02-Nov-2023

Molson Coors Beverage Co. (TAP)

Q3 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and welcome to the Molson Coors Beverage Company Third Quarter Fiscal Year 2023 Earnings Conference Call. You can find related slides on the Investor Relations page of the Molson Coors' website. Our speakers today are Gavin Hattersley, President and Chief Executive Officer; and Tracey Joubert, Chief Financial Officer.

And with that, I'll hand it over to Greg Tierney, Vice President of FP&A, Commercial Finance and Investor Relations.

Greg Tierney

Vice President of FP&A and Investor Relations, Molson Coors Beverage Co.

All right. Thank you, Brita, and hello, everyone. Following prepared remarks today from Gavin and Tracey, we will take your questions. In an effort to address as many questions as possible, we ask that you limit yourself to one question. If you have technical questions on the quarter, please pick them up with our IR team in the days and weeks that follow.

Now today's discussion includes forward-looking statements. Actual results or trends could differ materially from our forecast. For more information, please refer to the risk factors discussed in our most recent filings with the SEC. We assume no obligation to update forward-looking statements. GAAP reconciliations for any non-U.S. GAAP measures are included in our news release. Unless otherwise indicated, all financial results the company discusses are versus the comparable prior year period in US dollars and in constant currency when discussing percentage changes from the prior year period.

Also, US share data references are sourced from Circana. Further, in our remarks today, we will reference underlying pre-tax income, which equates to underlying income before income taxes on the condensed consolidated statement of operations.

And with that, I'll hand it over to Tracey.

Tracey I. Joubert

Chief Financial Officer, Molson Coors Beverage Co.

Thank you, Greg, and hello, everyone, and thank you for joining us. We will be doing things a little bit differently this quarter. I will open and address our results, our guidance, and importantly, our fourth quarter expectations at the start of the call. And then Gavin will close.

In the third quarter, we delivered another set of strong results. Our net sales revenue grew an impressive 11%, driven by double-digit growth in both our business units.

Our continued focus on efficiencies and cost savings, combined with volume leverage, significantly offset inflationary pressures resulting in meaningful margin expansion. This led to 43.5% growth in underlying pre-tax income with both business units up strongly. And with free cash flow nearly doubling for the first nine months of the year, we continue to prudently execute our capital deployment plan, investing in our business, reducing net debt and returning cash to shareholders.

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This performance underscores the strong momentum in our business, which is a function of the foundation we have built to sustainably grow both the top and bottom line. And this is exactly what we have done both in 2022 and year-to-date in 2023, all while navigating a challenging and dynamic global macroeconomic environment.

And while these macro conditions remain, the fundamental strength of our business, coupled with the actions we are taking to sustain the momentum we have achieved gives us confidence for another year of growth in 2023 and beyond.

For 2023, we are reaffirming our high single-digit top line growth guidance, but narrowing our expectations to the high end of that range. And we are raising our underlying pre-tax growth guidance to 32% to 36% as compared to 23% to 26% previously. We are also reducing our interest expense guidance to $210 million, plus or minus 5% as compared to $225 million plus or minus 5% previously. All other previous guidance metrics as detailed in today's earnings release remains unchanged.

There are a few key reasons for these guidance changes. First, the US beer category has been healthier than we had projected when we revised guidance on August 1. In other words, its rate of decline is better than we had expected and better than it was earlier this year.

Second, our brand volume growth is stronger than we had expected. In fact, we anticipate our global brand volume growth to accelerate in the fourth quarter. Third, pricing across our global markets and in particular, in Canada, has been better than we had planned. And fourth, due to higher-than-expected cash balances, we now anticipate lower net interest expense.

Okay. With that in mind, let's discuss the fourth quarter. Our updated full year 2023 guidance implies mid-single-digit top line growth and at the midpoint, a high single-digit decline in underlying pre-tax income for the quarter.

Now the fourth quarter growth rates do not imply a reversal in the trend for our brands in the US. In fact, our October brand volume performance is currently outpacing our trends in the third quarter, and we expect continued share growth roughly aligned with what we saw in the third quarter. In short, we are not seeing anything that suggests that our market share gains are slowing.

So let's talk about some of the key factors driving fourth quarter performance. First, we will experience a reduced level of pricing benefit in the US and EMEA and APAC. For example, we are lapping an approximate 5% general increase in the US. This fall, as anticipated and as supported by the strength of our brands, we took pricing in many of our US markets in the 1% to 2% historical average range.

Second, we expect our US brand volume to outpace financial volume growth in the fourth quarter, and this is due to a couple of reasons. We ended the third quarter with healthy US inventory levels. This was due to our strong brewery performance, which enabled us to ship ahead of expectations in the quarter. And this put us in a great position in the fourth quarter, providing the opportunity to give our employees some much deserved time off around the holidays. And it also allows us to execute planned downtime in the US network for system maintenance. Overall, we expect to be well positioned to build inventory in the first quarter ahead of peak season.

Also recall, we have a large US contract brewing agreement winding down ahead of its termination at the end of 2024. We continue to expect volume declines under this contract to accelerate in the fourth quarter, resulting in a quarterly headwind of approximately 2% to 3% in Americas' financial volume.

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Third, underlying COGS per hectoliter is expected to be a headwind in the fourth quarter. This was due to continued high inflation in EMEA and APAC and lower volume leverage than in the previous two quarters.

And fourth, we expect total MG&A to be up approximately $90 million, which is driven by both marketing and G&A. For marketing, this includes approximately $50 million higher spend in the fourth quarter. And this increase is particularly impactful in a lower profit quarter like the fourth quarter. G&A is expected to be up primarily due to higher incentive compensation given our strong performance this year.

Okay. So now let's talk about our third quarter performance. We delivered another quarter of strong results with net sales revenue growth supported by both rate and volume. Net sales per hectoliter grew 7.6%. This was driven by positive global net pricing, given the rollover benefits from the higher than typical increases taken in the fall of 2022, as well as favorable sales mix led by geographic mix. This geographic mix was due to particularly strong performance in the US.

In fact, consolidated financial volume increased 3.2%, while US shipments were up 7.2%. This was a result of our strong US brewery performance, which enabled us to ship ahead of our expectations, but also it was due to the continued strong momentum behind our premium brands.

Consolidated brand volume increased 1.1% with results varying by market. Americas' brand volume was up 3.6%. Growth was led by the US, where brand volume was up 4.5%. In fact, Coors Light and Coors Banquet were each up double digits, and Miller Lite was up high-single digits. But there were some notable timing impacts that masked the underlying strength in the US brand volume growth.

First, there was one less trading day in the quarter. On a trading day adjusted basis, US brand volume growth was 6.1%. In addition, we were cycling significant load in ahead of the 2022 forecast increases. And there was some shifting of calendar and holiday timing as compared to the prior year, which had an impact.

Canada brand volume increased 0.2%, benefiting from growth in its above-premium portfolio. While industry softness weighed on brand volume, we continued to grow share in Canada for the quarter, adding over 3 share points for the three-month period ending August. In Latin America, while mix improved, brand volume was down 2.5%. This was largely due to industry softness and economic conditions in some of our key markets in the region.

And in EMEA and APAC, brand volume declined 5.2%. The consumers in Central and Eastern Europe continued to be affected by inflationary pressures and UK demand was impacted by rainy weather. That said, our above-premium portfolio continued to benefit from strong growth from Madri, which grew brand volume over 50% in the quarter.

This strong top line performance translated to even stronger bottom line results, and this was across both business units, with underlying pre-tax income up 32.2% in Americas and up 58.1% in EMEA and APAC. We achieved this by prudently managing costs while continuing to invest strongly behind our brands. So, let's talk about some of these drivers.

Underlying COGS per hectoliter were up 2.6%. As expected, inflationary pressures continued to be a headwind, but moderated from the first half of the year. But the story differs by market. In the Americas, underlying COGS per hectoliter decreased 1% as cost savings, volume leverage, and lower logistics costs more than offset the impact of direct material inflation. While in EMEA and APAC, inflationary pressures remained significant, driving underlying COGS per hectoliter up 15.8%.

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To break down the drivers a bit more, as you may recall, we bucket COGS into three areas: first is cost inflation other, which includes cost inflation, depreciation, cost savings, and other items; second is mix; and third is volume leverage or deleverage. The cost inflation bucket drove over 85% of the increase and was mostly due to higher materials and manufacturing costs, partially offset by cost savings. The impact of volume leverage had an 80 basis points benefit in the COGS per hectoliter in the quarter. Other COGS per hectoliter drivers included mix, which accounted for the remainder of the increase and was largely due to geographic mix.

Underlying marketing, general and administration expenses increased 11.6%. About half of the planned incremental $100 million in marketing spend in the second half of 2023 was in the third quarter, and it largely went to supporting the momentum of our core brands. Our investment is focused on retaining our existing drinkers and attracting new ones, including using addressable channels or places, where we can use data to more precisely target them. And further, we continue to strongly invest behind live sports. Based on our brand health and shared performance, we believe that this investment is working.

Also, general and administration expenses were higher. This was primarily due to incentive compensation expenses, which is a variable expense tied to our operating performance. And as you have seen, it's been a very strong year.

Turning to capital allocation. Our priorities remain to invest in our business to drive sustainable top and bottom line growth, reduce net debt as we remain committed to maintaining and, in time, improving our investment-grade rating and return cash to shareholders. With our greatly improved financial flexibility, we now have increased optionality among these priorities and we will utilize our models to determine the best anticipated return for our shareholders.

Looking at these priorities. First, we continue to invest in the business with paid capital expenditures of $494 million for the first nine months of the year. This was down slightly due to the timing of capital projects. Capital expenditures continue to focus on our Golden Brewery modernization and expanding our capabilities to drive efficiencies, cost savings and sustainability initiatives.

And second, we made further progress in reducing our net debt. We ended the quarter with net debt of $5.4 billion, a decline of $584 million since December the 31, 2022. This was supported by our July cash repayment of our CAD 500 million debt upon its maturity on July 15.

As a reminder, our outstanding debt is essentially all at fixed rates. Our exposure to floating rate debt is limited to our commercial paper and revolving credit facilities, both of which had zero balance outstanding at quarter end.

Given our strong EBITDA performance and lower net debt, our net debt to underlying EBITDA ratio declined to 2.2 times. This is in alignment with our long-term goal of under 2.5 times. And I would like to add that in October, S&P Global upgraded its risk rating for Molson Coors to BBB from BBB-.

And that brings me to our third priority, returning cash to shareholders. We paid a quarterly cash dividend of $0.41 per share and maintain our intention to sustainably increase the dividend. And as announced at our Strategy Day on October the 3, our board authorized a new share repurchase program of up to $2 billion over the next five years. It replaces and supersedes the repurchase program previously approved by the board in the first quarter of 2022.

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The new program is intended as a mixture of sustained and opportunistic purchases as part of our balance and cohesive approach to prioritizing capital allocation intended to improve shareholder value creation.

In summary, we are extremely pleased with our third quarter performance and confident in our ability to sustainably deliver top and bottom line growth in the years to come.

And with that, I'll turn it over to you, Gavin.

Gavin D. K. Hattersley

President, Chief Executive Officer & Director, Molson Coors Beverage Co.

Thank you, Tracey. In the third quarter, we continued the growth trajectory that we've been on for nearly two full years. In the quarter, each of our top three global markets are growing net sales revenue, volume, share, or all three. In the US, our shipments were up over 1 million hectoliters compared to the third quarter of 2022, and we were the top volume share gainer in the industry.

Coors Light and Miller Lite are on track to collectively deliver net sales revenue growth for the third straight year, something they had not done since Miller and Coors came together in 2008.

Coors Banquet volumes were up nearly 30%. Coors Light volumes were up double-digits and Miller Lite volumes were up high-single-digits. We were the top dollar share gainer in the US economy segment. In fact, our two biggest economy brands grew dollar and volume share of industry in the quarter. We have gained the second most US share of flavored alcohol beverages of all major brewers.

We grew share nationally in Canada, in every region of the country and in every segment of our industry. Coors Light widened its position as the number one light beer in the country, a position it has held since March.

And the Molson brands grew share. Miller Lite grew volumes by 50%, and we grew more share in flavor alcohol beverages than any other company in the industry. We were the best-performing brewer in the UK in both value and volume share. And in some very exciting news from the UK market, we are now the number two brewer in London after ranking a distant number five player only a few years ago. The transformation of our portfolio in the London market is a real testament to our team's commitment to a clear strategy that drives focus across all channels and customers.

Additionally, Madri is now the second largest above-premium lager in the on-premise and third largest world beer in the total trade across the UK. And in Central and Eastern Europe, Ožujsko, our core power brand in Croatia is growing value share of the beer category year-to-date, and it has over 50% value share of the core segment.

Now of course, our business has benefited greatly from the broader dynamics of the US beer industry over the past seven months. But as you can see, the improvement in our business is being driven by more than one market. The improvement in our business is being driven by more than a couple of brands. The improvement in our business is being driven by more than one segment of the category. And the improvement in our business predates April the 1.

Year-to-date, each of the top three biggest global markets are growing net sales, revenue, volume and volume share. And as this slide clearly shows the trajectory of our business has been on the upswing.

And in regard to our future, we believe we can lap these results in 2024. We delivered top and bottom line growth in 2022. We're on track to do so again this year and we plan to do so next year, too. That's the plan we outlined at

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our Strategy Day last month. We've already gained thousands of tap handles across the US since the beginning of the second quarter. We are already gaining significant amounts of shelf space this fall as retailers work to adjust their space to meet consumer trends.

Now I have seen some, let's say, interesting commentary around shelf space. So I want to be extra clear here. The vast majority of chain retail accounts typically update their shelf space once a year due to the complexity of aligning all their stores and they typically do so in the spring. Over 50 retailers have made space changes in late summer or fall due to the massive shift in consumer purchase behavior we have seen since April the 1. This is not common.

In fact, in the last five-plus years, we haven't had any adjustments in the summer or a change to the premium segment in the fall. Among the chains that moved their resets up to the fall, Molson Coors was the biggest beneficiary with Miller Lite and Coors Light gaining 6% to 7% more shelf space. For brands of this size, that is a massive amount of space. In fact, it's tens of thousands of cubic feet of space.

Regardless of how some folks might characterize the current environment, those are the facts. The conversations for spring resets are well underway. And while we can't exactly predict the future, it's safe to say that we expect to gain more shelf space for our big brands in those resets as well. These retailers are smart business people. And when consumer trends shift to the degree they are shifting, chain retailers have 2 options, change shelf space allocations to meet the trends or leave money on the table. And they're not going to leave money on the table. It's as simple as that.

We'll have more to say about 2024 on our fourth quarter call in February. But between the work we have done to improve our business trajectory and the current dynamics in our industry, we feel confident in this year, confident in our ability to grow next year and confident in our ability to grow in the years ahead.

And with that, we'll take your questions.

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QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] We now have Lauren Lieberman of Barclays. Your line is open.

Lauren R. Lieberman
Analyst, Barclays Capital, Inc.

Q

Great. Thanks so much. Good morning. I was just curious if you could talk a little bit about going back to the beginning of the call, Tracey's comments and in the release on the beer category in the US being stronger than what you had previously expected. So any color you can add on that would be great. Kind of what do you think some of those key drivers are? Is it around key consumer cohorts? Just color on the beer industry backdrop would be great. Thank you.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

Thanks, Lauren. Look, I mean, in Q1, the industry was down 2.7%. In Q2, it was down 2.5%. And in Q3, it was down 1.3%, that's in the USA, obviously as per Circana, so an improvement. And as Tracey said, that wasn't the level of improvement that we were expecting to see. And obviously, Hard Seltzers are still a big part of that decline.

Certainly, while some buyers are switching categories, and certainly, our data says that some drinkers have left within the category, we're gaining share, Miller Lite, Coors Light are healthy and growing share strongly. And that share has been stable for the last 25 weeks. It's a structural change to the industry, that is sticking, whether you look at it on a one-week basis, a four-week basis, a 13-week basis, or a 26-week basis, it has stuck.

Tracey I. Joubert
Chief Financial Officer, Molson Coors Beverage Co.

A

Next question, operator?

Operator: Thank you. We now have Bryan Spillane of Bank of America.

Bryan D. Spillane
Analyst, BofA Securities

Q

Hey. Thanks operator. Good morning, everyone. So Tracey, I guess, I had just a question – two questions around cash flow. One is, I know we took the pre-tax profit or the – I'm sorry, the profit after tax guide up, but you left the free cash flow range. So I guess, it's just – why not, I guess, a higher conversion on free cash flow and then – or on cash flow?

And then second to that, just again, you've got some cash hanging around and the stocks performed the way it has. So just any thought – any way we should be thinking about whether or not you'd put some of that cash to work to buy back shares?

Tracey I. Joubert
Chief Financial Officer, Molson Coors Beverage Co.

A

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Yeah. Thanks, Bryan. So look, the free cash flow range that we gave was already quite wide. So we're comfortable just leaving it where it is. In terms of capital allocation, look, our priorities haven't changed. It's those three buckets that we speak about. It is investing in our business to drive the sustainable long-term top and bottom line growth. And that could be investment in our breweries or from an M&A point of view, the sort of string of pearls approach. We will continue to reduce net debt with a desire to improve our investment-grade rating.

And as I remarked, we did get an upgrade from S&P and then returning cash to shareholders. So we did announce the $2 billion – up to $2 billion share repurchase plan over the next five years. And we'll consider all of those things. I think the good thing is that with our strong free cash flow delivery, we do have optionality as to how we can balance the allocation of capital behind these priorities. But as always, we'll run all of the ideas through our models and make sure that we're investing – where we are driving the higher return for our shareholders.

Operator: Thank you. We now have Andrea Teixeira of JPMorgan.

Andrea Teixeira
Analyst, JPMorgan Securities LLC

Q

Thank you. I was just going to talk about a little bit of the share of voice. And I think you in the Analyst Day, you obviously discussed that against the incremental spend this year. Is there any KPIs you can talk about as you're tracking the development of the incremental spend? And if there is anything, I know most of that $90 million, I believe, incremental spend for, if I'm not mistaken in the quarter, it's mostly compensation, but wondering if it's going to reaccelerate even further in the fourth quarter, so it sets you up for 2024.

And on that, I was just trying to – Gavin, you mentioned that your market share continues to be solid. I think one of your main competitor talking about Bud Light recovering a bit. I know, obviously, from a variable base, anything you would be expecting to see. And I understand, obviously, you may not count on that being – or that share gain being structurally 100%, but most of it could be. So, I was wondering if you can comment a little bit more on the market share performance that is baked in your outlook for next year. Thank you.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

Thanks, Andrea. Look, from a marketing point of view, we're focused on the quality and effectiveness of our marketing spend versus the sort of level of spend that drive the best returns. And we certainly try and make sure that every single dollar counts. We've got great tools that we've had for a number of years, which evolve and they're designed to make sure that we get the required marketing effectiveness. We know which creative assets are working hardest and which channels are working hardest for that. So, we're going to continue to put the right commercial pressure behind our brands to support the momentum.

I just want to maybe correct you on one thing, right? So, the extra $90 million in the fourth quarter, there's about $50 million of that is the marketing. And that's part of the $100 million we said we were going to spend on extra marketing in the second half of the year. So, we spent half of that in the third quarter behind really big beer drinking occasions like football, which we'll do again in the fourth quarter. And then, obviously, a large component of what's left is, as Tracey said, the employee-related costs.

Look, as far as share gains are concerned, our share position has been stable for the last 25 weeks. It's a structural share change to the industry that we believe is going to stick. And yes, I know there's been a lot of noise about trends changing and whether these results are sticking. So, let me just share the facts and these aren't our facts, this is Circana, and the fact is total share for Coors Light and Miller Lite has stuck over the past seven

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months, through the latest four weeks of track channel data on a dollar change basis, Coors Light and Miller Lite both continue to put up double-digit growth. And at the same time, Bud Light has lost just under $3 share points. The overall portfolio for our biggest competitors lost under $5 share points. And that's consistent if you look at the four-week data, the 13-week data, and the 26-week data.

In fact, Bud Light's actually getting worse. The brand's dollar share lost over the last four weeks was more than any four-week period this year. And as I said, these aren't – I mean, this isn't a poll or a possibility, right? This is the fact as laid out in Circana, and we believe that the strength is going to continue into 2024, and we are very confident in the position of our core brands in both the US and, obviously, in Canada.

We've got a very clear plan on how to keep these share gains. We presented it to our distributors at our fall National Distributor Convention. We showed our plans. And honestly, the energy around our plans is something I have not seen, not only for Miller Lite and Coors Light, but for everything. We had a 95% positive score from our distributors. That has never happened. And we laid out a clear acceleration plan at our Strategy Day on how we're going to retain the share gain. So, yes, we believe we can retain this share that has proven to be extremely sticky on every measure that we look at.

Operator: Thank you. We now have Peter Grom of UBS.

Peter Grom
Analyst, UBS Securities LLC

Q

Thanks, operator, and good morning, everyone. Hope you're doing well. So, I was hoping to get some thoughts on just kind of the underlying COGS per hectoliter, which was kind of the lowest year-on-year increase in quite some time. Maybe just first, can you just help us understand what's embedded in the guidance for the fourth quarter?

I think you mentioned an increase in underlying COGS due to high inflation in EMEA and APAC. Is that just an increase year-on-year? Or is that an increase sequentially versus what we just saw in 3Q? And I know we're going to get more details on 2024 in February, but maybe you can just give us some insight in terms of how you're thinking about some of the key cost buckets based on what we can see today? Thanks.

Tracey I. Joubert
Chief Financial Officer, Molson Coors Beverage Co.

A

I'll take that. So, yeah, look, we did say that we expect inflation to continue to be a headwind for us in the back half of the year, but to moderate. Now, as it relates to Q4, we do expect our COGS per hectoliter to be a headwind. And this is because of the continued inflationary pressure in EMEA and APAC region, where we've seen continued inflation in the double-digit range.

But the other drivers of our Q4 COGS per hectoliter would be our lower volume leverage in Q4, lower than Q3 and Q2, for those reasons that we spoke about coming out of Q3 and into Q4, and then also expecting our brand volume to outpace the financial volume growth. Also, we've got higher planned maintenance costs in the fourth quarter, so those would be the big drivers of COGS per hectoliter in Q4.

Operator: Thank you. We now have Bonnie Herzog of Goldman Sachs.

Bonnie Herzog
Analyst, Goldman Sachs & Co. LLC

Q

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Morning. I guess, I wanted to ask a little bit about your MG&A expense. Could you maybe talk a little bit more about the areas where you're going to be investing incremental marketing dollars as you kind of talk through the end of the year? And then should we think about you continuing to invest at a higher rate as we think about next year to support your brands and the growth that kind of Gavin, you mentioned in the stickiness. Just trying to think about or trying to hear how you're thinking about this? Thank you.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

Thanks, Bonnie. Yeah. Look, without giving a complete look under the tent for competitive reasons, obviously, we're going to continue to drive strong pressure in the market with our very effective campaigns have made to chill with Coors Light and taste like Miller Time. We've got significant increases planned and already executed in the third quarter and also in the back half of this year, especially behind the high beer consumption moments like football is.

We're also going to leverage targeted media and digital tactics to retain the new drinkers, which we've got into our brands, primarily Coors Light, Miller Lite and Coors Banquet. We've also got some innovation that's coming in the fourth quarter. Blue Moon non-alc, is launching in December, so we're ahead of the dry January timeframe. And we're going to invest to make sure that we get more space in store, so whether that's continuing to capitalize on the share that we've gained of displays, we've gained more than any other major brewer.

We're going to invest in appropriate areas to make sure that our retailers understand that the incremental shelf space and the tap handles that we're getting, that we're going to support that with strong marketing. And then we're going to invest in our EMEA/APAC business, particularly behind brands like Madri, Carling, and Ožujsko. So those would be the general directions and themes, Bonnie.

Bonnie Herzog
Analyst, Goldman Sachs & Co. LLC

Q

All right. Thank you.

Operator: We now have Filippo Falorni of Citi.

Filippo Falorni
Analyst, Citigroup Global Markets, Inc.

Q

Hey. Good morning, guys. I had a question on...

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

Morning.

Filippo Falorni
Analyst, Citigroup Global Markets, Inc.

Q

...your US brand volumes even on an adjusted basis, the 6.1% that you quoted, it still looks below what we've seen in track channel data. So maybe can you comment on the performance in on-track, on-premise and other smaller off-premise retailers?

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And then thinking about Q4, you mentioned you expect brand volume to accelerate but you're planning to ship below brand volumes. It didn't seem like the over-shipment in Q3 was that large? So maybe you can comment on where inventories are in the distributor channel that would be helpful as well. And whether we should think, if you don't ship over in Q4, should we see a catch-up in Q1 of next year? Thank you.

Gavin D. K. Hattersley A
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

Thanks, Filippo. Tracey, do you want to take the shipment question and I'll take the sort of Circana or Nielsen number difference between ours and what you're seeing in track channels.

I would say there's probably three big differences between the number we disclosed and the track channels, you highlighted one of them, which is the trading adjustment. But then the other one is obviously the significant loading that took place at the end of the third quarter last year, which obviously we didn't have this year, because we had that large price increase last year.

And from a track channel's point of view, that measures consumer behavior, whether our brand sales represent sales that our distributors put into the retail stores. So the retailers would be buying ahead of the price increase that doesn't necessarily mean that the consumer is buying ahead of the price increase. And those would be the two biggest differences between those two numbers, Filippo. From a shipments point of view, Tracey, do you want to take that?

Tracey I. Joubert A
Chief Financial Officer, Molson Coors Beverage Co.

Yeah. So look, we've spoken about our expectations for our brand volume to exceed our financial volume and really that's because of the healthy inventory levels that we ended Q3 on – which enabled us to ship ahead of our expectations. So just in terms of our inventory levels, like coming out of Q3 and even today, we are at higher inventory levels than we saw in the prior year. So again, we feel very comfortable with the inventory levels going into Q4, coming out of Q4 and being able to have inventory levels healthy too – as we go into peak selling next year.

Operator: Thank you. We now have Vivien Azer of TD Cowen.

Vivien Azer Q
Analyst, TD Cowen

Hi. Yeah, over the course of...

Gavin D. K. Hattersley A
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

Hi, Vivien.

Vivien Azer Q
Analyst, TD Cowen

...good morning. The earnings season thus far, we've heard some cautious commentary from some of your peers around negative mix shift, shifting to smaller sizes, some weakness in the lower income consumer more broadly. Student debt repayments obviously came October 1. I know you guys probably hesitant to comment on intra-quarter trends. But I was just wondering, Gavin or Tracey, [audio gap] (00:39:09) perspective on whether you're

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seeing similar dynamics where there might be [indiscernible] (00:39:15), spending more choiceful spending? Thanks.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

Yeah. Thanks, Vivien. You broke up a little bit there, but I think I got the gist of your question. From an overall consumer health point of view, we do remain cautious given the macroeconomic environment that is out there. We're particularly cautious in Central and Eastern Europe, which has been pretty consistent with our view for a while, right? I mean the tough economy, the high inflation has impacted our Central/Eastern Europe business much more than our UK business, which is honestly more weather-related. We do, though, expect conditions to improve as inflation falls in Europe, and we are starting to see inflation falling there.

In Canada, we are seeing softness. It's a tough economic environment out there. We're particularly pleased with our own performance in Canada, where we've really grown strongly. And actually, our share growth in Canada is higher than it is in the United States. In March, Coors Light took over as the number one light beer and has maintained that position and even Molson's growing share of industry volume and NSR. In the US, we're still seeing premiumization with growth in RTDs and spirits, albeit at a slower rate because of the fall-off in seltzers.

Consumers, to your point, are seeking more value through purchasing decisions, which they're making, either into the larger pack sizes like 30 packs or into the smaller pack sizes singles and six packs. The on-premise is running pretty at pace with the off-premise business. And we haven't seen any material trade down into our economy brands. If it happens, we're ready. I mean, Miller High Life and Keystone, in particular, are well positioned and are showing very nice improvement, given where they were. So if it comes, we believe that the portfolio that we've got is ready for it. Thanks, Vivien.

Operator: We now have Rob Ottenstein of Evercore.

Robert Ottenstein
Analyst, Evercore ISI

Q

Great. Thank you very much. Just a few follow-ups on some of the points that have been mentioned. So Gavin, strong results. You're obviously super confident in the business and the momentum disconnect, right, in terms of what the stock is doing, I think you're trading at about a 10% free cash flow valuation.

So given that, and I know your general points on capital allocation. I guess the question is, is there any impediments or any issues in terms of buying back stock now as in – between now and the end of the year. So is there anything to stop you from doing that? So that's question number one. Question number two is just – you had mentioned that the business was better in October than in Q3. Is that global? Is that US, Canada and Europe? Or is it just a particular region? Thank you.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

Thanks, Rob. To your second question, I'll take that first. It is global. It's across the spectrum, not just the US. To your earlier question around why I believe and why we're confident that we're going to continue to deliver, I'm not going to rehash the points I made earlier about our share position having been stable for the last 25 weeks and the gains we've made being very sticky.

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But I would say to you that over the last four years, Robert, yeah, we made a lot – we made a number of statements when we launched our revitalization plan. We said, we would streamline our company and deliver $600 million savings, and we did that. We said we would grow the top and bottom line of our business. And by the end of this year, we will have done it two years in a row.

We said we would strengthen our core brands, and we've done exactly that. We said we would become more than just a beer company, and we have become more than a beer company. We also said we would grow more of our portfolio in above-premium, and we've done exactly that, not just in beyond beer, but also in beer with a brand like Madri. We certainly...

Robert Ottenstein
Analyst, Evercore ISI
Q

Sorry, Gavin, I don't mean to interrupt you. I mean, I know time's short. I wasn't challenging that. I was just saying, in the light of that, right, in the light of your progress, given where the stock is coming down here in the light of everything you're saying, which I'm not challenging. Is there any impediment? Is there anything to stop you from buying back stock between now and the end of the year? And again, sorry for interrupting.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.
A

I'm glad you agree with all my points, Robert, I had a few more I was going to make too.

Robert Ottenstein
Analyst, Evercore ISI
Q

I am not sure that...

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.
A

Look...

Robert Ottenstein
Analyst, Evercore ISI
Q

...there's no miscommunication.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.
A

As Tracey said, if we look at our capital allocation priorities, we're where we need to be. We have an approved buyback program. And Robert, as we are required to do, we will disclose any and all shares that we may buy in a quarter when we release our Q – I think, in February of next year.

Robert Ottenstein
Analyst, Evercore ISI
Q

Thank you.

Operator: We now have the next question from the line of Nadine Sarwat of Bernstein.

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Nadine Sarwat
Analyst, Bernstein Autonomous LLP

Q

Hi, morning everybody. Two questions from me. So first, with earnings clearly coming ahead of expectations today. You guys have taken up full year guidance, so that's clearly not just a timing issue, but could you perhaps give us a sense of how much of that stronger earnings are driven by temporary versus permanent factors, perhaps particularly thinking to any temporary benefit from positive operating leverage on the fixed cost base, given shipments exceeded depletions.

And then, secondly, circling back to the point of market share gains, sustainability, fully appreciate your comments on the latest scanner data and when the facts are there. I believe, ABI, though, quoted some survey data indicating a wiliness of some lost Bud Light drinkers to return to the brand. I'd be curious to hear if you have any survey data or additional consumer insights that you could share that adds to your conviction that those market share gains will continue to be sticky. Thank you.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

Thanks, Nadine. Do you want to talk about operating leverage...

Tracey I. Joubert
Chief Financial Officer, Molson Coors Beverage Co.

A

Yeah.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

...Trace, and I'll talk about the market share gains and the stickiness.

Tracey I. Joubert
Chief Financial Officer, Molson Coors Beverage Co.

A

Yeah. So, Nadine, in the prepared remarks, we spoke about the volume leverage benefiting us by about 80 basis points on the COGS per hectoliter increase, so yes, that's for Q3. Just in terms of operating leverage, our fixed cost comprise approximately 20% of our enterprise underlying COGS. Obviously, volume leverage helps us with those fixed costs over more of the volume. And so, as we saw in Q3, it does have a fairly significant impact – and also that does depend on – the year-over-year does depend on the markets. In some of our markets, the fixed cost may be slightly higher, so the 20% that I've given you is really on an enterprise basis.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

Thanks, Trace. Look, I can't really comment on Anheuser-Busch's polling data, Nadine. But what I can say to you is that sales are what matter, right? And the sales are continuing as they have done since early April. As I said, the share gains are unchanged in 4-week, in 13-week, and in 26 week. And in fact, in the latest four-week read the big brand is actually getting worse. So, that's the best indication of what's actually happening is, the share has come to us and it is sticking and has done now for seven months. And we've got a bunch of plans in place, which we showed our distributors, and we revealed a little bit of it at our Strategy Day, which highlights our intention to retain that share gain.

Operator: Thank you. We now have Eric Serotta of Morgan Stanley. Your line is open.

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Eric A. Serotta
Analyst, Morgan Stanley & Co. LLC

Q

Good morning. Thanks for the question. So, coming back to US brand volume, you called out the double-digit for Coors Light and Banquet and the high single-digit for Miller Lite. Your overall depletions were up kind of mid-single digits, which implies the rest of the portfolio was a lot lower. I realize a lot of those segments are not growing, but the premium lights are growing right now. But can you give some color as to how you're doing – I'd say, your performance in the rest of the portfolio, either by segment or call out a couple of brands and how that is tracking versus three, six months ago? Thanks.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

Yeah. Eric, that was tough to catch the total drift of your question. Let me try. Obviously, there is the trading day adjustment we talked about, there is the timing of holidays, and there is the timing of the price increases that come into that. We obviously do have some tail brands which impact us. We are seeing some of the same trends as everybody else is seeing from a seltzer point of view, in particular. And that's why we've taken a much more broader approach to flavor.

The total flavor segment, seltzers, FABs and RTDs, was about 5% of the category. That number has tripled to about 13% now. It's a $9 billion business. But there's no question that seltzers within the flavor category is declining fairly meaningfully. You've seen that with our brands, and you've seen that with our competitors' brand. The data that we've looked at from a hard seltzer's point of view, shows that it provided an entry point into flavor for consumers. And once they discovered flavor, they started to experiment and trade into FABs and RTDs and so on. And that's why we built a diversified portfolio of brands.

And from a performance point of view, we're very pleased with the performance in the flavor space. We're the number two share gainer for major brewers in F&Bs. We've got the number three and the number five hard seltzer in the category or admittedly a declining category. We've got the top innovation in flavor in 2021, 2022, in the summer of 2023. We've got Simply Spiked within that space, which is on fire. It's got nearly 5% of the FAB segment. And we're bringing new build and borrow brands to the space with the Peace Hard Tea and the launch of Happy Thursday.

From a premiumization point of view, Peroni doing well. Blue Moon is operating in a challenged segment, as you've seen from a craft point of view, it's still the number one brand in the craft segment. But we've experienced softness with Blue Moon largely due to those craft category challenges. We've got a really clear plan in place of how we're going to change that. We're already starting to see positive display trends. And we've got a big year planned for Blue Moon in 2024, which we unveiled for our distributors in September, and which they liked a lot, and that includes new innovation, which is coming, as I said, in December.

And then finally, in economy, yeah, it's a challenged segment, but we're the top dollar share gainer in the economy space that – we're pleased with the performance of our two big brands there, Miller High Life and Keystone. So that's a walk around the park for you, Eric.

Operator: Thank you. We have our final question from Chris Carey of Wells Fargo Securities.

Christopher Carey
Analyst, Wells Fargo Securities LLC

Q

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Hi, everyone. Thanks for the question. So one on the EMEA and APAC segment and then just a high-level question. The price mix tailwinds that we're seeing right now, how much of that is your premiumization within the business versus on-premise versus just straight list pricing? I'm trying to determine how much of this tailwind that we're seeing right now is perhaps sustainable, structural versus maybe just a cyclical recovery of the business. And then I was wondering if you could just comment on competitive activity as we get closer to spring and spring resets, are you seeing any notable shift in the market? Thanks so much.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

I'm sorry, what was the second question, Chris?

Tracey I. Joubert
Chief Financial Officer, Molson Coors Beverage Co.

A

Competitive activity, are we seeing anything?

Christopher Carey
Analyst, Wells Fargo Securities LLC

Q

Competitive activity, are you – sorry, yeah, I should have been more clear. Competitive activity for the total business, specifically in the US as we get closer to spring resets as competitors are jostling for space. So are you starting to see any changes? Obviously, you're stepping up marketing spending in Q4, I don't know if that's why, but just a broader comment on whether you're seeing any developments from a competitive activity, specifically in the US? And then the other question was on the pricing in EMEA and APAC and how much of this is sort of durable, because of premiumization and how much is perhaps just list pricing that all that will normalize and some cyclical recovery of your channel mix? So thanks so much.

Gavin D. K. Hattersley
President, Chief Executive Officer & Director, Molson Coors Beverage Co.

A

Thanks. Chris, look, it's a bit of everything there, right? So, I mean, obviously, we did get strong pricing in our EMEA/APAC business. Obviously, it varies by country and is driven largely by whatever the inflation environment is in those countries.

But from a mix point of view, we're getting strong benefits from particularly, the continued very strong growth in Madri, which is an above-premium brand and as – I can't remember it was me or Tracey that said that, but it's up 50% in the quarter, and it is continuing to grow strongly. It's one of the primary reasons why we are the number two brewer in London, which was somewhat unthinkable a few years ago.

So a large part of the overall UK business is now in the above-premium space, and it is accelerating. So, that's part of it. Hard to tell where pricing is going to land out in EMEA/APAC and it does vary by country. And it is driven largely by the local dynamics. I do think it's safe to say that it's not going to be at the historical levels that we've experienced over the last few years.

From a US point of view, from a price realization point of view, we put price into the markets that we were expecting to put it into in the fall. And as we've said before, I would expect pricing to fall back to more historical levels in the new year, the ones that go in spring. And from a shelf reset point of view, yeah, I guess everybody is fighting for space. The beauty of our position at the moment is that we've got the facts and data to support meaningful increases in space for our brands. And the retailers that have gone in fall have given us tens of

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thousands of extra cubic feet of space. And we're going to fight for every square foot of space based on those trends as we head into the spring reset. So thanks, Chris.

Operator: Thank you. I would like to turn it back to Greg Tierney for any final remarks.

Greg Tierney

Vice President of FP&A and Investor Relations, Molson Coors Beverage Co.

Yeah. Very good. Thank you, operator, and I appreciate everyone joining us today. I know there may be additional questions we weren't able to answer, so please follow-up with our Investor Relations team, and we look forward to talking with many of you as the year progresses.

So, with that, thanks, everybody, for participating, and we'll talk soon. Cheers.

Operator: I can confirm that does conclude today's call. Thank you all for joining. Please have lovely rest of your day and you may now disconnect your lines.

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