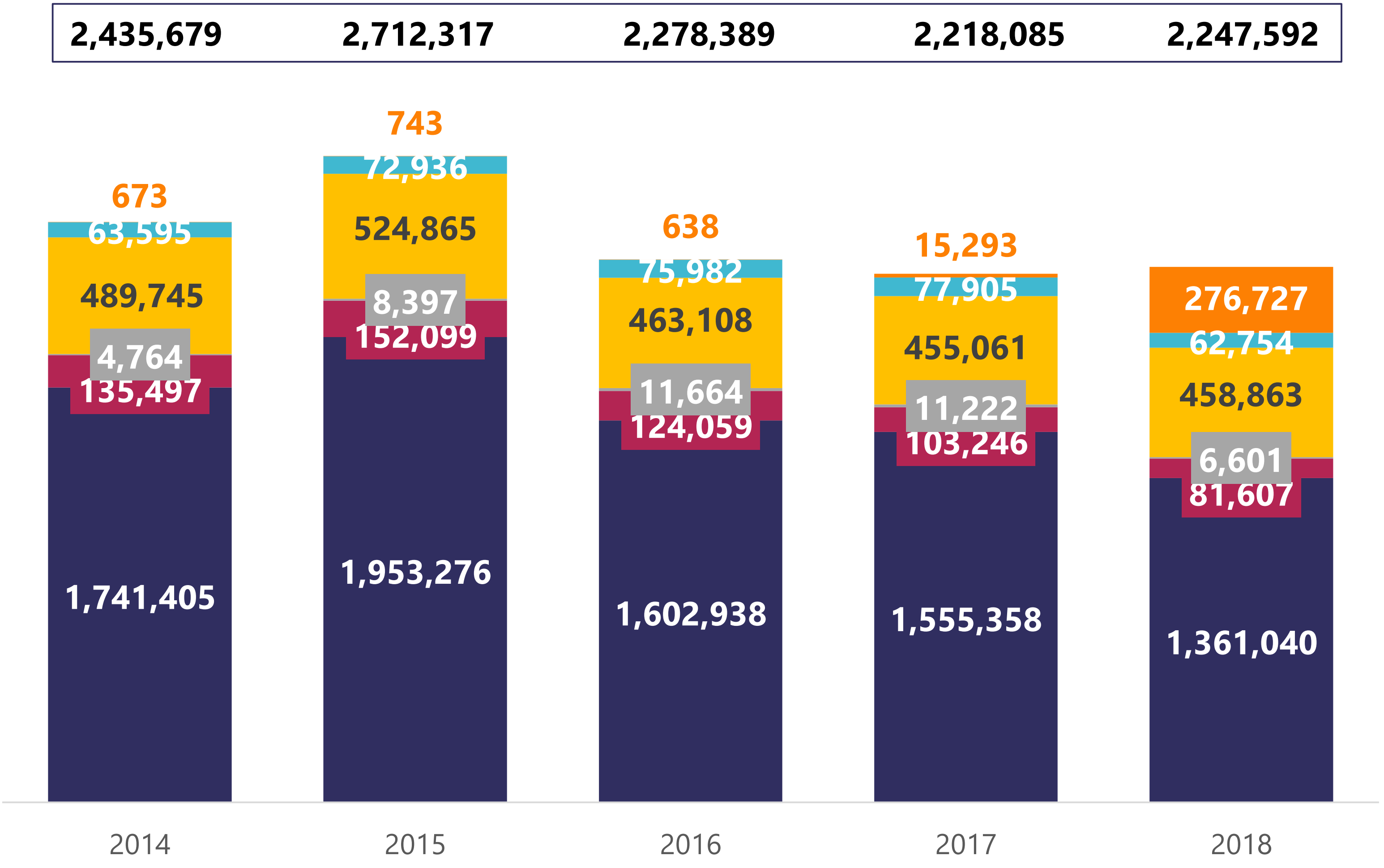
Overall Market and Craft in Context

Wine Australia

IWSR drinks market analysis

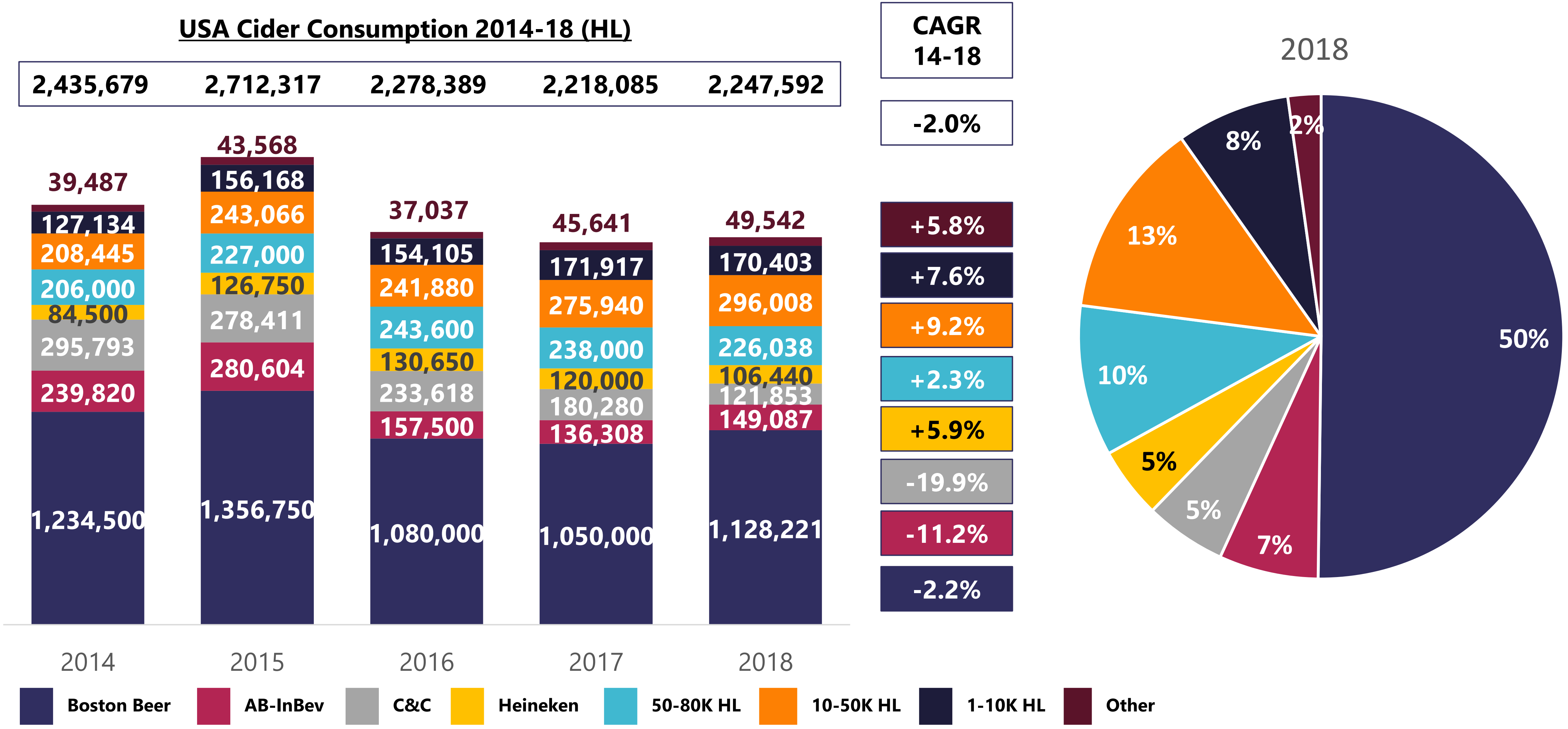
The US cider market is in the process of very significant change. While in slight decline overall (with an errant peak year of 2015) the big change is the **collapse of the dominant apple variant** to the detriment of **exponential growth in rosé ciders**, who had a pivotal year in 2018. Fruit ciders have remained relatively stable while hybrids have followed a path of boom-and-bust in recent years.

USA – Cider Consumption 2014-2018 (HL)

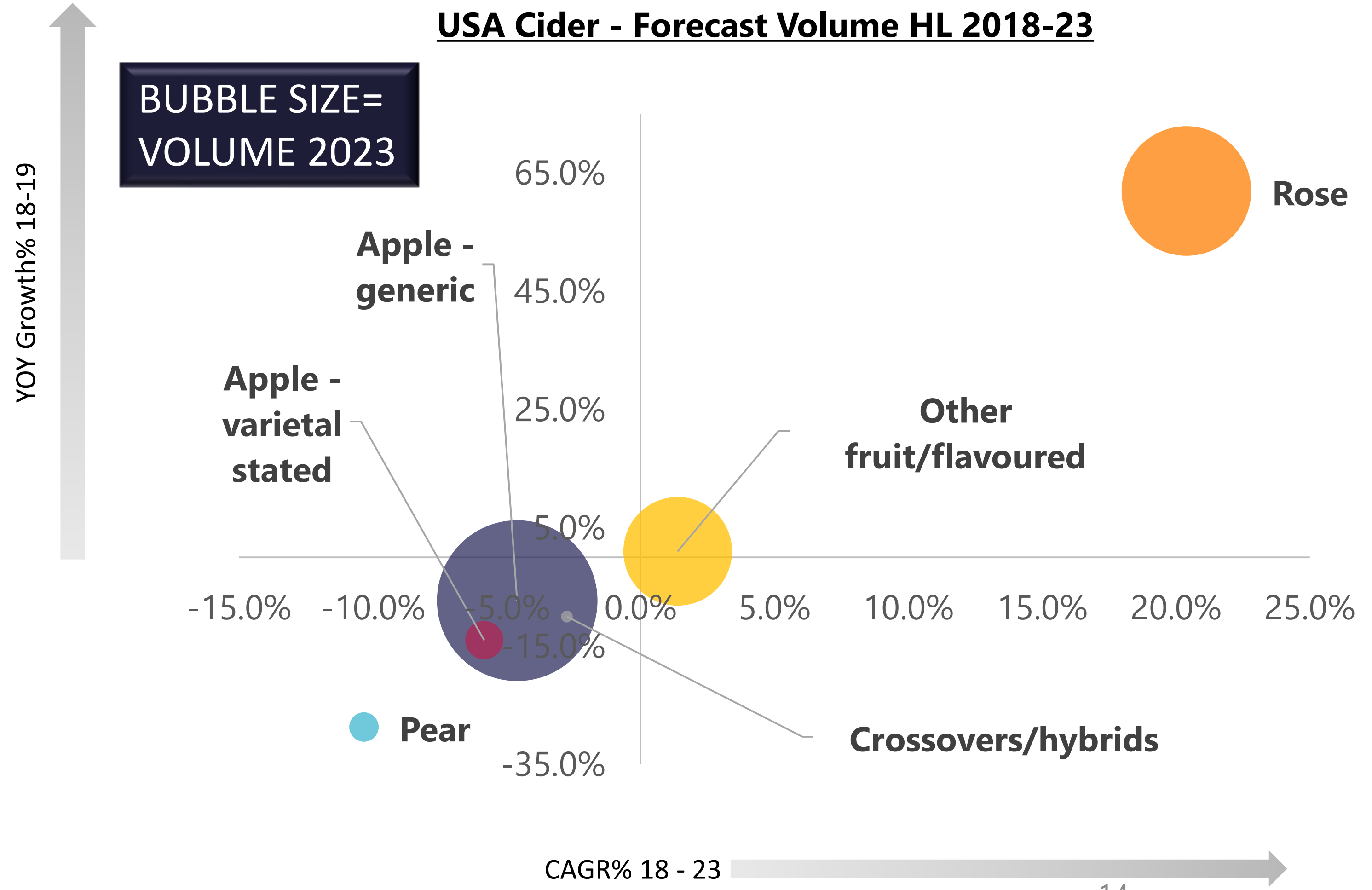


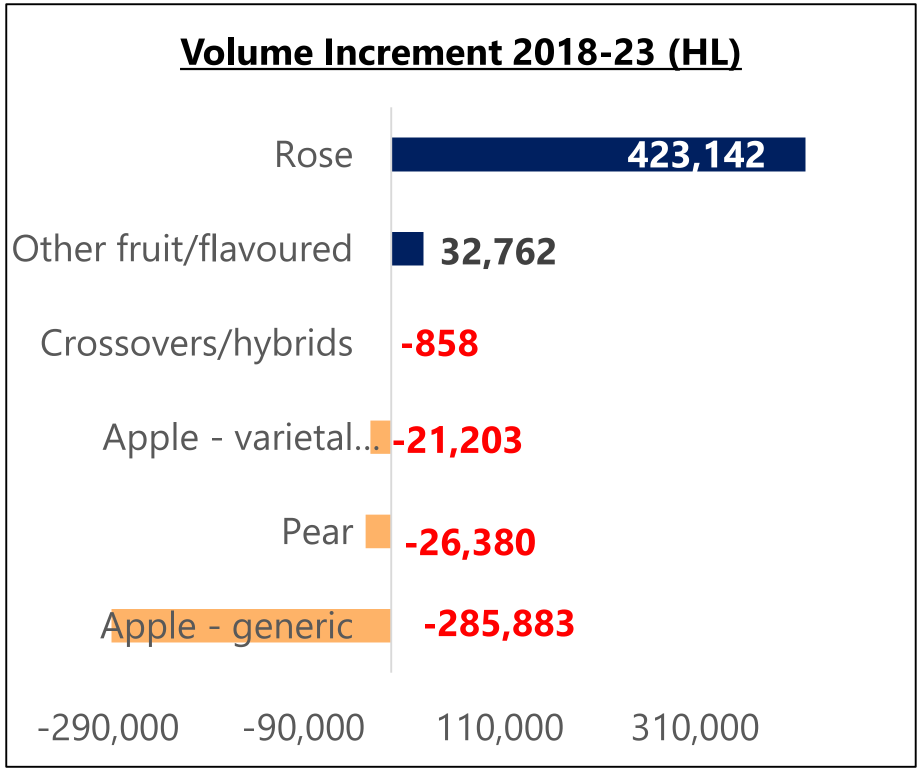
CAGR 14-18	
-2.0%	
n/a	Rosé
-0.3%	Pear
-1.6%	Other Fruit/Flavoured
+8.5%	Crossovers/Hybrids
-11.9%	Apple – Varietal
-6.0%	Apple – Generic

The US cider market has an **unusual make-up** with a **dominant force of more than 50% market share (Boston Beer/Angry Orchard**), three MNCs with much more moderate sales and a **highly-fragmented but very dynamic mid- and lower-field**. Apart from Heineken all leading suppliers have been in decline recently (especially C&C) while all of the lower tiers combined managed to expand.



While the **US cider market overall is expected to resume growth** the structural change is expected to continue, with the **vast majority of growth arriving from rosé ciders**, offset by **significant decline in consumption of generic apple ciders.**





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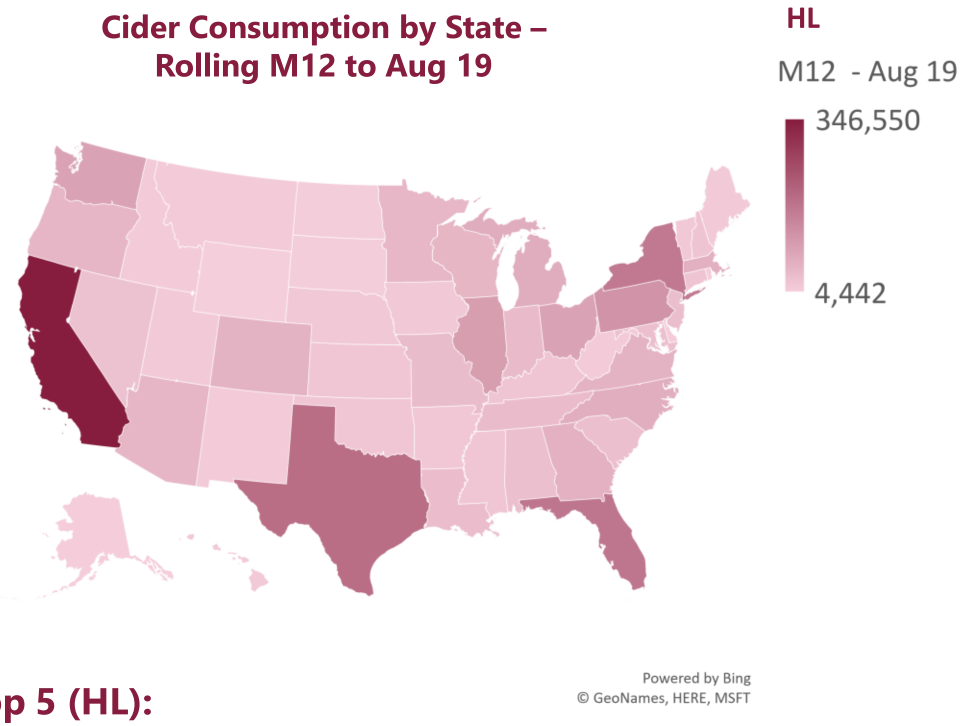
USA – The States: The large population states lead overall consumption while per capita consumption is led by the production states in New England and the Pacific Northwest

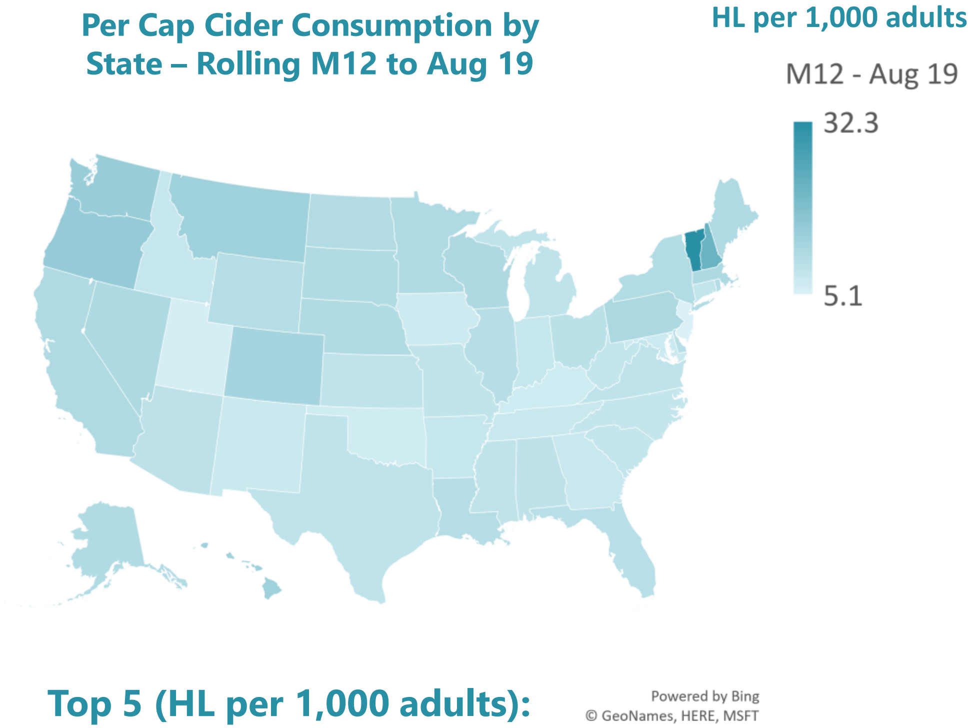
Cider Consumption by State – Rolling M12 to Aug 19



Top 5 (HL):

- California – 346,550
- Texas – 189,319
- Florida – 173,119
- New York – 166,078
- Pennsylvania – 177,206

Per Cap Cider Consumption by State – Rolling M12 to Aug 19



Top 5 (HL per 1,000 adults):

- Vermont – 32.3
- New Hampshire – 22.3
- Oregon – 15.5
- Washington – 15.1
- Montana – 14.0

USA – The Cider Industry and Craft

Defining a craft cider is relatively complex because the market is broken up into a number of different brands that could all be viewed as craft. The **consumer perception** of craft is of a small scale, backyard-style artisan producer but the reality is that larger producers also market brands as 'craft' ciders.

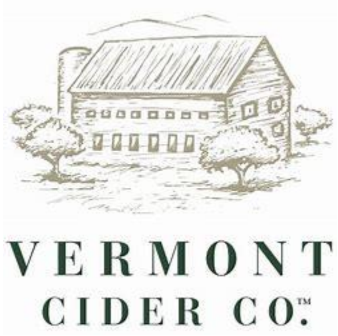
We follow the segmentation offered for the UK 'craft' cider market into distinct segments, most of which are by far dominated by domestic ciders in the US:

- 'Big' and mid-tier craft
- 'Accidental' craft ciders (not relevant in the US context)
- 'Modern' and 'New-to-market' craft ciders (a conflated category with its components in the US indistinct from each other)
- Imported craft ciders
- Traditional farmhouse producers

USA – The Cider Industry and Craft

a) ‘Big’ and mid-tier ‘craft’

Beyond their significant brands of Strongbow, Stella Artois, Woodchuck, Magners or Blackthorn the involvement of multinationals in the US craft cider scene has remained relatively modest. Heineken has so far refrained from marketing its Orchard Thieves cider – successful elsewhere – in the US market, although possibly only a matter of time. AB InBev has limited its engagement with the Virtue and Johnny Appleseed range while C&C is trying to further its credentials with Vermont Cider.



USA – The Cider Industry and Craft

b) Modern/New-to-market craft ciders

In the US particularly this may consist of craft **brewers** who launch craft cider ranges and sell them alongside their brewed products, in addition to ***hard seltzer* manufacturers** (a particular form of American RTD mixed drinks – essentially alcoholic sparkling water) who are branching out into cider. This highlights the US trend that craft *anything* is, indeed, more important than the category itself.

These take their cues from the international craft beer movement, are more 'edgy' in messaging and are aimed primarily at a young, urban consumer base. They often feature in a stub can to mimic craft beer brands and are mostly new to the market. They are not bound by traditional cider conventions. These products are also more likely to experiment with new flavours. Many of these start-ups have probably made more noise than sales, and may derive a significant part of their existing turnover from sales from their own on-premise outlets before developing solutions for the third-party distribution market.

Warren's CIDER

Fifty Trees

USA – The Cider Industry and Craft

b) Modern/New-to-market craft ciders (cont'd)

They do, however, also consist of strong regional brands such as the ones below who may have started in their own regions, have gained strength in those regions against the national brands and who have started to branch out into other areas through a state-by-state rollout.

USA – The Cider Industry and Craft

c) Imported craft ciders

An interesting development is the reported preparation of BrewDog USA (a subsidiary of UK craft brewer BrewDog who has had success with both its products and branded on-premise) to launch Hawkes in the USA but as a **locally-blended product**, a hybrid between imported bulk Hawkes from the UK and US cider.

Other brands style themselves as domestic product (eg E. Krispers by Baltimore's Heavy Seas Beer) but are actually **contract-packed abroad** (in this case, UK).

Other imported brands are few and far between – with the largest being Rekorderlig, potentially being considered a craft product given its Swedish-ness within the American context.

HAWKES
— LONDON —

REKORDERLIG
CIDER

USA – The Cider Industry and Craft

d) Traditional farmhouse producers

Longstanding producers who have serviced their local communities for many years and occasionally break out to the wider world through cider festivals or enterprising retail and/or pub chains running themed weeks. They are, however, far less "farm" orientated as, for example, the UK equivalents. It is increasingly difficult to discern these from 'modern' ciders as imagery and positioning even for established brands is constantly upgraded to keep track of/compete with new regional market entrants who may have started their life in other regions and are starting to branch out. Some of these are interesting to foreign investors – such as Seattle Cider Co acquired by French giant Agrial.

PENNINGS FARM CIDERY WARWICK, NY

IWSR

USA – The Cider Industry and Craft

e) US Craft Market Size

It is argued by the various craft cider associations in the US that only Boston Beer Co/Angry Orchard, AB InBev, MillerCoors, Heineken and C&C *cannot* be counted as 'craft cider', with the remainder of the market falling into the definition. Arguably, however, there are some brands of these multinationals that should, indeed, be counted to having a craft profile – AB InBev's Virtue and Johnny Appleseed, as well as C&C's Vermont cider specifically.

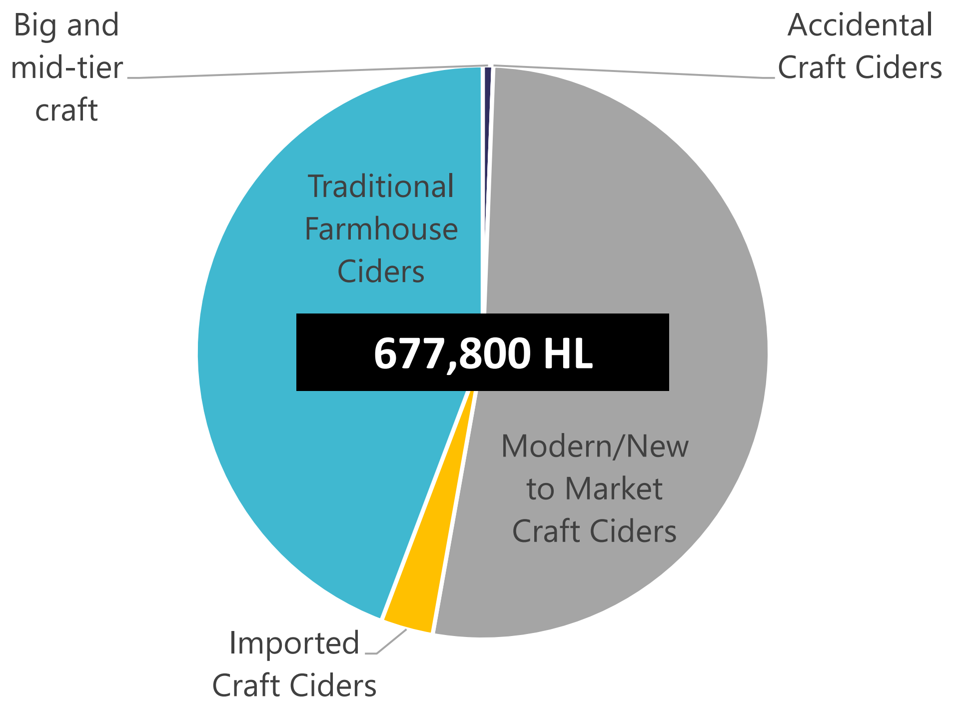
This would size the craft cider market remarkably closely to that of the UK, at **677,800 HL** in 2018, or around 30% of the total market for cider. While this is a substantial proportion – much higher than in the UK - this falls into line with retail audit estimates that say only about two thirds of the US market is accounted for by national brands, with regionality basically equated with craft.

The market for these craft ciders has grown in recent years, in contrast to a fluctuating market overall. Craft cider is seen to be rescuing the overall category, notably through a much-needed modernisation of what used to be seen as a stale beverage alcohol sector.

USA – The Cider Industry and Craft

e) US Craft Market Size (cont'd)

Craft Cider: '000 HL	**2018**
Big and mid-tier craft	4
Accidental Craft Ciders	-
Modern/New-to-market Craft Ciders	354
Imported Craft Ciders	20
Traditional Farmhouse Ciders	300
Craft Cider Market	**678**



Notes:
- **Big and mid-tear:** Brands owned by multinationals – Virtue, Johnny Appleseed, Vermont, limited in size
- **Accidental:** Does not apply in the US context
- **Modern/New to Market:** Brands positioned as competing with modern craft beer and RTD mixed drinks brands, often governed by extensions of brewers and RTD companies. This is definitely the growth area.
- **Imported:** Fairly modest part of the market, growing perhaps with some innovative products like the new Hawkes hybrid
- **Traditional:** A mature market starting to be usurped by modern and new-to-market brands, or whose established brands are receiving a makeover thatt qualifies them to become 'Modern'.

USA – Applicable Duties, Tariffs and Other Regulations

Under AUSFTA provisions it is believed that Australian cider can enter the United States **free of trade tariffs**.

Taxation, however, applies to all products (whether domestic or imported) and varies state-by-state. There is a warren of regulations regarding distributorship licenses, excise duties, state sales taxes and sometimes even county/city sales taxes applicable for cider products, with varying levels of complexity but certainly no uniformity.

At federal level the Tax and Trade Bureau of the US Treasury is in charge. It has issued a helpful guide/FAQ on alcohol taxation and other regulations with a dedicated section on cider – see following link, which is frequently updated:

https://www.ttb.gov/resources/faqs/alcohol#Cider

State-by-state rules on excise rates are summarised in the US Association of Cider Makers' factsheet on the following link. Note that even their basis varies widely – some are calculated as a percentage on value, some as a flat fee per gallon or litre, some follow wine or beer rules.

https://ciderassociation.org/wp-content/uploads/2018/10/Cider_50-State_Survey_of_Regs.pdf

State-by-state rules on sales taxation – including state, county and city taxation – are frequently updated on www.tax-rates.org

US – Price Comparisons

A margin build-up may look as follows (example based on Angry Orchard – 6 x 12oz case) – **Off-premise** in four key consumption states. Note particularly the divergence between New York and Florida re sales taxation/excise levy.

OFF-PREMISE PRICE BUILD-UP PER LITRE		California	Texas	Florida	New York
Price to consumer	LC/l	4.34	4.06	4.31	5.62
City Sales Tax Rate	%	2.75% (max)	2.0% (max)	2.0% (max)	4.875% (max)
City Sales Tax Amount	LC/l	0.11	0.08	0.08	0.25
State Sales Tax Rate	%	6.0%	6.25%	6.0%	4.0%
State Sales Tax Amount	LC/l	0.24	0.23	0.24	0.21
Price before Sales Tax	LC/l	3.99	3.75	3.99	5.16
Trade margin %	%	30%	30%	30%	30%
Trade Margin Amount	LC/l	0.92	0.87	0.92	1.19
Price ex Margin	LC/l	3.07	2.88	3.07	3.97
Tariff	LC/l	-	-	-	
Excise	LC/l	0.05 ($0.20/gallon)	0.05 ($0.20/gallon)	0.24 ($0.89/gallon)	0.01 ($0.04/gallon)
Net selling price	LC/l	3.02	2.83	2.83	3.96
Average price to consumer	% RSP	100%	100%	100%	100%
Sales taxes	% RSP	8%	8%	7%	8%
Trade margin	% RSP	21%	21%	21%	21%
Tariff	% RSP	-	-	-	-
Excise	% RSP	1%	1%	6%	Neg
Net selling price	% RSP	70%	70%	66%	71%

Note: state-by-state prices before sales tax as per www.wine-searcher.com

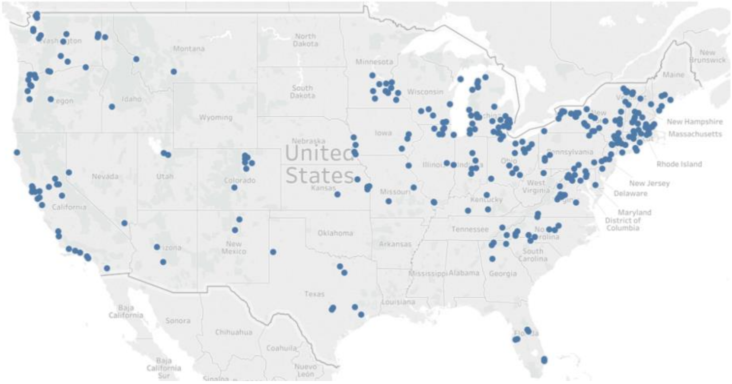
US – Price Comparisons

On-premise follows the same logic. For New York and Florida, the margin build-up is as follows, based on an average price of US$6 per US draught pint ($12.68/litre) in a typical sports bar **including** sales tax:

ON-PREMISE PRICE BUILD-UP PER LITRE		Florida	New York
Price to consumer	LC/l	12.68	12.68
City Sales Tax Rate	%	2.0% (max)	4.875% (max)
City Sales Tax Amount	LC/l	0.23	0.57
State Sales Tax Rate	%	6.0%	4.0%
State Sales Tax Amount	LC/l	0.70	0.47
Price before Sales Tax	LC/l	11.74	11.65
Trade margin %	%	70%	70%
Trade Margin Amount	LC/l	4.83	4.80
Price ex Margin	LC/l	6.91	6.85
Tariff	LC/l	-	
Excise	LC/l	0.24 ($0.89/gallon)	0.01 ($0.04/gallon)
Net selling price	LC/l	6.67	6.84
Average price to consumer	% RSP	100%	100%
Sales taxes	% RSP	7%	8%
Trade margin	% RSP	38%	38%
Tariff	% RSP	-	-
Excise	% RSP	2%	Neg
Net selling price	% RSP	53%	54%

USA – Cider Market Features

- **50 separate local markets for beverage alcohol**
- **The North American cider industry continues to legitimize itself**
  - The Cider Institute of North America (CINA), which formed in 2016, has announced in February 2019 the launch of the Advanced Certificate in Cider & Perry Production.
- **Heightened experimentation occurring, similar to craft brewers and distillers**
  - The 'outside the box' approach to product development is capturing consumer interest
  - Stowe Cider's 'Brainwaves' experimental ciders are limited innovative releases from co-fermentation to being aged on gummy bears
- **Acquisitions; as competition increases consolidation follows suit**
  - At the local level; Stem Ciders acquired Black Twig Cider House
  - At the international level; in 2016, France-based Agrial acquired Seattle Cider Company. In 2012, Ireland-based C&C Group acquired Vermont Hard Cider Company



USA – Cider Market Trends

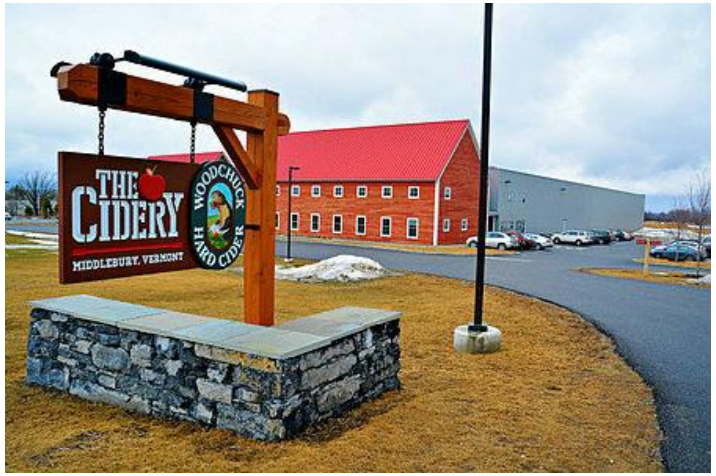
- Current consumer focus is on **trending products** with **much less focus on authenticity** than in neighbouring Canada. No real consumer understanding of varietals, key regions, vintage issues etc.
- Focus is on a **new beverage experience**, moving away from earlier products that were perceived to be overly sweet
- Tight competition with **RTD mixed drinks** (hard seltzers in particular, also hard teas) as well as the **craft end of the beer spectrum** in terms of positioning, brand propositions and route to market
- **Simplicity and transparency** is key
- Naturally **gluten-free**, cider is ideally placed to be offered as a gluten-free alternative to beer
- **Casual** positioning is key as evidenced in rise of rosé ciders, and rise of leading brand Angry Orchard

USA – Relevant/Recent Cider Innovation

Trend Sharing

Leveraging trends occurring within the beer industry

- Sour-Style
- Shandy
- Hazy/Unfiltered (New England IPAs)
- Brut Style (Brut IPAs)
- Destinations/Cider Houses (Brewpubs)
- Barrel-Aging
- Functional Benefits (Probiotic)



USA – Relevant/Recent Cider Innovation

Ciders made using beer yeast

The type of yeast strain to use is a major decision.

- Foraged yeast, or yeast from spontaneous fermentation, can produce funky, wild flavors
- Champagne yeast evokes wine notes; some yeast producers make cider-specific strains that almost guarantee consistent, predictable results.
- **Ale/beer yeast**, is also **growing as a popular choice for cider makers**, as the flavors often play really well with apples, and the **stylistic fusion creates another bridge for craft beer drinkers** to explore the world of cider.

Belgian Abbey Ale yeast

Nine Pin Belgian: reminiscent of top-quality Belgian beers, with notes of tropical fruit, and a smooth creamy mouth feel.

Finnriver Apple Abbey: sweetness from the blend of organic apples helps to amplify the qualities of two Belgian yeast strains: tropical aromas of ripe banana, pepper and clove spice and a nutty, bready finish.

Belgian-style saison yeast

Citizen Cider Wit's Up: super-crisp and easy to drink, starting off reminiscent of an ale, and finishing like a session cider.

Potters Craft Saison: crisp, tart Saison is made with a blend of fresh pressed melon and Virginia apples, and then it's fermented with a fruit-forward Belgian saison yeast.

Common Hibiscus Saison: hibiscus flavors are kicked up with the addition of saison yeast for a dry, fruity, spicy profile.

USA – Relevant/Recent Cider Innovation

Cider-based Cocktails

Overall interest in cocktails are surging

- Producers capitalize on current trends by creating bridge products between categories
- Trending spirit categories for cocktail use include bourbon/rye & Italian Aperitifs (Campari/Aperol)
- Two examples of harnessing this trend include the **cider mint julep** and the **hard cider spritz**
- While few are currently available in pre-made RTDs, **opportunity lies in offering these cider-based prepared cocktails** like the Shacksbury Cider Spritz

Cider Mint Julep

The classic American cocktail typically consisting of muddled mint, sugar and bourbon over crushed ice is enhanced through the addition of 4-6 ounces of hard cider

Hard Cider Spritz

Low-proof cocktails, such as the Campari/Aperol Spritz, are trending. The acidic-zest addition of 3 ounces of dry hard cider compliments the consumer experience.

USA – Relevant/Recent Cider Innovation

CBD-Infused Cider

Cideries and dispensaries are beginning to collaborate

- CBD, one of the cannabinoids found in marijuana plants **provide a mellow mood** without 'high' effects of THC is now commonplace in the US.
- Beginning a few years ago in health food-type applications: tinctures, gummies, oils, skin creams, salves has now turning up in all kinds of creative ways with food and beverage. For example, CBD coffee, CBD ice cream, CBD chocolate, CBD baked goods and smoothies, CBD maple syrup, CBD olive oil, CBD kombucha …**now cider!**

<u>Nano Juice</u>

Cider Creek's Nano Juice is a 2019 release, a **non-alcoholic sparkling cider** made with New York State apples. It contains 10 milligrams of high-quality, organic CBD (sourced from Alaska's High Expedition dispensary) which will shine through without the effects of alcohol.

<u>Stowe CBD Cider Trial 1</u>

The Stowe, Vermont based cidery recently (January 2019) announced it has made its first trial batch of CBD-infused cider**. This 5% ABV dry cider** contains 15 mg. of CBD per 12-ounce serving. The collaborative production was possible in conjunction with Sterling Hemp Farms.