

Virginia Spirits Board Funding Proposal

Final Version for Vote - December 7th, 2020

This memo outlines the proposed funding the newly created Virginia Spirits Board (the 'Board' or 'VSB').

Summary

An industry assessment of five cents to one dollar (\$0.05 - \$1.00) based on the retail price per liter of Virginia spirits sold, to be collected via Virginia ABC in a mechanism that pulls from supplier FOB.

Per Liter			Per 750ml			Per 375ml		
Retail Price		Assessment	Retail Price		Assessment	Retail Price		Assessment
<	\$19.99	\$ 0.05	<	\$14.99	\$ 0.038	<	\$7.50	\$ 0.019
\$20.00 -	\$29.99	\$ 0.15	\$15.00 -	\$22.49	\$ 0.113	\$7.50 -	\$11.25	\$ 0.056
\$30.00 -	\$39.99	\$ 0.25	\$22.50 -	\$29.99	\$ 0.188	\$11.25 -	\$15.00	\$ 0.094
\$40.00 -	\$49.99	\$ 0.35	\$30.00 -	\$37.49	\$ 0.263	\$15.00 -	\$18.75	\$ 0.131
\$50.00 -	\$59.99	\$ 0.45	\$37.50 -	\$44.99	\$ 0.338	\$18.75 -	\$22.50	\$ 0.169
\$60.00 -	\$69.99	\$ 0.55	\$45.00 -	\$52.49	\$ 0.413	\$22.50 -	\$26.25	\$ 0.206
\$70.00 -	\$79.99	\$ 0.65	\$52.50 -	\$59.99	\$ 0.488	\$26.25 -	\$30.00	\$ 0.244
\$80.00 -	\$89.99	\$ 0.75	\$60.00 -	\$67.49	\$ 0.563	\$30.00 -	\$33.75	\$ 0.281
\$90.00 -	\$99.99	\$ 0.85	\$67.50 -	\$74.99	\$ 0.638	\$33.75 -	\$37.50	\$ 0.319
\$100.00 +		\$ 1.00	\$75.00 +		\$ 0.750	\$37.50 +		\$ 0.375

This approach would mean that suppliers would have the option to: (i) adjust their FOB prices to have consumers pay for the assessment or (ii) maintain FOB prices so that the supplier pays the assessment.

The assessment amount will not be subject to any incremental markup or excise tax in formulating the retail price.

Retail Price Group	Tax per Liter	Total Liters	Total Dollars
<\$20.00	\$ 0.05	2,982	\$149
\$20.00-\$29.99	\$ 0.15	102,611	\$15,392
\$30.00-\$39.99	\$ 0.25	171,604	\$42,901
\$40.00-\$49.99	\$ 0.35	43,091	\$15,082
\$50.00-\$59.99	\$ 0.45	63,664	\$28,649
\$60.00-\$69.99	\$ 0.55	46,778	\$25,728
\$70.00-\$79.99	\$ 0.65	20,235	\$13,153
\$80.00-\$89.99	\$ 0.75	2,549	\$1,912
\$90.00-\$99.99	\$ 0.85	4,303	\$3,658
\$100.00+	\$ 1.00	18,150	\$18,150
Total		475,967	\$164,772

Based on data provided by Virginia ABC.

Against current liter volumes of Virginia spirits sold across government stores, to licensees, and via distillery stores, the proposed assessment would generate **\$165K** in total funding.

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Industry Analysis

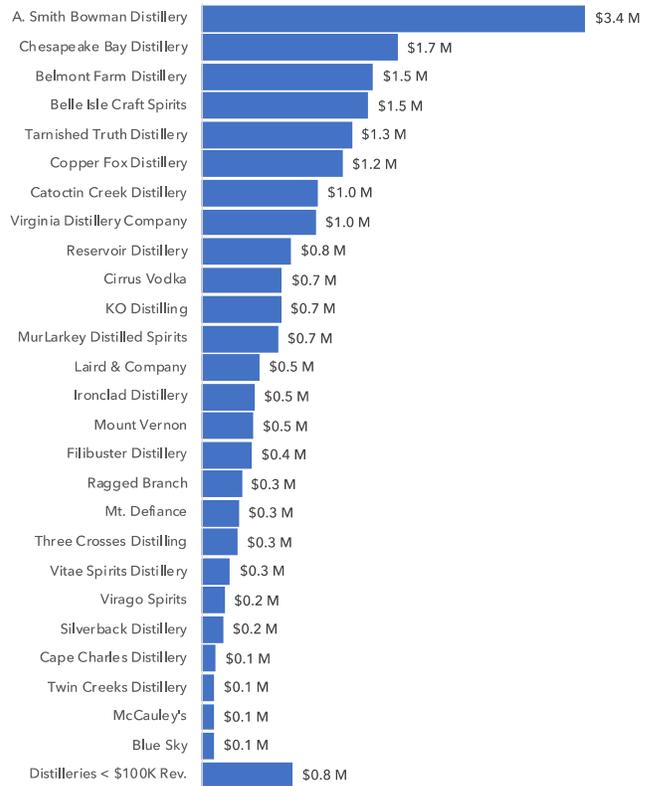
The chart at right outlines retail revenue by distillery through ABC stores, licensees, and distillery stores. Note this data is from VDA so is missing some distillery store sales.

There are a total of 51 manufacturers selling Virginia-made products in the Commonwealth. A Smith Bowman is the largest group, representing 17% of the industry, combined with the next five largest groups represents over 50% of the industry. There are 25 distilleries with revenue under \$100K that combined represent 4% of total retail revenue.

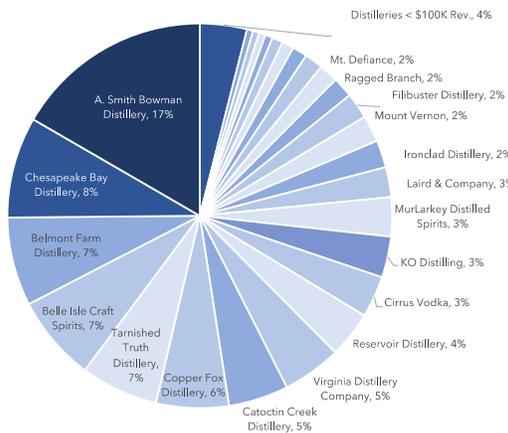
The charts below outline the distribution of retail revenue across all producers compared to the proposed assessment distribution. In nearly every case, retail revenue aligns with the proposed assessment structure. Small deviations exist with a handful of manufacturers who have either: (i) products priced on the low end within a given price tier; and (ii) products that skew towards the higher price tiers.

In summary, the assessment is distributed in a fair manner across industry constituents.

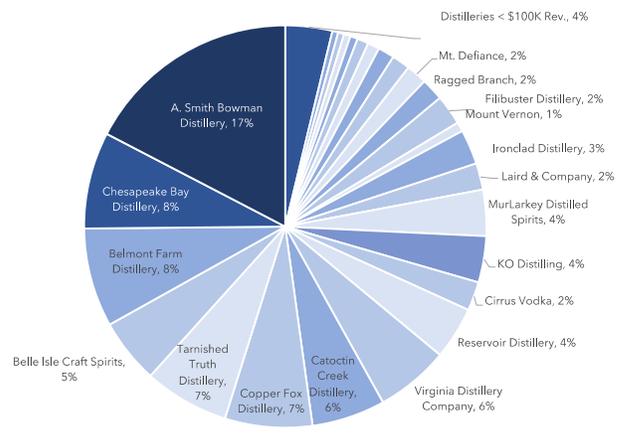
ABC Retail Revenue by Distillery, TTM



ABC Retail Revenue by Distillery, TTM



Proposed Assessment by Distillery, Estimated



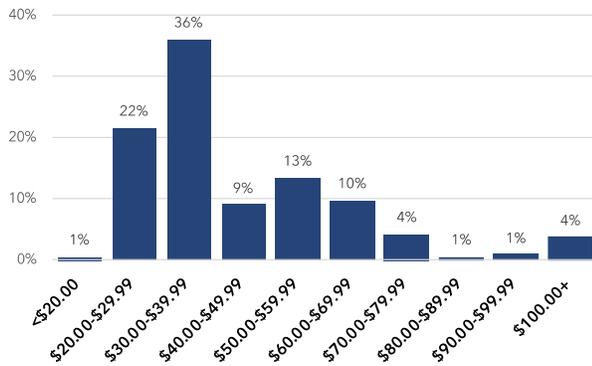
The charts below outline the distribution of retail revenue and the distribution of the proposed assessment across the different price categories. Note that while more than one third of retail revenue comes from products in the \$30.00 -

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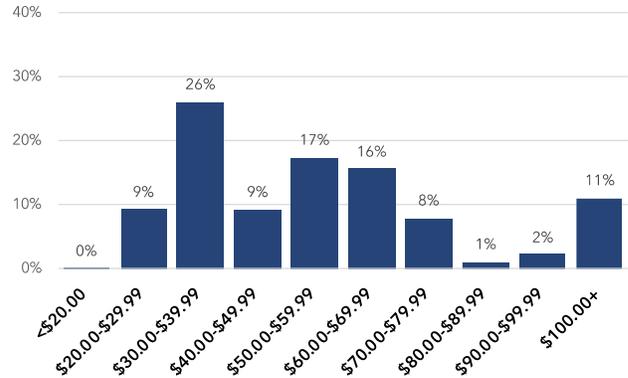
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\$39.99 price tier, the contribution of the proposed assessment from that category is nearly one quarter of the total assessment, reflecting the higher assessment in the higher tier products.

ABC Retail Revenue by Price Category, TTM



Proposed Assessment by Price Category, TTM



Return on Investment Analysis

The VSB needs to demonstrate a positive return on investment (ROI) for the industry. The analysis at right outlines the minimum growth hurdle necessary to provide a positive ROI.

Total incremental gross profit to distillers needs to be higher than the assessment volume. Applying a gross profit margin of 40.0% means that FOB (supplier revenue) needs to increase by \$412K. With an average total retail markup of 48%, retail revenue needs to increase by \$858K. Based on TTM retail revenue for the industry of \$20.3M, the VSB will need to demonstrate 4.2% or more growth through its activities. That growth will result in a net neutral ROI.

ROI Analysis - Minimum

Total Assessment	\$164,772
Gross Profit Growth Hurdle	\$164,772
Est. Profit Margin / FOB	40.0%
FOB Growth Hurdle	\$411,931
Est. Retail Margin / FOB	48.0%
Retail Growth Hurdle	\$858,189
Retail Revenue - TTM	\$20,330,336
Retail Growth % Hurdle	4.2%

ROI Analysis - Goal

Retail Growth % Goal	10.0%
Retail Growth Goal	\$2,033,034
Est. Retail Margin / FOB	48.0%
FOB Growth Goal	\$975,856
Est. Profit Margin / FOB	40.0%
Gross Profit Growth Goal	\$390,342
Assessment Investment	\$164,772
Growth Profit Growth	\$390,342
Investment Return \$	\$225,570
Investment Return %	36.9%

The VSB will be prepared to exceed the retail growth hurdle with staged, industry-wide initiatives including all Virginia distilleries through programming to activate direct and indirect sales of Virginia Spirits. Examples include an e-commerce portal for DTC sales on industry website, retail partnerships with ABC, broader distribution of the Virginia Spirits Trail, formal brand / marketing / and public relations plans, and much more.

A minimum retail revenue growth rate of 10.0% will be implemented for all VSB initiatives. Per the chart at left, achieving that growth provides an ROI of 36.9%.