

# BOSTON BEER COMPANY

MIRANDA ROST & JACK MURPHY

AUSTIN PREECE, JACOB MAURER, & KIANA CANNON



**Ticker: SAM**  
**Sector: Consumer Staples**  
**Industry: Alcoholic Beverages**

**Stock Exchange: NYSE**  
**Current Price: \$373.12**  
**Valuation Date: December 2, 2019**

## INTRODUCTION

The Boston Beer Company, which operates in the alcoholic beverages industry, was founded in 1984 after Jim Koch brewed his great-great grandfather's recipe for lager in his kitchen and experimented with the flavors and ingredients. His first brew that he sold by walking bar-to-bar, which he named Samuel Adams Boston Lager after one of nation's founding fathers, started a revolutionary change in the American beer industry. Samuel Adams Boston Lager quickly became "The Best Beer in America". Over the years, Jim Koch continued to impress beer drinkers everywhere and continued to innovate to stay ahead of the competition. This included expanding into growing areas such as flavored malted beers, hard seltzers, kombucha, and more.

As of latest filing, Boston Beer Company has revenues of just under one billion with a market cap of \$4.5 billion. The company has been able to grow to this size due to the determination and creativity of the founder, Jim Koch, as well as the innovation-friendly culture that has been created under him.

## RECOMMENDATION

We recommend a **BUY** for Boston Beer Company with a target price of \$426.64, which is an upside of 14.34% from the Monday, December 2, 2019 price of \$373.12. With a sensitivity analysis, our potential upside is between 12.81% and 15.93%. The following reasons support our buy recommendation:

- Rapid growth in the hard seltzer segment, which Boston Beer Company has a strong #2 position in
- Emerging flavors that have been scientifically tested to meet consumer preferences, specifically within the hard seltzer segment
- Expanding market with new demographics due to acquisition of Dogfish Head and partnership with NHL
- Brewing the American Dream program that they developed, which helps to promote entrepreneurs in the food and beverage industry by lending money and offering business advice

- One of largest salesforces in the beer industry and a ‘Freshest Beer Program’ that helps to greatly strengthen relationships with their approximately 275 wholesalers
- Overlooked brands like Samuel Adams, 26.2 Brew, Tura, and Wild Leaf, which have great protentional due to current trends of premiumization and healthy lifestyles

## INVESTMENT THESIS

The main drivers for Boston Beer Company are growth in hard seltzers, brand building, their distribution network, and their overlooked brands.

## GROWTH IN HARD SELTZERS

Hard seltzer is by far the fastest growing segment of the alcohol consumption market. The hard seltzer segment is a \$500 million industry; this year it has grown over 200%. By 2021, hard seltzers are estimated to be a \$2.5 billion dollar industry. Hard seltzers are taking over the market because they are perceived to be healthier: fewer calories, fewer carbs, and gluten free. They are not too sweet and their alcohol by volume is relatively low. This market is relatively new, so there will be a lot of innovation over the next few years, and Boston Beer is well positioned to take the lead in this segment of the industry.

## BRAND BUILDING

This past year, Boston Beer Company’s brand, Truly, signed a partnership with the NHL, making them the official hard seltzer of the NHL. The partnership with the NHL will help to reach a different group of people from the typical “hard seltzer drinker.” Another stride made with Truly was the advertising campaign using comedian, Keegan Michael Key (from Key and Peele).

Boston Beer Company is big in helping their community. Ten years ago, they introduced the Brewing the American Dream. This project is a way to help entrepreneurs that are in the food and beverage industry by loaning them money as well as business coaching and access to other resources. Another part of their brand is their constant innovation; they have changed up their cans to benefit the consumer in the best way possible.

## DISTRIBUTION NETWORK

The Freshest Beer Program was created by the founder of Boston Beer Company, Jim Koch, as a way to reduce time and inventories at the plants. By better forecasting and planning they are able to send orders to the distributors in a timelier manner and limit the amount of beer that goes bad. Boston Beer takes back stale beer from their distributors to make sure they have the best tasting beer they can. Of their 375 wholesalers, currently over 75% of them take part in the Freshest Beer Program.

This program along with their salesforce of around 410 employees – which is one of the largest in the beer industry – helps to strengthen these key relationships with wholesalers. This is important considering many states have a three-tier system in place, which requires that the manufactures like Boston Beer Company sell to wholesalers rather than directly to retailers. Because of this, wholesalers can have a huge impact on product that is pushed to consumers through retailers.

## OVERLOOKED BRANDS

Boston Beer Company has many valuable brands. However, many of them have been overlooked due to the hype surrounding the hard seltzer segment. Four key brands of Boston Beer Company that have been overlooked are Samuel Adams, 26.2 Brew, Tura, and Wild Leaf – all of which have large growth potential due to current trends of consumers including premiumization and wanting to live a healthier lifestyle.

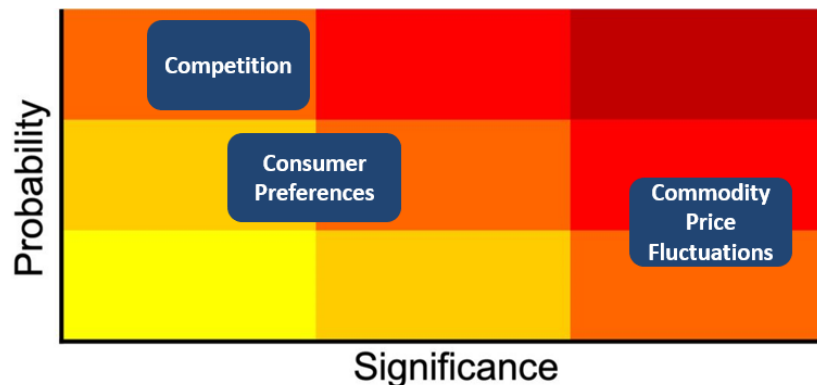
Samuel Adams has seen negative sales growth recently. However, the company has decided that they are going to take time and improve this brand for long-term success. They plan to do so while they have the cash flow that is being generated from their Truly brand. Rather than rush an improved Samuel Adams to market, they want to make sure they get it right the first time with their strong, premium brand that tells a great story – something consumers want to pay for.

26.2 Brew, which is brewed by the Marathon Brewing Company under Boston Beer Company, is another overlooked brand that has potential to become a premium brand due to its story and history. 26.2 Brew is the official beer of the Boston Marathon and was created by Shelley Smith, a triathlete and marathon runner, who wanted to help runners celebrate their hard work with a healthier – but still tasty – beer.

Tura, which is an organic alcoholic Kombucha, and Wild Leaf, which is a craft hard tea, are two of Boston Beer Company's brands which have extremely large growth potential due to the jump in demand for a healthy lifestyle and products that meet that lifestyle. These brands, which are low calorie and low sugar, are options for consumers who are focused on their health, but still want to enjoy a social gathering whether it be at a bar or at their homes. 59% of respondents in a survey actually listed their health as a reason that they quit drinking beer. Boston Beer Company understands this trend and is trying to give alternatives to their consumers, which will help them to retain more in the future.

## RISKS

Boston Beer Company, like any other company, faces competition. However, how they have been able to differentiate themselves within fast growing categories and how they have been able to be adaptive to consumer trends has allowed them to secure a competitive advantage in the alcoholic beverages industry minimizing the significance of this risk.



The company also has to keep up with changing consumer preferences. If they don't continue to do so, that could pose a risk to their bottom line. Whether a person chooses wine or spirits, or if a person prefers craft beer over light beer, it has an impact on Boston Beer Company and their position in the market.

A major risk for Boston Beer Company is the fluctuation in commodity prices considering malt (barley), hops, and apples make of large amount of the ingredients needed for their products. To mitigate this risk, Boston Beer Company has entered into contracts with suppliers and even bought an apple orchard in New York. They are sufficiently hedged against this risk, but it is still possible that demand could outpace what the contracted suppliers can offer.

## MANAGEMENT

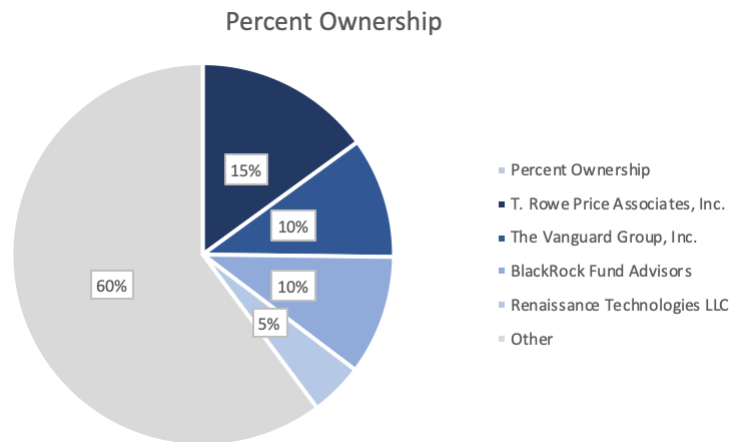
Boston Beer Company has 16 members on their management team: 10 are a part of the management group, while 7 members are on the board. The President and CEO, David Burwick is a part of both groups. Burwick has been a board member for 14 years, and, just this past year, he was named President and CEO as long time CEO Martin Roper stepped down in 2017. Before coming to Boston Beer Company, Burwick was President and CEO of Peet's Coffee and Tea, Inc. and CMO for Pepsi-Cola. In the chart below, you can see the average age, average tenure, number of women directors, as well as some additional information about the board and management.

	Board	Management
Number of Directors	7	10
Women Directors	2	3
Average Age	56	55
Age Range	34 - 69	45 - 61
Average Tenure (Years)	11	11
Number of Directors > 5 Years	4	6
Number of Directors > 10 Years	3	5

Jim Koch, who is the chairman for Boston Beer Company, founded the company in 1984 when he quit his consulting job and started brewing beer in his kitchen with his family's recipe. Because of his revolutionary actions in the beer industry specifically with Samuel Adams, Boston Beer Company's historical brand, he is known as the founding father of the American craft brewery movement. In addition to being the chairman of Boston Beer Company, he is also on the board of the Brewers Association of America, which he and Sam Calagione, formed together. Sam is the President and founder of Dogfish Head Craft Brewery, Inc., which Boston Beer Company acquired on July 3<sup>rd</sup> of this year. In addition to the Brewers Association, Koch and Calagione are also known for defining craft beer, creating the craft brewer seal, and creating the SAVOR food and beer event.

## OWNERSHIP OF SHARES

Total Shares Held: 9.19 Million	
Institutional Holdings	65.3%
Insider Holdings	8.8%
Unknown Holdings	25.9%



## VALUATION

To determine our target price, we did a combination of two methods – a discounted cash flow and a multiples method. Below is a brief explanation of how we used each.

### DISCOUNTED CASH FLOW

For the WACC for our DCF, we used 8.0%, which may seem conservative when comparing it to Boston Beer Company's WACC on Bloomberg of 6.2%. However, historically Boston Beer Company has a much higher WACC than this, sometimes reaching almost 11%. Therefore, it seems like a reasonable assumption to make that their WACC will increase in the future. For our perpetual growth rate, we used 2.5%. Then, we adjusted Boston Beer Company's cash flows based on four assumptions: growth in hard seltzer for Boston Beer Company due to new flavors/innovations, growth related to the NHL partnership, growth due to stronger relationships within their distribution network, and growth from overlooked brands for each of the next five years. For the first two years, we added this to the average growth rate expected by analyst for Boston Beer Company, which is 22.25%. Then, for the following three years, we cut this average in half since we believe most of these estimates are based on the rapid growth in hard seltzer, which we expect to level off once we near 2021, and added it the growth from our assumptions to get cash flows through 2023 for our DCF. This gives us a target price of \$427.73.

For our DCF, we also performed a sensitivity analysis by changing the WACC and perpetual growth rate of the company to first 8.5% and 2.0% and then to 7.5% and 3.0%, which gave us a target price range of \$418.19 and \$437.57.

### MULTIPLES METHOD

For our multiples method, we looked at the historical premium of Boston Beer Company for their Price/Book compared to the industry. From this, we noticed they normally trade at a 42% premium, but currently are only trading at a 25% premium making them undervalued. Their current Price/ Book is 5.97. The industry average of just alcoholic beverage companies is 2.29, but the current and historical premiums, which we found on Bloomberg, relate to the mean of the industry that includes both alcoholic and nonalcoholic companies. This mean is 4.8, which is what we used to calculate our multiples method. Considering their historical premium of 42%, Boston Beer Company should be trading at a multiple of 6.8. Using this and their current book value of \$62.50 per share, we get a target price of \$425.00 per share.

## WEIGHTING

We decided to weight our DCF model at 60% and our multiple method at 40% since the DCF provides a more in-depth analysis of Boston Beer Company and the assumptions we made about areas of growth within the company that we think the market is overlooking. We did this weighting with our initial target price from the DCF as well as the two from the sensitivity analysis to get a target price of \$426.64 and a range of \$420.92 to \$432.54, which is a potential upside of 14.34% with a range of 12.81% to 15.93%.

## PEER ANALYSIS

Company	Gross Margin (%)	ROA (%)	ROE (%)	Price/ Book
Boston Beer Company (SAM)	51.45	15.32	20.97	5.97
Anheuser Busch InBev NV (BUD)	60.25	1.81	6.37	2
Molson Coors Brewing Company (TAP)	37.8	3.7	8.35	.9
Constellation Brands (STZ)	50.55	13.81	33.36	2.55
Industry Average	46.38	9.32	20.47	2.29

Boston Beer Company has one category of revenue which is alcoholic beverages. The largest two players in alcoholic beverage company are Anheuser Busch InBev NV and Molson Coors Brewing Company. Boston Beer Company outperforms the industry in many financial metrics, especially with returns on assets, equity, and invested capital.