

Boston Beer Company Inc. (SAM: NYSE)

Financial Analysis By: Nicholas Luca – Consumer Goods

Company Profile as of 2/19/2015

Market Price: \$309.61
Industry: Beverages - Brewers
Market Cap: \$4.02B
52-Week: \$208.82 - \$325.00
Beta: 0.25

Source	Target Price	Recommendation
Yahoo Finance	\$316	BUY
Bloomberg	\$319	BUY
Siena	\$291	SELL



Thesis

- Threat of new entrants in an already competitive market
- Diminishing comparative quality of product to competitors
- Loss of brand loyalty
- Unsustainable growth

Company Overview

The Boston Beer Company produces and sells alcohol beverages primarily in the United States, Canada, Europe, Israel, the Caribbean, the Pacific Rim, Mexico, and Central and South America. The company primarily sells their Samuel Adams or the Sam Adams brand

names which contain over 50 different styles. Their portfolio also contains 10 flavored malt beverages under their Twisted Tea brand name and 8 hard cider beverages under the Angry Orchard brand name. It sells its products to a network of wholesale distributors, who in turn sell to retailers, such as pubs, restaurants, grocery stores, convenience stores, package stores, stadiums, and other retail outlets. The Boston Beer Company, Inc. was founded in 1984 and is based in Boston, Massachusetts.

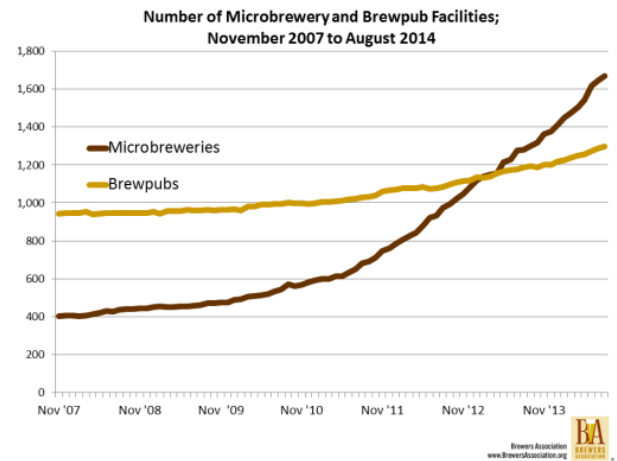
Management

Their management team is led by Founder and Chairman James “Jim” Koch, a graduate of Harvard that left his prior position in a consulting firm to transform a beer recipe, founded by his great grandfather in 1860, into a product. Koch is often credited for popularizing craft beer in the 1980s and 1990s, a time when the alcoholic beverage market was dominated by lighter style, less flavorful beer producers such as Budweiser and Coors. Jim was known as a leader in the marketing aspect of the company, but now at age 65, has less in store presence in retailers and brewpubs. Jim, as a founder of the company, admires the traditional style of craft beer that he grew up on, but unfortunately his ability to adapt to where the market has headed has been relatively slow.

Next on the management team is President/CEO Martin Roper, who recently has been in headlines for selling 10,000 of his shares of the company, lowering his shares of SAM by 90%. Roper has been with the company since 1999, shifting his position from COO to CEO in January of 2001.

New Entrants/Preexisting Competitors

The surge of a richer, more flavorful beer would be said to be started around 2010-2011 in the United States. Although craft beers have been present since the 70's, it wasn't until recently they became a growing percent of the beer industry at roughly 8% currently and expected to be low double digits by the end of 2015, according to founder Jim Koch. A distinction between a craft brewery and a microbrewery is a matter of production numbers, with microbreweries having an annual production of less than 15,000 US beer barrels and craft brewery's producing between 15,000 and 6,000,000 barrels per year. Microbreweries basically have the ability to emerge into craft breweries, a feat that is becoming tougher now because of the increasing competition. The most recent number of microbreweries has been updated to be over 1,700 in the U.S. as of August 2014, a number that is almost double since emergence of craft beer in 2010-2011 which stood at 700 microbreweries.



	2013
Anheuser-Busch InBev	47.5%
SABMiller	14.9%
Molson Coors	14.4%
Constellation Brands	6.8%
Heineken	4.4%
S & P	3.2%
Yuengling	1.6%
Boston Beer	1.4%
Diageo	0.7%
Sierra Nevada	0.5%
Total	95.4%

Source: Euromonitor International

The leaders of the industry understand that craft beer is growing and that although they only currently represent a relatively small portion of the beer industry, there is a lot of growth expected in upcoming years. Market leaders want to eliminate this competition through acquisition. Rather than competing for shelf space, they would rather add them to their portfolio through buying them out at a fairly cheap price, figuring they're fairly new companies. These sought after microbreweries have only been around so long, so for brand acceptance is a huge growth figure when it comes to acquiring them. Essentially, these microbrews are creating and perfecting certain styles that connoisseurs love, a task that these light beer developers struggle with. To compensate with that, rather than trying to create a similar recipe or style, they are merely acquiring the breweries. SAM is up against competitors that are in a much better

position of acquiring these microbreweries. In a \$92 billion U.S. beer industry, SAM represents an inferior percent of the market, as compared to the top three leaders that combined hold 77% of the industry. The top performers are acquiring more and more companies each quarter.

The market leader, Anheuser-Busch InBev has spent the past few years acquiring competing breweries to expand its reach into a growing market. Some of these acquisitions include Chicago's Goose Island for \$38.8 million in 2011, the largest craft beer acquisition ever. Another notable acquisition is of Blue Point Brewery of NY, which was a \$24 million acquisition in 2013. Adding to the buyout of microbreweries, BUD is also buying stake into craft competitors within the industry. They now have 32% stake in Craft Brew Alliance (NASDAQ:BREW), one of the few public craft breweries. If you add up their more popular acquisitions: Blue Point, 10 Barrel, and Elysian, BUD added about 150,000 bbls to its portfolio.

Even though SAM is in a decent position financially to endure some debt in acquiring microbreweries, any brewery worth pursuing can easily be out-bid by the big contenders like BUD. In an industry filled with partnering, there isn't much discussion along acquiring other breweries or partnering coming from discussion with management.

Loss of Brand Loyalty

Rise of local breweries

While Sam Adams once topped leaders like Budweiser as far as quality goes, with the new fast paced growth of local breweries, Sam Adams is now being outdone in quality. What they used to be able to sell themselves as, the highest quality beer, they are now unable to. As stated before, they are adding more and more styles to their portfolio in hopes of competing with the smaller breweries that create all new styles of beer. But this isn't what craft consumers are looking for. They don't want mass produced, mass marketed beers. Beer snobs want to know the quality in the beer they're ordering is superb to the other choice. The assumption is that the local brewery will always be fresher and better in taste as compared to the Sam Adams that you can order at almost any bar or restaurant now. The issue with Samuel Adams is they wanted to get their name in every bar, and with that they are becoming the Budweiser and Coors Light of craft beer now. Their brand is so well known and recognized, of which is great to new customers to the craft market, but for those that have been consumers of craft beer for quite some time are looking at the Sam Adams as a mass produced, better Bud Lite.

These viewpoints are heavily reflected in the ratings all across the web, more specifically in the table below, of which charts Samuel Adams at only the 39th best brewery in the Northeast region. Of the top 25, there are four Boston breweries higher ranked than Boston's very own, Samuel Adams.

	Brewery	Location	↕ # Beers	↕ Avg ABV	↕ SOLID	↕ SOLID%	↕ Avg BAR	↕ BAR25	📊 BAR
1.	Hill Farmstead Brewery	Greensboro Bend, VT, US	74	5.6	68.29	100%	6.0	165.01	444.08
2.	Southern Tier Brewing Company	Lakewood, NY, US	94	7.5	55.12	97%	1.93	127.57	181.4
3.	Jack's Abby Brewing	Natick, MA, US	52	6.3	60.56	100%	3.48	81.35	181.21
4.	Allagash Brewing Company	Portland, ME, US	65	7.7	58.48	100%	2.76	90.06	179.36
5.	New England Brewing Co.	New Haven, CT, US	31	6.5	61.89	100%	4.78	64.19	148.21
6.	Lawson's Finest Liquids	Warren, VT, US	29	6.1	61.08	100%	4.14	59.48	120.04
7.	Maine Beer Company	Portland, ME, US	22	6.6	60.75	100%	4.57	49.69	100.58
8.	Brewery Ommegang	Cooperstown, NY, US	48	7.3	57.92	100%	2.06	45.89	98.79
9.	Brooklyn Brewery	Brooklyn, NY, US	91	7.1	54.03	92%	1.06	78.68	96.4
10.	Tree House Brewing Company	Brimfield, MA, US	18	5.6	69.21	100%	5.18	35.21	93.15
11.	Night Shift Brewing	Boston, MA, US	43	6.1	58.4	98%	1.93	42.45	82.78
12.	The Alchemist Pub & Brewery	Waterbury, VT, US	14	7.5	58.46	93%	5.63	46.24	78.84
13.	Sixpoint Brewery	Brooklyn, NY, US	56	6.0	55.02	96%	1.32	53.36	73.81
14.	Clown Shoes	Ipswich, MA, US	46	9.1	55.41	100%	1.08	33.03	49.88
15.	Barrier Brewing Company	Oceanside, NY, US	37	5.6	56.78	97%	1.34	31.08	49.74
16.	Pretty Things Beer & Ale Project	Boston, MA, US	24	7.6	60.1	100%	2.01	20.94	48.17
17.	Smuttnose Brewing Co.	Portsmouth, NH, US	50	6.6	53.48	96%	0.79	34.89	39.37
18.	SingleCut Beersmiths	East Elmhurst, NY, US	19	5.6	59.09	100%	1.89	16.94	35.89
19.	Peekskill Brewery	Peekskill, NY, US	19	3.5	56.18	100%	1.89	20.78	35.84
20.	Relic Brewing Co.	Plainville, CT, US	18	6.8	59.1	100%	1.8	15.61	32.34
21.	Harpoon Brewery	Boston, MA, US	52	6.0	53.47	100%	0.61	27.26	31.9
22.	Great South Bay Brewery	Bay Shore, NY, US	18	5.8	56.65	94%	1.74	18.3	31.32
23.	Cambridge Brewing Co.	Boston, MA, US	26	5.9	56.19	100%	1.18	17.73	30.8
24.	Portsmouth Brewery (NH)	Portsmouth, NH, US	30	6.1	53.65	93%	1.01	30.89	30.31
25.	Wormtown Brewery	Worcester, MA, US	14	6.5	57.54	100%	2.04	16.58	28.61
39.	Boston Beer Company (Samuel Adams)	Boston, MA, US	133	6.8	50.73	82%	0.08	133.91	11.21

Quality

With these new entrants come new styles of beer. Microbreweries attempt to differentiate themselves from others through developing new styles, or even creating hybrids of two or more styles. This is ultimately leading to thousands of different styles on the market. SAM has been able to diversify, having over 50 barrels of different styles; and also adding the Angry Orchard brand that provides for the new hard cider craved by consumers. They clearly see the rise of new styles, and are attempting to expand their styles rapidly to keep up. However, while SAM is trying to keep up the varieties coming out, they are losing quality within their other styles. They have expanded their Samuel Adams line so much that the quality control is fading. With less focus on each beer individually, they are losing a grasp of their beer quality as a whole. When they first started, Koch with the help of his brew masters perfected their first style, the Boston Lager. This is what got the ball rolling for Sam Adams. They emphasized so much on the precision of making the beer taste great and that was what they were known for. Now, with the vast varieties, the quality just isn't there, and the industries connoisseurs are responding.

Poor Adaption of Popular Styles

On its website, the company writes, "30 years later, we're still brewing for the craft beer revolution with our latest release, Rebel IPA." SAM has realized a demand for the IPA but the authenticity of their IPA is questioned. Koch grew the company through "door to door" sales with his family's coveted recipe. His IPA brand is noted as a "West Coast IPA", with a highly unique and different bottle design. Their addition of a popular style allowed them to compete in the IPA category, but their approach on the style is very questionable compared to what originally grew this company. The bottle also has been critiqued as identical to a competitor's bottle, Punk IPA of BrewDog Brewery. Now even though the IPA segment seems to be gaining popularity at a quick rate, the popularity of Sam Adam's Rebel IPA is actually weakening according to BeerGraphs.com, shifting from 3.5/5 towards a 3.0/5 in 2014.



Unsustainable Growth

Samuel Adams is regarded as the pioneer for craft beer, as it was the first of its kind. Now, after 30 years, they have raised a lot of interest from others, as new entrants are overwhelming the market. In a market where gaining brand acceptance is as easy as developing a good recipe, it is hard for Sam Adams to be the leader in craft beers. Currently, there are record numbers of people entering the craft beer liking. Samuel Adams is almost the stepping stone from light, low-quality beer, to the luxury high end craft beers. They are capitalizing on this shift and ultimately once the number of new consumers starts to slow in pace, they are to suffer severely.

Conclusion

The Boston Brewing Company is a **SHORT** immediately following Quarter 4 earnings of which are released on February 24, 2015, due to historically strong Q4 earnings. SAM is a short because of unsustainable growth due to an immense increase in competitors within the market. Their products are being questioned by the industry's connoisseurs, largely concerning the quality of their product in comparison to their competitors. Although the Better Beer (Craft beer) segment continues to grow, the percent of market share for Boston Beer Company is soon to decline with new competitors establishing acceptance from consumers. With minimal focus on acquiring emerging microbreweries, while market leaders Anheuser Busch InBev (BUD) and Molson Coors (TAP) continue to make acquisitions, SAM is going to have a limited portfolio to sell to distributors, eventually leading to less shelf, cold box and tap space. The reason for past success is heavily due to the rapid growth in the craft beer market, of which they held most of the market share. Now, with over 3,000 breweries in the United States alone, while over half of them are microbreweries, SAM must differentiate themselves, of which will be tough with a fully exhausted product line and limited acquisitions.

CENTER FOR GLOBAL FINANCIAL STUDIES

Boston Beer Co. Inc. SAM

**Analyst
Nicholas Luca
Current Price
\$309.70**

**Intrinsic Value
\$271.19**

**Target Value
\$291.75**

**Divident Yield
0%**

**Target Return
-5.79%**

BEARISH

<u>General Info</u>		<u>Peers</u>		<u>Market Cap.</u>		<u>Management</u>									
Sector	Consumer Staples	Anheuser-Busch InBev SA/NV				Professional	Title	Comp. FY2011	Comp. FY2012	Comp. FY2013					
Industry	Beverages	Molson Coors Brewing Company		\$14,192.04		Koch, C.	Founder and Chairman of the Board	\$ 754,163.00	\$ 817,949.00	\$ 994,313.00					
Last Guidance	Oct-30-2014	Brown-Forman Corporation		\$19,434.68		Roper, Martin	Chief Executive Officer, President	\$ 933,818.00	\$ 1,052,493.00	\$ 1,519,541.00					
Next earnings date	2/24/2015			0		Urlich, William	Chief Financial Officer, Principal	\$ 3,437,998.00	\$ 599,363.00	\$ 617,682.00					
						Lance, Thomas	Vice President of Operations	\$ 693,401.00	\$ 721,454.00	\$ 787,353.00					
						Geist, John	Vice President of Sales	\$ 4,078,189.00	\$ 527,448.00	\$ 597,441.00					
						Wade, Kathleen	Vice President of Legal and Corp	\$ -	\$ -	\$ -					
<u>Market Data</u>		<u>Current Capital Structure</u>		<u>Historical Performance</u>											
Enterprise value	\$3,967.55	Craft Brew Alliance, Inc		\$235.18		SAM		Peers		Industry		All U.S. firms			
Market Capitalization	\$4,024.14	Grupa Zywiec Spolka Akcyjna		\$3,937.00		Growth	27.1%	10.9%	14.1%	6.0%					
Daily volume	0.01	Guangzhou Zhujiang Brewery Co., Ltd		\$9,393.03		Retention Ratio	6.5%	83.8%	96.1%	61.6%					
Shares outstanding	13.06	Royal Unibrew A/S		\$12,252.74		ROIC	295.2%	11.2%	16.4%	11.8%					
Diluted shares outstanding	13.49					EBITDA Margin	12.6%	25.0%	12.5%	13.7%					
% shares held by institutions	63.36%					Revenues/Invested capital	348.1%	55.0%	136.1%	202.3%					
% shares held by insiders	29.93%					Excess Cash/Revenue	9.6%	5.2%	11.1%	18.5%					
Short interest	7.60%					Unlevered Beta	0.72	0.29	0.68	0.95					
Days to cover short interest	12.30					TEV/REV	1.5x	0.7x	1.8x	2.4x					
52 week high	\$325.00					TEV/EBITDA	12.8x	2.2x	11.8x	11.3x					
52-week low	\$208.82					TEV/EBITDA	12.8x	2.2x	11.8x	11.3x					
5y Beta	0.54					TEV/EBITDA	15.4x	2.7x	22.3x	15.4x					
6-month volatility	25.74%					TEV/UFCF	24.1x	2.4x	33.2x	26.8x					
<u>Past Earning Surprises</u>				<u>Non GAAP Adjustments</u>											
	Revenue	EBITDA	Norm. EPS												
Last Quarter	4.3%	0.0%	24.1%	Operating Leases Capitalization		100%	Straightline		10 years						
Last Quarter-1	3.1%	0.0%	5.0%	R&D Exp. Capitalization		0%	N/A		N/A						
Last Quarter-2	2.6%	0.0%	-8.8%	Expl./Drilling Exp. Capitalization		0%	N/A		N/A						
Last Quarter-3	6.3%	0.0%	-10.6%	SG&A Capitalization		0%	N/A		N/A						
Last Quarter-4	8.0%	0.0%	6.5%												
<u>Proforma Assumptions</u>				<u>Forecasted Profitability</u>											
		Period		Rev. Growth		Adj. Op. Cost/Rev		Revenue		NOPLAT		Invested capital		UFCF	
Operating Cash/Cash	0.0%	LTM		27%		79%		\$890.57	\$111.39	\$378.05		\$8.80			
Unlevered Beta	0.70	LTM+1Y		14%		75%		\$1,013.85	\$143.55	\$284.43		\$140.06			
Rev/Invested Capital	280.0%	LTM+2Y		10%		75%		\$1,111.41	\$155.97	\$286.49		\$153.91			
Continuing Period Revenue Growth	3.0%	LTM+3Y		9%		74%		\$1,206.72	\$173.75	\$288.37		\$171.86			
Long Term ROIC	26.9%	LTM+4Y		5%		74%		\$1,272.99	\$184.37	\$289.89		\$182.85			
Invested Capital Growth	Equals to Maintenance	LTM+5Y		4%		74%		\$1,326.16	\$191.48	\$295.69		\$185.68			
Justified TEV/REV	1.0x	LTM+6Y		4%		74%		\$1,376.31	\$198.48	\$298.89		\$195.27			
Justified TEV/EBITDA	8.0x	LTM+7Y		4%		74%		\$1,424.62	\$205.35	\$300.39		\$203.86			
Justified TEV/EBITDA	13.0x	LTM+8Y		3%		74%		\$1,471.79	\$212.15	\$301.49		\$211.05			
Justified TEV/UFCF	18.0x	LTM+9Y		3%		74%		\$1,518.27	\$218.82	\$305.07		\$215.24			
<u>Valuation</u>				<u>Monte Carlo Simulation Assumptions</u>				<u>Monte Carlo Simulation Results</u>							
	ROIC	WACC	EVA	Enterprise Value		Total Debt		Other claims		Equity		Adjusted Price			
LTM	40.4%	6.8%	\$90.54	\$3,421.22		\$0.58		-\$28.28		\$3,448.93		\$272.15			
LTM+1Y	47.8%	7.0%	\$115.91	\$3,445.10		\$0.58		-\$270.42		\$3,714.94		\$292.50			
LTM+2Y	54.8%	7.1%	\$136.36	\$3,538.13		\$0.58		-\$417.56		\$3,955.11		\$310.57			
LTM+3Y	60.6%	7.3%	\$153.58	\$3,626.97		\$0.58		-\$585.69		\$4,212.08		\$330.40			
LTM+4Y	63.9%	7.4%	\$163.49	\$3,707.27		\$0.58		-\$767.66		\$4,474.35		\$350.78			
LTM+5Y	66.0%	7.6%	\$172.60	\$3,791.51		\$0.58		-\$955.50		\$4,746.43		\$372.94			
LTM+6Y	67.1%	7.7%	\$177.20	\$3,874.26		\$0.58		-\$1,155.89		\$5,029.57		\$394.10			
LTM+7Y	68.7%	7.9%	\$182.39	\$3,963.28		\$0.58		-\$1,368.13		\$5,330.82		\$417.58			
LTM+8Y	70.6%	8.0%	\$188.40	\$4,055.19		\$0.58		-\$1,591.21		\$5,645.82		\$442.00			
LTM+9Y	72.6%	8.2%	\$196.16	\$4,149.16		\$0.58		-\$1,822.69		\$5,971.27		\$457.09			
	Base	Stdev	Min	Max		Distribution		Intrinsic Value		1y-Target					
Revenue Variation	0	10%	N/A	N/A		Normal		Mean est.		\$272.15		\$292.50			
Op. Costs Variation	0	10%	N/A	N/A		Normal		σ(e)		\$0.32		\$0.25			
Market Risk Premium	6%	N/A	5%	7%		Triangular		3 σ(e) adjusted price		\$271.19		\$291.75			
Long term Growth	3%	N/A	3%	27%		Triangular		Current Price		\$309.70					
Terminal Value	0	0.1	N/A	N/A		Normal		Analysts' median est.				\$300.75			