



National Beverage Corp.
SELL: US\$64.86 (-21.4%)

Fizzing Out

16 October 2020



Company Overview

Figure 1. National Beverage Corp. Revenue and EBIT Margin Profile

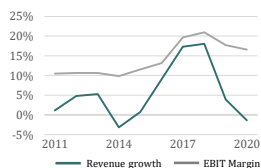
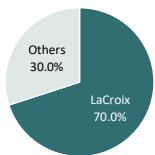


Figure 2. Revenue Distribution by Product



National Beverage Corp. ("National Beverage" or the "Company") is an American beverage developer, manufacturer and distributor with revenues concentrated in US and Canada. As the fifth largest soft drink company in the US, its product lines include the "Power+ Brands" of healthy drinks, and carbonated soft drinks. The company's most popular product line LaCroix, holds approximately 33% market share in the flavored bottled water market in the US, which gained widespread prominence beginning in 2016.

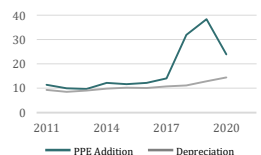
(US\$m)	2019A	2020A	2021E	2022E
Revenue	1,014.1	1,000.4	1,088.8	1,183.5
Rev Gr Rate (%)	3.9	(1.4)	8.8	8.7
EBIT	179.9	165.7	193.9	189.4
EBIT Gr Rate (%)	(11.9)	(7.9)	17.0	(2.3)
EBIT Margin (%)	17.7	16.6	17.8	16.0
ROA (%)	31.1	20.0	20.9	20.4
ROE (%)	42.5	28.7	29.2	28.5
EPS	2.94	2.71	3.19	3.11
D/E	0.2	0.1	0.1	0.1

Investment Thesis

Figure 5. 2019 Dollar Sales Growth

bubly	216.3%
Topo Chico	37.3%
Sparkling ICE	19.3%
Polar	17.3%
Perrier	4.7%
LaCroix	-3.1%
LaCroix Curate	-13.5%

Figure 6. PPE Schedule



Sources: Company Filings, Forbes, Statista, NUS Investment Society Estimates and Research

- Continued Decline in Market Share** – Momentum from extremely strong growth in sales by competitors such as bubly and Topo Chico will allow rivals to continue capturing market share from Lacroix. National Beverage's unorthodox influencer marketing strategy will continue to be dwarfed by the marketing reach of rivals, compounded by the company's inability to carry growth momentum from Q1 2021.
- Deteriorating Margins** – High net capital expenditures in FY2017-20 have failed to translate into higher gross margins, which have declined instead with consistent increases in cost per case attributed to changes in product mix and increased aluminium costs. National Beverage also persists in employing a less cost-efficient distribution strategy, and combined, these factors will exacerbate the decline in future margins.
- Poor Corporate Governance** – National Beverage currently has a record high cash holding of US\$353m on its balance sheet. However, the lack of opportunities to create value discounts this cash holding. This is attributed to inconsistent capital return policies, historically poor capital employment, and difficulty in penetrating markets beyond US and Canada should the company pursue market development.

12M Industry Outlook

Figure 3. Unit Sales Growth (%) for Non-alcoholic Beverages in 2018

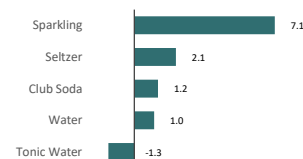
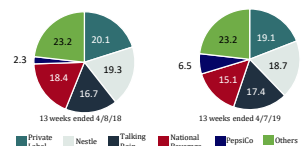


Figure 4. Market Share (%) of Brands by Retail Dollars



- Strong long-term growth:** The sparkling water industry grew an estimated 118% from 2013 to 2018 and is projected to grow at 10.6% CAGR through to 2023. This growth can be attributed to rising health consciousness, leading to increased demand for healthier alternatives to traditional carbonated soft drinks such as Coca Cola and Pepsi.
- Increasing competition:** LaCroix's success has attracted industry incumbents, including Coca-Cola and PepsiCo into the sparkling water market, with Coca-Cola acquiring Mexican mineral water start-up "Topo Chico" in 2017 and Pepsi launching "bubly" in 2018. Such developments have increased competition and fragmented the market for sparkling water. This has resulted in declining market share for LaCroix in 2019 and 2020, which is expected to persist in the medium-term.
- Risk:** Strong industry growth in the future may mitigate the loss of market share to competitors, and result in strong sales growth for National Beverage and LaCroix. LaCroix also has a certain degree of brand loyalty which may stem future losses in market share, seen from Q1 2021 results where revenue growth was 11.0% q-o-q with the introduction of new flavours.

Valuations

Perpetual Growth Method (US\$m except per share amounts)	
Perpetual growth rate	0.7%
Terminal Value	3,078.0
PV of Terminal Value	1,714.6
PV of FCFE	1,016.6
Enterprise Value	2,731.2
Implied Equity Value & Share Price	
Enterprise Value	2,731.2
Less: Total Debt	(46.0)
Plus: Cash & Cash Equivalents	352.5
Less: Value of options	13.3
Value of Equity in common stock	3,024.4
Shares Outstanding	46.6
Implied Share Price (US\$)	64.9
Current Share Price (US\$)	82.5

Revenues: National Beverage will enjoy y-o-y revenue growth of 8.83% for FY2021, reflecting revenue growth momentum from the new flavours. Revenues will then grow below the industry forecasted growth rate of 10%, reflecting the company's declining market share. Revenue growth will gradually decline towards the perpetual growth rate of 0.73%.

Operating Margins: Operating margins will remain at 16%, in-line with global beverage producers' average operating margins of 16%, and reflecting National Beverage's non-effective PPE.

Reinvestment: With depreciation expense forecasted to grow at 10% annually, National Beverage will increase capital expenditure by 8% annually, in line with management's commitment to reduce capital expenditure due to excess capacity

WACC: 6.14%; Risk-free rate 0.73%, Unlevered beta 1.09, Equity risk premium 4.97%, Pre-tax cost of debt 1.99%, Market debt-to-equity ratio 0.012.

Valuation and Recommendation: A target price of US\$64.86 is obtained, representing a 21.4% downside.

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